SHERMAN WELLS
SYLVESTER & STAMELMAN LLP

TAX AND TRUSTS & ESTATES UPDATE

November 2017

2018 Inflation Adjustments for Tax Items

With the new year will come new inflation adjustments for several tax-related items. Some of the more significant changes that will take effect on January 1, 2018 (and noteworthy items that have remained unchanged), are listed below.

ESTATE AND GIFT ADJUSTMENTS

Estate, Gift and Generation-Skipping Transfer (GST) Tax Exemption. The estates of decedents dying in 2018, as well as gifts made in 2018 above the annual exclusion, will have an aggregate exemption of $5.60 million (up from $5.49 million in 2017).

Annual Gift Tax Exclusion. The annual gift tax exclusion for 2018 is $15,000 (up from $14,000). The annual gift tax exclusion for gifts to a spouse who is not a United States citizen will be $152,000 (up from $149,000).

PERSONAL INCOME TAX ADJUSTMENTS

Application of the Highest Tax Rate. The tax rate of 39.6% affects single filers whose income exceeds $426,700 (up from $418,400) and $480,050 for married joint filers (up from $470,700).

Standard and Itemized Deductions. The 2018 standard deduction rises to $6,500 for single filers and $13,000 for married couples filing jointly (up from $6,350 and $12,700, respectively).

For itemized deductions, the deductions begin to phase out at the rate of 3% of the excess adjusted gross income over $266,700 for single filers (up from $261,500) and $320,000 for married joint filers (up from $313,300), with a cap of an 80% maximum reduction in total value of deductions.

Personal and Dependent Exemption. The personal exemption for 2018 is $4,150 (up from $4,050). It phases out at the rate of 2% for every $2,500 of adjusted gross income above $266,700 for single filers (up from $261,500) and $320,000 for married joint filers (up from $313,800). The personal exemption phases out completely at $389,200 for single filers (up from $384,000) and $442,500 for married joint filers (up from $436,300).

Alternative Minimum Tax. The Alternative Minimum Tax exemption amount for taxable year 2018 is $55,400 for single filers (up from $54,300) and $86,200 for joint filers (up from $84,500).

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RETIREMENT SAVING ADJUSTMENTS

Retirement Plan Contribution Limits. The 2018 contribution limit for 401(k), 403(b) and 457 plans is $18,500 (up from $18,000), with the additional catch-up contribution limit for these plans for taxpayers who are age 50 or older remaining at $6,000. The maximum contribution to IRAs remains at $5,500, with the additional catch-up contribution limit for taxpayers who are age 50 or older remaining at $1,000.

Deduction for Traditional IRA Contributions. The deduction for a traditional IRA for single people and heads of household covered by a workplace retirement plan will phase out at adjusted gross income between $63,000 and $73,000 (up from between $62,000 and $72,000). For married couples filing jointly, the income phase-out will be between $101,000 and $121,000 when the IRA contributor is covered by a workplace retirement plan (up from between $99,000 and $119,000), and between $189,000 and $199,000 (up from $186,000 and $196,000) when the IRA contributor is not covered at work but is married to someone who is.

Maximum Roth IRA Contributions. For Roth IRAs, the income phase-out range is between $189,000 and $199,000 for married couples filing jointly (up from $186,000 and $196,000). For singles and heads of household, the income phase-out range is $120,000 to $135,000 (up from $118,000 and $133,000). For a married individual filing a separate return who is covered by a workplace retirement plan, the income phase-out range remains $0 to $10,000.

Increase in Gift Tax Annual Exclusion to $15,000

As you may have read in the inflation adjustment article above, in 2018, taxpayers will be able to make "annual exclusion" gifts of up to $15,000 per donee (or $30,000 per donee for a married couple that elects to "split" such gifts on a timely filed 2018 federal gift tax return, which would be due on April 15, 2019, unless extended). The annual exclusion amount was finally increased from $14,000, where it had been holding steady since 2013. Accordingly, for 2018, outright gifts to individuals (and gifts to certain eligible trusts) that are below the annual exclusion will not reduce your available lifetime gift and estate tax exemption. These gifts, if made regularly on an annual basis over many years, can significantly reduce the size of your taxable estate at your death. If you think you'd like to incorporate annual giving into your overall estate plan, now (before year end) is a great time to get started.

