
Trump the Estate Tax**By Richard S. Franklin**

Starting next year, Republicans will control the White House and Congress. Estate tax repeal is now being considered again. Will that happen, what shape will repeal take, and what estate planning changes should now be considered are all good questions.

Unfortunately, we cannot predict if repeal will actually happen. The national debt and effect of rising interest rates on it, the budget deficit and legislative constraints on increasing it, competing legislative agenda items, and on and on, all make this complicated and difficult to predict. We do know that repealing the "death tax" was part of President-Elect [Trump's tax plan](#) as reported on his campaign web site. We also know that the [Republican plan](#) includes a repeal of the estate and generation-skipping transfer (GST) tax.

Some commentators believe a repeal will not happen for various reasons, including because the \$5.49 million exclusion¹ already effectively exempts 99.8% of the U.S. population from the estate tax,² and because of the bad publicity President-Elect Trump would generate by reaping the benefits of repeal. However, others believe that repeal is likely, but because of budgetary rules it may be a temporary repeal similar to what happened in 2001 legislation that culminated in a temporary repeal in 2010. Some believe the gift tax will remain intact to prevent gaming the income tax system. Still others believe that migrating to a capital gains tax on death system similar to that in Canada is likely, perhaps retaining the gift tax. This allows Republicans to claim a repeal of the death tax, a long-held Republican position, while essentially just reducing the rate of taxation, which would cost the government less than outright repeal. Another capital gain alternative to the existing estate tax is to not immediately tax the appreciation in assets upon death, but provide that a beneficiary's income tax basis in inherited property would be the same as the income tax basis such property had in the hands of the decedent during his or her lifetime (i.e., carryover basis).

However you analyze the changing landscape, repeal of the estate tax is a far more realistic possibility than it was before the November 8th election. What should you do now and what estate planning changes should be considered?

From a big picture perspective, if maintaining capital within the family is your goal, then thoughtfully planning to mitigate the effect of taxes on the transfer of wealth is critical to accomplishing that goal. For example, a core component to estate planning that we have long

¹ The federal estate tax exclusion is \$5.45 million in 2016 and will be \$5.49 million in 2017.

² Alicia Adamczyk, [How Many People Pay the Estate Tax?](#), Time (Aug. 9, 2016).

advocated is that it is more efficient for tax purposes and more beneficial for non-tax reasons to transfer the wealth desired to benefit children and other family members during the parents' lifetime, usually into irrevocable trusts. Traditionally, such transfers were accomplished through gifts, sales of appreciating assets to irrevocable trusts, so-called grantor retained annuity trusts (GRATs), insurance trusts, and the like. Over the past several years, a colleague and I have developed a quantitative approach of making annual taxable gifts (that uses gift exclusion and in some cases the payment of gift taxes) to irrevocable trusts, at a steady pace over a client's life expectancy, sufficient to achieve the target amount desired to be set aside for family. This approach could be used exclusively or in combination with other traditional techniques, such as GRATs. We have been presenting this idea at continuing education conferences for trusts and estates attorneys around the country. The approach is far more tax efficient than could have been predicted without the quantitative analysis.³

The approach of moving wealth during lifetime to irrevocable trusts remains a sound, long-term estate planning strategy, even with the prospect of repeal on the horizon or in a post-repeal environment, for three primary reasons:

Repeal and Reinstatement. If the federal estate tax were repealed, wealthy families should be concerned that it will return when the political tides shift again. Both Secretary Clinton and Senator Sanders advocated an increased estate tax. Moreover, the modern estate tax has been around since 1916 – 100 years!⁴ If repeal of the estate tax is enacted, many attorneys would advise clients to immediately move assets to irrevocable trusts to protect against the possibility of it returning (“reinstatement”). Imagine counting on the repeal to hold, not implementing estate tax planning strategies in reliance on the repeal holding, and then when it's too late for estate tax planning to mitigate the impact of estate taxes, Congress re-enacts the estate tax shortly before death.⁵ Repeal is alluring to some, but too ephemeral to warrant serious reliance.

Asset Protection. Transferring wealth to irrevocable trusts should provide the family with greater protection from creditors, including divorcing spouses. Trust law has long permitted the interests of trust beneficiaries to be protected from the beneficiaries' creditors, subject to certain exceptions. This is a significant non-tax advantage to using irrevocable trusts.

