ALERT

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Nine Estate Planning Tips to Prepare for 2019

There have been a number of significant estate planning developments in 2018 which will help clients prepare for 2019.

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TAKEAWAYS

- *The historically high increased exemption amounts for gift, estate and generation-skipping transfer taxes is scheduled to increase to $11.4 million on January 1, 2019.*
- *The IRS proposed rules that will allow taxpayers to take advantage of the historically high exemption amounts for gift, estate and generation-skipping transfer taxes with respect to transfers made on or before December 31, 2025, even if the exemption amounts are subsequently reduced.*
- *Estate plans that have not yet been reviewed since the Tax Cuts and Jobs Act of 2017 was enacted should be reviewed to determine if there are new planning opportunities of which they can take advantage.*

The Tax Cuts and Jobs Act (the Act), which was signed into law on December 22, 2017, continues to provide extraordinary opportunities for our estate planning clients. However, some of the opportunities are temporary. As 2018 comes to an end, clients should consider the following nine things as they wrap up 2018 and begin their planning for 2019.

1. Take Advantage of the Temporary Increases in Exemptions from Gift and Estate Taxes.

Currently, gratuitous transfers of property, whether by lifetime gift or upon death, in excess of the unified gift and estate tax exemption (the "lifetime exemption") and which are not otherwise exempt from transfer tax are taxed at a federal rate of 40 percent. The Act doubled the lifetime exclusion amount to $10 million, as adjusted for inflation. Beginning January 1, 2019, the already significant $11.18 million lifetime exemption will increase to $11.4 million due to the inflation adjustment. This increase permits individuals who have already used their $11.18 million lifetime exemption to pass on an additional $220,000 in 2019 without incurring a federal gift tax. Individuals who used their lifetime exemption prior to the Act should consider making additional gifts. With proper planning, married couples will be able to transfer up to $22,800,000 of property without incurring a transfer tax.

Clients should consult their advisors regarding which assets to transfer in order to optimize the benefits of any lifetime gifts. For example, it is generally advisable to make gifts of assets with a high tax basis and retain assets that have significantly appreciated. Retaining appreciated assets until death will result in those assets being included in the client's taxable estate and receiving a step-up in income tax basis. That step-up, in turn, may reduce the income tax that will be due if the assets are sold.

Although the lifetime exclusion is scheduled to increase to increase for inflation through 2025 under the Act, the

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increase is temporary. Prior to the Act, the lifetime exemption was $5 million, indexed for inflation. Unless new laws are passed, the doubled exemption amount will terminate and the lifetime exemption will revert to the prior $5 million level (adjusted for inflation) on January 1, 2026.

On November 23, 2018, the Internal Revenue Service published proposed regulations which clarify that there will be no "clawback" of gifts made by taxpayers on or before December 31, 2025, regardless of whether the lifetime exemption amount is subsequently decreased. Although the regulations have not yet been finalized, there is a temporary opportunity to transfer significant wealth to future generations without paying Federal estate or gift taxes.

2. Take Advantage of the Temporary Increase in Exemptions from Generation-Skipping Transfer Taxes.

Like the lifetime exemption, the generation-skipping transfer tax (GSTT) exemption amount affecting transfers to grandchildren and more remote generations will increase to $11.4 million per individual or $22.8 million per married couple. However, this opportunity is also scheduled to sunset to pre-2018 levels in 2026.

The Act does not impose any limitation on the duration of a generation-skipping transfer to a trust beyond that imposed by state law. Thus, it is still possible under the Act to create a generation-skipping transfer trust in some states that will continue in perpetuity, and avoid the GSTT on the transferred amount plus appreciation after the date of the transfer.

Clients who have implemented planning techniques to take advantage of the GSTT exemption should ensure that their GSTT exemption is properly allocated by timely filing Form 709 with respect to the transfers.