Proposed U.S. Tax Legislation – Stay Tuned

As you may be aware, the House Ways and Means Committee recently released the proposed Tax Cuts and Jobs Act (H.R. 1), and the Senate Finance Committee has released a policy framework that it intends to incorporate into its own tax reform bill. The two proposals flesh out the outline of the Trump tax plan and bring Congress one step closer to the enactment of comprehensive tax reform legislation. Each of the House bill and the Senate proposal contains various provisions that would increase the federal estate, gift and generation-skipping transfer ("GST") tax exemptions substantially, and the House bill proposes eliminating the estate and GST taxes entirely after 2023. Both the House bill and the Senate plan would retain the basis step-up for inherited assets.

As expected, the two plans each also propose changes to current individual income tax rates, corporate and pass-through tax rates, and available deductions and credits; however, there are substantial differences in the specifics of the House and Senate proposals. The legislative landscape is likely to change rapidly, as the Senate Finance Committee completes its bill, both chambers work to pass their respective versions (which will ultimately need to be reconciled) and Republicans push for enactment of legislation by the end of the year. Stay tuned.

New Jersey Estate Tax Repeal

Beginning on January 1, 2018, the New Jersey estate tax is completely repealed. The New Jersey transfer inheritance tax remains. For the inheritance tax, property received by “Class A” beneficiaries (i.e., spouses, parents, children and grandchildren) and “Class E” beneficiaries (i.e., qualifying charities) is exempt from the tax, which means that many estates will not incur the inheritance tax at all. If you have provisions in your will or other documents that expressly reference the amount of the New Jersey estate tax exemption for formula or other purposes, you should revisit those documents in case adjustments to those provisions are needed in light of the estate tax repeal. Additionally, clients should be revisiting estate plans that leave small bequests to unrelated persons or extended family members that will trigger the imposition of a New Jersey inheritance tax, and inheritance tax reporting, where otherwise, with the repeal of the New Jersey estate tax, no New Jersey tax reporting would be required.

The Nonprofit Forum

This is another in a series of articles on nonprofit organizations that we feature in our regular Updates. We have found this area to be one of ever-increasing interest to our clients and colleagues, and we hope you will find these articles helpful and insightful.

Does Your Charitable Donor-Advised Fund Name Successor “Recommenders”?

Charitable donor-advised funds established at community foundations and other charities can be a very effective way for charitably-inclined individuals to house a charitable contribution (and obtain a current tax deduction) before the contributor has determined the particular charitable objectives to which he or she would like the donated monies to he directed. While the donor-advised fund remains subject to the complete control of the charity where it is custodied, that charity will allow the donor to recommend the charitable purposes to which the donor-advised fund will be directed. That recommendation privilege has caused many charitably-inclined individuals to opt for a donor-advised fund in lieu of a private family foundation (which has significantly greater costs and compliance issues).

Nevertheless, most individuals who establish donor-advised funds would like to see multi-generational participation in the recommendation process, again more in keeping with the structure of the family foundation, which provided the opportunity for successive generations to participate in the family's philanthropy. Contributors to donor-advised funds should therefore exercise the necessary due diligence to ensure that this multi-generational participation happens.

Most donor-advised funds allow the donor to select the next generation of "recommenders," and many funds allow all future recommenders to select their successors. Some funds, however, do not allow successor recommenders. And many funds will not allow successors to be named if the donor, or the current recommenders, have not appointed their successors in accordance with procedures specifically set forth by the charity where the donor-advised fund is located.

As an initial matter, before establishing a donor-advised find, it is very important for the prospective donor to know the charity's policies about appointing future fund recommenders. The inability to appoint future recommenders in many instances will be a reason to reject a particular donor-advised fund.

And, assuming the fund does allow for successor recommenders, the current recommenders should be especially diligent in ensuring that the proper paperwork is in place with the charity to designate their successors.

We would encourage anyone who has already established a donor-advised fund to check with the particular charity to confirm that they have designated successor recommenders. And if you are considering establishing a new donor-advised fund, you should first determine the fund's policies with respect to the naming of successor recommenders, if that is an important feature for you.

Internal Revenue Code Section 2704 Valuation Regulations Withdrawn

In August of 2016, the IRS proposed new Treasury Regulations that would modify the treatment of certain restrictions on liquidation for purposes of gift and estate tax valuations of intra-family transfers of interests in family-controlled organizations. In a previous alert, we noted that the regulations, as drafted, may have significantly curtailed the ability of a holder of an interest in a family entity to discount the value of such interest for gift or estate tax purposes on the basis of a lack of control and/or lack of marketability. As of October 20, 2017, these proposed regulations have been withdrawn, meaning these discounts will remain available unless the IRS chooses to revisit this issue in the future.

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