Recent Developments Affecting Estate Planning

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I. The Federal Estate Tax—*What* Federal Estate Tax?

A. **Estate tax exemption increased to $11.18 million—for now.** In reviewing my outline from last year's program (December 15, 2017), I noted that the House had passed the Tax Cuts and Jobs Act of 2017, but the Senate had not—yet—enacted the bill. Well—the Senate did pass the TCJA, which was signed by President Trump on December 22, 2017. TCJA doubled the estate, gift and generation-skipping transfer tax exemption, by increasing the exemption from its $5 million base to $10 million in 2018—actually, $11.18 million resulting from CPI adjustments. Effectively, this means $22.36 million in exemptions for spouses.

1. **Preparing and filing estate tax returns is (almost) no longer a part of the practice.** A federal estate tax return is not required to be filed unless the value of the decedent's gross estate plus "adjusted taxable gifts" (taxable gifts over annual exclusions) exceeds $11.18 million—unless a return is filed in order to make the deceased spouse's unused exemption (DSUE) portability election.

2. **Higher exemption will sunset at the end of 2025.** Under the TCJA, the higher exemption will continue through 2025. Effective January 1, 2026, the exemption will revert to the former base level of $5 million per person unless Congress extends the higher exemption. This means that we know what the estate, gift and GST exemption will be for the next eight years—unless a Democrat Congress reduces the exemption in the meantime. (Recall that in 2016, the Obama Administration proposed reducing the exemption from $5 million to $3.5 million.)

   a. **"It's déjà vu all over again"** said the noted philosopher, Yogi Berra (albeit in a different context). The one constant with respect to transfer taxes has been constant change. It all began with the Tax Reform Act of 1976, which "unified" the federal estate tax and gift taxes, increased the estate tax exemption from $60,000 to $175,625, introduced the first (mercifully short-lived) version of the generation-skipping transfer tax, repealed (for a few years) the "new basis at death" rule, and made other significant changes (and some insignificant changes—remember the orphan's deduction?). ERTA 1981 increased the estate tax exemption to $600,000 (phased in gradually), introduced the unlimited marital deduction, and gave us QTIP trusts. The Tax Reform Act of 1986 gave us the current generation-skipping transfer tax. In 1990, we were introduced to the Special Valuation Rules of Chapter 14. EGTRRA 2001 increased the exemption in spurts ($1,000,000 in 2002 to $3,500,000 in 2009). After an estate-tax-free year in 2010, in 2012 Congress made the exemption "permanent" at $5,000,000 (with annual CPI adjustments).

      1) And now we have an estate tax exemption that will sunset on January 1, 2026. As Yogi Berra also said, "It ain't over 'til it's over."

   b. **"Yes, but every past change in the exemption has resulted in an *increase* in the deduction!"** Bon't put any money on this history being an accurate guide as to where the road will be taking us. Yogi Berra put it well: "When you come to a fork in the road, take it."

3. **Congress did not merely double the exemption; it generated a *SEISMIC SHIFT IN THE ESTATE PLANNING PRACTICE!*** The Tax Reform Act of 1976 ***tripled*** the estate and gift tax exemption, from $60,000 to $176,525. In response to the specific provisions in the 1976 Act, new estate planning tools and techniques of course were developed—but tripling the exemption did not result in fundamental changes in the estate practice. For many clients, deferral of the estate tax (if not partial or total elimination of the tax) remained a factor in estate

planning decisions. The same was true of the 1981 Tax Act, which also ***tripled*** the exemption (to $600,000), and EGTRRA 2001, which ***quintupled*** the exemption (from $675,000 in 2001 to (after spurts) $3,500,000 in 2009. After each of those Acts, many clients continued to have reason to be concerned about the estate tax (and the gift tax, and the generation-skipping transfer tax).

a. **Estate planning concern in all of those earlier years: eliminate (or at least reduce) the estate tax**. Throughout all of those years, with estate tax rates as high as 50 or 55 percent, for many clients a planning objective was to reduce if not wholly eliminate estate taxes on the death of the client and his or her spouse. This could be accomplished through the use of not just marital deduction formula clauses and bypass trusts, but some rather sophisticated planning techniques, including discount planning, all designed to reduce the value of the client's and the surviving spouse's gross estate for estate tax purposes.

b. **Under the new law, the vast majority of our clients have NO concern about the estate tax!** After Congress increased the exemption to $5 million in 2011, in CLE speeches I sometimes referred to "mere millionaires" who no longer had estate tax concerns—individuals with estates of $3 million to $5 million, or couples with estates of $8 million to $10 million. For the foreseeable future—or at least the immediate future, the class of "mere millionaires" includes individuals with estates of "only" $8 million to $10 million, or couples with a "mere" $15 million to $20 million of accumulated wealth.

c. **An inclusion in the decedent's gross estate used to be a matter of concern ... but now a gross estate inclusion is our *friend***. To the extent that taxes affect estate planning decisions, the concern will be securing, for the client's beneficiaries, ***the benefits of the "new basis at death" rule***. For this reason, instead of taking steps to *avoid* a gross estate inclusion, many planning decisions will involve efforts to *include* the value of interests in the decedent's gross estate.

d. **Discount planning has been turned on its head**. Planning techniques that reduced value by way of discounts—fractional interest, minority interest, restrictions on transferability, lack of marketability, etc.—no longer project benefits but are a matter of concern because of the potential *harm* they may cause with respect to the "new basis at death" rule. In more than a few cases, the concern now is to find ways to unwind these transactions so as to avoid valuation reductions.

4. **"But I have all of those sophisticated estate planning tools that I won't be using anymore! And I spend so much time learning all of those things! Should I consider shifting my practice to another area?"**

Au contraire! These "mere millionaire" clients are still going to need wills (with those wills invariably containing at least some trust provisions), and will continue to have concerns about retirement planning, planning for disability and incapacity, creditor protection, second spouse protection, business succession planning, planning for descendants with disabilities, planning for clients who own real property in another state—and that's just a partial list.

a. January 2017 article from The Onion ("America's Finest News Source"): "GENEVA, SWITZERLAND—World Health Organization officials expressed disappointment Monday at the group's finding that, despite the enormous efforts of doctors, rescue workers and other medical professionals worldwide, the global death rate remains constant at 100 percent."

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