3. Be Sure to Make Your Annual Gifts.

In 2018 and 2019, individuals may make gifts of up to $15,000 per recipient without triggering the tax. Married couples eligible to split gifts may make gifts of up to $30,000 per recipient. Gifts to a spouse who is a U.S. citizen are not taxed, regardless of the value of the gift. The annual amount which may be given to noncitizen spouses without subjecting the transfers to gift tax has increased to $155,000 for 2019.

4. Consider Interest Rate Sensitive Opportunities.

Each month, the IRS publishes interest rates that taxpayers may use, or in some circumstances must use, in connection with their income or gift tax planning. These rates are called the Applicable Federal Rates (AFR). Since 2012, when the AFR reached an historic low, the rates have been slowly increasing. There are several planning strategies which are advantaged by the still-low interest rates.

Clients who would benefit from planning strategies that use low interest rates should consider implementing those strategies before the AFR increases any further. In addition, clients who implemented such techniques when the AFR was higher than the current AFR should reevaluate their plans to determine if application of the current AFR could enhance the benefits of their plans. For example, clients who sold assets to a grantor trust in exchange for a promissory note prior to 2009, when the AFR used to determine the promissory note's interest rate may have been higher than the current AFR, or made a loan to a child for a note, should consult with their legal advisors about refinancing the promissory note in order to take advantage of the lower AFR.

5. Take Advantage of Basis Planning.

If a grantor trust owns assets with a low tax basis relative to their current fair market value, clients should consider exchanging those assets for cash or assets with a high tax basis. This type of exchange between an individual and grantor trust is not treated as a sale for income tax purposes, and, consequently, will not trigger an income tax. When the individual dies, under current law, the low basis assets that he or she owns will receive a "step-up" in basis equal to the fair market value of those assets at the time of death. If the assets are then sold, no tax will be owed on the sales proceeds up to the amount of the new "stepped-up" basis.

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6. Consider Bunching Charitable Contributions into a Single Year.

The Act allows taxpayers to deduct charitable contributions of cash up to 60 percent of their adjusted gross income—an increase from 50 percent under prior law. Clients should consider accelerating their charitable donations to offset the tax burden created by the reduction in itemized deductions discussed above, possibly through a donor-advised fund. It may be desirable to consolidate planned charitable gifts into a single year instead of making gifts over the course of multiple years.

7. Keep an Eye on State and Local Taxes.

Your Pillsbury Team is closely monitoring developments with respect to the deductibility of state and local taxes. The Act significantly limited deductions for state and local income taxes, sales taxes and property taxes. Both single and joint filers are permitted a maximum itemized deduction of $10,000 for their state and local taxes. This limitation negatively affects taxpayers who reside or work in states with high income tax rates, such as California, Connecticut, New Jersey and New York. These states have been seeking ways to reduce the impact of the loss of this deduction on their residents. Connecticut, Maryland, New York and New Jersey have filed a lawsuit asserting that the cap is unconstitutional.

8. Be Aware of State-Level Developments.

A significant number of states impose a form of estate or inheritance tax on their decedents. California continues not to impose an estate tax on its residents. In 2019, the New York State estate tax exclusion is scheduled to increase to $5.74 million for deaths on or after January 1, 2019 and before January 1, 2020. Decedents with dates of death on or after January 1, 2019 will also no longer be required to include the amount of gifts in the calculation of their New York gross estates, regardless of the date they were given.

9. Determine if Old Trusts Would Benefit from Modification.

The concept of trust decanting, or pouring over assets from one trust into a new trust with more favorable terms, has become increasingly popular in recent years. California adopted the Uniform Trust Decanting Act in September 2018, and it will become effective January 1, 2019. The new law permits trustees to modify certain existing irrevocable trusts without court approval or consent of the settlor and beneficiaries.

Please contact our team to discuss ways in which you and your family may benefit from the opportunities afforded by the current law in 2019. If you have not had your estate plan reviewed since the changes in the law, we encourage you to contact us at your earliest convenience to ensure the changes in the law have not impacted your estate plan.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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