HECKSCHER TEILLON
TERRILL & SAGER, P.C.
PERSONAL, TRUST & ESTATE LAW

(610) 940-2600
100 Four Falls, Suite 300
West Conshohocken, PA 19428

To Our Clients and Other Friends: February, 2019

We hope that this message finds you and your families well as we begin 2019.

We last wrote to you in the beginning of 2018 to explain the Tax Cuts and Jobs Act of 2017 (the "Act"), and how it could impact our clients' estate planning. As a reminder, the Act significantly increased the federal estate, gift and generation-skipping transfer (GST) tax exemptions. In 2019, as a result of the inflation adjustments, all three exemptions are now $11,400,000. This means that a married couple, with proper planning, has the use of $22,800,000 in gift tax, estate tax and generation-skipping transfer tax exemptions, provided that certain actions are taken when the first spouse dies (the unused gift and estate tax exemption of the first spouse to die still can be "ported" to the surviving spouse, although the unused GST exemption cannot be). The increased exemptions are still scheduled to sunset as of January 1, 2026, at which time the exemptions will revert back to the 2011 exemption amounts of $5,000,000 each, adjusted for inflation.

The annual gift tax exclusion remains $15,000 per donor per recipient in 2019.

The Act's dramatic increases in the exemptions led many clients to re-visit their estate plans to ensure that the actual flow of assets based on these formulas and their estate plans remained consistent with their wishes. Throughout 2018, we assisted with updates to many clients' estate plans because their wills or revocable trusts provided for transfers at death that were computed based on a formula tied to the estate tax exemption amount or the generation-skipping transfer tax exemption amount. *We encourage those of you who think your estate plans might have been impacted by the increases in the exemption amounts to reach out to us to re-visit your estate plan.*

Important Guidance on the New Tax Act

The IRS issued some guidance on the new Act in 2018. Although the guidance provided by the IRS is useful, we expect that the Act's full effect will be felt and understood more fully as we enter the 2018 income tax filing season early this year.

After the new Act, some commentators had expressed concern about a potential "clawback" effect if a donor makes lifetime gifts at a time when the gift tax exemption amount is large (now $11,400,000) but then dies when the federal estate tax exemption amount is smaller (for example, in 2026 when the exemption amount would be $5,000,000, inflation adjusted).

In November 2018, the IRS issued Proposed Regulations alleviating these concerns. The proposed rules will allow decedents' estates the benefit of higher credit amounts for gifts made in years in which the exemption amounts were greater. Assuming that this rule will be finalized, donors will be able to be confident that by making significant gifts using the temporarily-increased exemption amounts that the benefit of such gifts will not be "undone" if the exemption amounts are reduced in later years. Of course, if the exemption amounts are reduced in future years, and the donor has not made significant gifts in years in which the exemption amounts are higher, then the donor would not get the benefit of those increased exemption amounts. Although 2026 is several years away, this has led some of our clients to accelerate their gifting agendas to ensure that they take advantage of the increased (and eventually expiring) exemption amounts.

Also in November 2018, the IRS issued Final Regulations on the new §199A deduction for qualified business income of pass-through entities, such as partnerships and S corporations. The application of the §199A deduction to trusts and estates which own interests in partnerships and S corporations was an area of particular concern for planners. The Final Regulations have clarified some open questions, allowing for planners to implement new structures and techniques to maximize the benefit of the qualified business income deduction for individual owners and for estate/trust owners of partnerships, LLCs and S corporations.

Continuing Opportunities for Income Tax Planning

Income tax planning for existing trusts continues to be an area of opportunity, particularly given the increases in the estate/gift tax exemption amounts. In many cases, we advise clients as to whether it would be more beneficial ***from an income tax perspective*** to have appreciated trust assets included in a beneficiary's estate achieve a step-up in income tax cost basis at the beneficiary's death. Fortunately, the Pennsylvania Uniform Trust Act, and in some cases the terms of a trust instrument, might allow for planners to make modifications, exercise certain powers or otherwise take steps to achieve the step-up in income tax cost basis at death for appreciated assets, thereby reducing or eliminating income tax on pre-death capital gains. *If you have a trust with highly appreciated assets, please contact us to evaluate.*

Further, under the new Act, trusts (like individuals) are permitted to claim income tax deductions only for up to $10,000 of state income taxes. Thus, planning to reduce or eliminate state trust income tax has taken on new significance now that state income tax deductions are limited. We are regularly finding opportunities to modify or adjust the circumstances pertaining to the administration of a trust to allow for a more preferable posture for state income tax purposes to reduce or eliminate the state income tax on the trust. *In particular, if you have a trust with few or no contacts with Pennsylvania remaining, then contact us to review whether there are opportunities to reduce the Pennsylvania fiduciary income tax.*

Other Updates

We at HTT&S are committed to alerting our clients through these Client Blasts about how they might be affected by the Act and other tax law changes. *If you would like to discuss the specific aspects of how the Act might affect your estate plan, you always should feel free to contact us.*