

Estate Tax Reform Predicted for 2017

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February 22, 2017



A key goal for those of us who practice with Ward and Smith is to inform our clients and future clients of potential developments that may impact them. With respect to Trust and Estate Law, the potential for repeal of the federal estate tax, and a possible replacement for it, is the number one topic of discussion in 2017.

The politics of the estate tax have been in flux since 2001. Republicans have long set tax reform as a goal, including repeal of the estate tax. Its repeal is once again a

possibility with a Republican President, Senate, and House of Representatives. President Trump's platform of major reform of the Tax Code included a proposal to repeal "death taxes." However, President Trump's proposal also alluded to the possibility of enactment of a capital gains tax at death. Recently, both President Trump and Vice-President Pence have commented that major tax reform will be announced in the near future. Thus, political commentators predict that tax reform will be undertaken in early 2017.

Although it is anticipated that reform of the estate tax laws will be part of the tax reform, the predictions vary as to the form that those new laws may take. Proposals include:

- Repeal of the federal estate, gift, and generation-skipping transfer taxes;
- Repeal of the estate and generation-skipping transfer tax, but not the gift tax;
- Repeal of the estate and generation-skipping transfer tax, but not the gift tax; and imposition of a capital gains tax on death;
- Repeal of the estate and generation-skipping transfer tax, but not the gift tax; and imposition of a capital gains tax on death and on lifetime gifts;
- Phase-in of any such laws;
- Sunset of any such laws; or,
- Repeal of the repeal.

It's even possible, if not likely, that any legislation passed will result in something substantively different from any of the above options.

Will the Past be the Prologue to the Future?

A review of the estate tax enacted in 2001 provides us with insight as to what might occur in 2017. In 2001, newly elected President George W. Bush pushed for a repeal of federal estate taxes. At that time, there was a Republican-controlled Senate. Although new estate tax laws were enacted in 2001, all predictions about what they would look like were well off-base. The reform passed in 2001 included a phase-in of increases in the estate tax deduction, actual repeal of the estate tax in 2010, and then the sunset of all the 2001 tax laws,

including the repeal, as of December 31, 2010! The prediction that tax law reform would occur was accurate, yet none of the tax experts accurately predicted the new tax legislation which was actually enacted.

Thus, rather than focusing on the various proposals that have been advanced at this time, the focus should be on what you should do in the midst of this uncertainty.

Will You Be Affected by Estate Tax Repeal?

First, to determine if any of the proposed changes will impact you, you need to understand the current tax laws. As of January 1, 2017, the federal estate tax laws continue to provide for your ability to leave an unlimited amount to your spouse or a charity. The estate tax exemption for transfers at death to individuals other than a spouse or charity, which was set at \$5,000,000.00 in 2013, was indexed for inflation, and is currently \$5,490,000.00.

In addition, since 2013, if you are a surviving spouse, you may elect to use your deceased spouse's remaining estate tax exemption in addition to your own estate tax exemption. Thus, with appropriate planning, a married couple can exempt the first \$10,980,000.00 of assets left to their family from estate taxes. Any property in excess of the applicable exemption is subject to an estate tax rate of forty percent (40%).

According to the Tax Policy Center, only one in 517 decedents (or .019%) will pay an estate tax. But even for those who are unaffected now, estate planning is important.

Currently, any asset that is included in your estate will receive a new "stepped up basis" for capital gain purposes to the value of such asset as of the date of your death. For example, if you paid \$1 for a share of stock years ago and that stock is worth \$100 at your death, the individual who inherits your stock will now have a \$100 basis in the stock (this basis treatment is commonly known as "stepped up basis") and will pay no income tax if he or she sells the stock for \$100. However, if you give the stock away during your life, the person who receives the gift would continue to have only your \$1 basis in the stock (this basis treatment is commonly known as "carry-over" basis) and would have to pay tax on a \$99 gain if they sold the stock. Thus, good estate planning could result in the basis step-up allowing all of your gain on investments to pass free of income tax when you die. Your beneficiary will receive all of it instead of sharing it with Uncle Sam.

Planning if You Are Not Subject to Estate Taxes

Even if you are not currently impacted by estate taxes, you should not postpone estate planning. With the increase in financial abuse of the elderly, lawsuits, and divorce, planning to protect yourself and your beneficiaries remains critical. The need for planning to reduce expenses, public disclosure of assets, and red tape at your death is also becoming more and more important. Finally, you may also be interested in ensuring basis step-up. A well drafted estate plan can be the solution to many of these issues.

Review of Estate Plan if You Are Subject to Estate Taxes

If your estate is likely to be subject to liability for estate taxes, you may want to review your documents to ensure that your goals will not be undermined by changes in the tax laws with respect to estate taxes or capital gains. Building in flexibility may prevent an unintended result and minimize both estate and capital gains tax consequences. With all the unpredictability, adding flexibility to your lifetime documents such as powers of attorney will allow you to adapt to future changes in the tax laws, even if you become incapacitated. Likewise, adding flexibility to your testamentary plan to respond to future changes in the estate tax laws may assist in minimizing taxes at your death and the death of your surviving spouse.

Summary

With the uncertainty of what federal estate tax provisions will be enacted, it is as important as ever that you continue with, and update, your estate and trust planning.

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