COMPARISON OF THE SENATE AND HOUSE BILL PROPOSALS FOR ESTATE TAX REFORM

Estates & Trusts Alert
November 13, 2017

Practices & Industries

Trusts & Estates

After years of calling for a comprehensive overhaul of the federal tax code, congressional Republicans in both the House and Senate, unveiled their plans for sweeping tax change – the Tax Cuts and Jobs Act – on November 2nd and November 9th, respectively. The House and Senate bills, while generally similar in their basic structure and aims, diverge sufficiently on the details such that reconciliation will likely lead to changes in both bills. As it stands now, both proposed bills would substantially alter the taxation of wealth transfers in the United States, with the House proposal including more radical changes than that of the Senate.

The Senate Bill Proposes:

- **Increased Personal Estate and Gift Tax Exemption.** Currently, an individual is entitled to a $5 million estate and gift tax exemption, as indexed annually for inflation ($5.49 million in 2017). The proposed legislation seeks to double that amount to $10 million, which would also be indexed to increase annually for inflation. A married couple would be able to transfer $20 million, plus the inflation adjustment, without paying any estate or gift tax. The generation skipping transfer tax ("GSTT") exemption will continue to mirror the estate and gift tax exemption, and will also be increased to $10 million per person, indexed annually for inflation.
- **Continued Step-Up in Basis at Death.** Under current law, an individual's income tax basis in property that he or she inherits from a decedent is the fair market value of the property as of the decedent's date of death. This income tax treatment would continue under the proposed bill, without any change from the current law.
- **Changes to the Charitable Income Tax Deduction**. While there are no proposed changes to the charitable deduction for estate tax purposes, and it remains to be seen how the proposed changes to the estate tax would impact charitable giving at death, lifetime charitable giving will continue to be a powerful income tax tool under the proposed legislation. The charitable income tax deduction is preserved, but with an increase on the deductibility limit for cash contributions to public charities. Under the bill, the deductibility limit would increase to 60% of the taxpayer's adjusted gross income, up from 50%.

The House Bill Proposes:

- **Increased Personal Estate and Gift Tax Exemption.** As with the Senate bill, the House also proposes an increase in the estate and gift tax exemption, up to $10 million, indexed to increase annually for inflation.
- **Repeal of the Estate Tax.** The proposed bill seeks a complete repeal of the estate tax for individuals dying after December 31, 2024. The repeal date had been set for December 31, 2023 in the original House bill, but has been pushed forward a year by a subsequent amendment.
- **Increased Exemption and Repeal of Generation-Skipping Transfer Tax ("GSTT").** In parallel with the estate tax, the bill proposes the repeal of the GSTT for transfers to individuals two or more generations below the transferor occurring after December 31, 2024. Prior to the repeal, the GSTT exemption would be increased to $10 million per person, indexed for inflation, just like the estate and gift tax exemption.
- **Continued Step-Up in Basis at Death.** As with the Senate bill, the House proposal continues stepped-up basis treatment for property passing at death. This is a more dramatic shift, however, considering the proposed repeal of the estate tax. Currently, stepped-up income tax basis is essentially a trade-off – because estate tax was paid on the property (or would have been paid if the decedent's estate exceeded the $5 million exemption amount plus the applicable inflationary adjustment), the inheritor gets full basis in the property and can sell the property in short order without triggering a significant capital gains tax. The proposed legislation keeps the stepped-up basis provision even after the 2024 estate tax repeal. This gives taxpayers both benefits: eliminating estate tax and allowing their beneficiaries to receive stepped-up basis in inherited assets.
- **Adjusted Gift Tax Rates and Increased Exemption.** Also proposed are changes to the gift tax regime. Even after the proposed estate tax and GSTT repeal, the gift tax would remain in place. However, for gifts made after December 31, 2024, the top gift tax rate would be 35%, down from 40%. The gift tax exemption would continue to be $10 million per person, indexed for inflation.
- **Changes to the Charitable Income Tax Deduction**. The House bill proposes the same changes to the charitable income tax deduction as the Senate version.

Currently, the House proposal has been voted out of Committee and is scheduled to be voted on by the full chamber in the coming weeks. The Senate bill will likely undergo the markup and amendment process in the Senate Finance Committee before being brought to the floor of the Senate. Congressional Republicans have expressed a desire to have a reconciled bill passed and on the President's desk by the end of the 2017.

Significant changes to the transfer tax regime may be on the horizon. Until the landscape becomes clearer, taxpayers should continue to monitor and maintain their current estate plans, keeping in mind that the estate tax, gift tax, and GSTT exemptions are scheduled to increase to $5.6 million per person in 2018. In addition, the gift tax annual exclusion is scheduled to increase from $14,000 per donee to $15,000 per donee as of January 1, 2018.

For more information on the proposed Tax Cuts and Jobs Act, and its impact on estate planning, please contact one of the members of Hodgson Russ's Estates and Trusts Practice Group.