Prince Charles Effect. Life expectancy is nearing 100 years. The average life expectancy in the U.S. is 81.2 years for females; 76.4 years for males (based on 2012 data as reported by the Centers for Disease Control and Prevention's National Center for Health Statistics). However, the statistics for the wealthy are substantially better: 91.9 years for females; 88.8

³ If you would like to have a copy of our latest materials on the Annual Taxable Gifts Approach, please email [Sharon](#) to request a copy.

⁴ Prior to 1916, the death tax was repealed and revived a few times.

⁵ It is also worth noting that about 20 states and the District of Columbia have separate estate taxes. In D.C. and Maryland, if the federal estate tax is repealed, the effective rate of tax at maximum rates would be about 16%. Moving assets into irrevocable trusts would mitigate the state estate taxes too.

years for males.⁶ This means that the children are often in their 70s before inheriting wealth from their parents – i.e., similar to Prince Charles, age 68, waiting to inherit the kingdom from his mother, Queen Elizabeth II, age 90! An additional benefit of moving the wealth being targeted for family during the lifetime of the parents is that it will be available sooner to the children and more remote descendants (through irrevocable trusts designed as the parents see fit). This reduces the negative energy associated with inheriting wealth (and the prolonged anticipation of that event) upon death.

This approach of moving wealth into irrevocable trusts represents what we believe is the best long-term strategy for tax and non-tax benefits. The merits of this strategy are durable and sufficient to justify continuing the approach notwithstanding changing tax laws. Of course, changing tax laws, as well as changing trust and property laws, should be considered and, when possible, used creatively to further the strategy. For example, as alluded to above, if the gift tax is repealed, it may allow greater freedom and tax efficiency in transferring assets to irrevocable trusts. Rather than thinking in terms of a repeal of the estate tax being a reason to abandon the strategy, we intend to creatively use any such changes to further the strategy that we believe best supports maintaining capital within the family.

On the personal level, estate planning documents should be reviewed to consider if changes may be desired in light of possible repeal. The following circumstances indicate a review may be appropriate:

Formula Marital Clauses. Many Wills and revocable trusts contemplate obtaining an estate tax marital deduction for transfers to a surviving spouse. Some estate planning documents use a formula based approach that essentially transfers the amount that can pass free of federal estate tax to a trust benefiting the surviving spouse and/or children, with the balance passing outright to the surviving spouse or a marital deduction trust for the surviving spouse's benefit. Consider whether the formula remains appropriate and if the formula provisions should be rewritten in the alternative – i.e., if the federal estate tax exists upon the decedent's death, then do X, and if not, do Y.

Large Charitable Gifts. Another common provision in Wills and revocable trusts is a gift to charity that under current law qualifies for the unlimited estate tax charitable deduction. Consider if it is desirable to make such a gift contingent on whether the estate tax is in effect. That is, would you rather make such gift to family members if it could be made without any estate tax being imposed – i.e., if the estate tax is repealed?

Durable Powers of Attorney. We alluded above to the prospect of families quickly moving assets into irrevocable trusts if the gift tax is also repealed as part of any estate tax repeal. The goal of this planning would be to grandfather assets from any subsequent reinstatement

⁶ See Max Ehrenfreund, [The stunning — and expanding — gap in life expectancy between the rich and the poor](#) (Washington Post, Sept. 18, 2015).

of the estate tax, as well as furthering non-tax goals. Consider updating your durable powers of attorney to authorize the agent to implement such a plan of action during any period of incapacity.

Shortened Life Expectancy. Anyone with a shortened life expectancy should review his or her plan immediately, as incapacity may prevent revisiting it later when and if estate tax changes are made.

Estate Administrations. Any decedent's estate currently being administered should extend the time for filing the estate tax return. Estate tax changes may impact certain decisions. Portability elections, for example, should be considered in the context of possible repeal. It could be that funding a traditional discretionary by-pass trust is beneficial to grandfather assets from a possible reinstatement of the estate tax, whereas any transferred estate tax exclusion from a deceased spouse could be worthless if there is no estate tax in the future or if the reinstated estate tax does not recognize transferred exclusion from a deceased spouse prior to reinstatement. Accelerating the estate's income tax deductions in 2016 may be beneficial too if income tax rates are reduced in 2017.

Gift Planning. We can envision circumstances in which making gifts to irrevocable trusts in anticipation of estate tax repeal (or, as mentioned above, during the actual period of repeal) is advisable for the purpose of grandfathering wealth from a subsequent reinstatement of the estate tax, as well as achieving non-tax goals. We have ideas on this.

If you have any questions, please contact us.

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