First Bankers Trust Services

estate planning briefs®

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Middle-class tax cut?

While campaigning ahead of the midterm elections, President Trump promised a 10% tax cut for the middle class, to be voted upon after the election. There were no details on how such a cut might be designed, and the White House later clarified that the idea would be incorporated in the "Tax Reform 2.0" already under Congressional consideration. Ways and Means Chair Kevin Brady (R-Texas) promised to work with the Treasury Department to flesh out the proposal. Senate Finance Chair Orrin Hatch (R-Utah) was more skeptical that another tax cut was possible, but he did say that he had "seen miracles happen."

Tax reform 2.0?

Three separate tax bills cleared the House of Representatives in October, and then stalled in the Senate. Taken together, they are being referred to as "Tax Reform 2.0," an extension and expansion of the Tax Cuts and Jobs Act enacted last year.

These bills illustrate the current priorities of the Ways and Means Committee.

Protecting Family and Small Business Tax Cuts Act (H.R. 6760). This bill makes permanent almost all of the individual items from TCJA that are scheduled for a sunset at the end of 2025, including the doubling of the amount exempt from federal estate and gift tax. The bill also makes permanent the $10,000 cap on the deduction for state and local taxes. The cost of permanent tax reform was scored at $631 billion over ten years.

Family Savings Act (H.R. 6757). The bill is the successor to the Retirement Enhancement and Savings Act (H.R. 5282) from earlier this year. Among the provisions of FSA is a waiver of the required minimum distribution rules for accounts of less than $50,000. New parents would be permitted penalty-free withdrawals from their retirement accounts for the expenses of births or adoptions. Rules for 529 plans would be loosened, as some expenses of apprenticeship and home schooling would become qualified expenses. The more important provision might be the creation of a Universal Savings Account (a USA). After-tax contributions of up to $2,500 would be permitted, and tax-free withdrawals would not need to be tied to retirement.

American Innovation Act (H.R. 6756). Rules for start-up and organizational expenses would be consolidated for new business ventures, and up to $20,000 could be expensed in the first year. Start-up net operating losses and tax credits would be preserved after an ownership change. The tax cost of the changes was estimated at $5.4 billion over ten years.

COMMENT: Should the $11+ million per taxpayer exemption ($22+ million per couple) become permanent, the conversations that estate planners have with most of their clients will be different. Planning for taxes at death will be focused on basis planning and capturing basis step-ups, rather than transfer taxes, except in the few states that retain their death taxes. Another effect of making the larger exemption permanent could be a loss of momentum in the movement to repeal the federal estate tax entirely.

Scrivener's error repaired

Taxpayer and his spouse created and funded generation-skipping trusts for their three children. The trusts provided the beneficiaries with *Crummey* powers of withdrawal of additions to principal.

When the taxpayer changed estate planning advisors, the new attorney spotted three errors in the estate plan. First, the *Crummey* power had not been limited to the annual exclusion amount, but it could potentially apply to the entire addition to principal, which would make it a general power of appointment. Second, the lapse of the power was limited to $5,000 or 5% of trust assets and was not cumulative, but lapsed annually. Each lapse thus could be a taxable transfer by the beneficiary. Finally, although the first attorney had properly filed the gift tax return for the funding of the trust, he failed to affirmatively apply the couple's GSTT exemptions to the trust.

The state court was asked to reform the trust to conform it to the settlors' intentions, and it did. Are there federal transfer tax consequences?

Happily, for this taxpayer, all the tax problems have been solved. The IRS holds that the correction of a scrivener's error by the state court will not be considered an alteration or amendment of the trust. An additional 120 days was granted to the couple to file their GSTT elections.

—Private Letter Ruling 201843006

Discount for limited partnership of 18%

In 2008 Streightoff and his wife created a family limited partnership for their investment portfolio. The portfolio was 61.6% in stocks, 23.6% in municipal bonds, 13.5% in mutual funds, and the balance in cash. The initial value of the transfer is not given in the decision. Streightoff Management, LLC (managed by Mrs. Streightoff), was the general partner. Upon creation there were nine limited partners, with Streightoff retaining an 88.99% limited partnership interest. Limited interests of 0.77% and 1.54% for the younger generation family members were reported as taxable gifts.

On the same day as the family limited partnership was created, Streightoff created a revocable living trust. He transferred his limited partnership interest to the trust, and he also executed an assignment of that interest to the trust. Under local law, an assignment of a partnership interest grants rights to partnership distributions but not responsibilities in managing the partnership.

Streightoff died in 2011. On the alternate valuation date of November 11, 2011, the net asset value of the partnership was $8.2 million. The estate claimed substantial discounts to Streightoff's interest, which the IRS objected to, issuing an estate tax deficiency of $491,750.

The Tax Court held that whether the trust held the partnership interest directly or by assignment made little economic difference for federal tax purposes. The estate's 13% discount for lack of control was not allowed, as the Court found that Streightoff maintained control of the trust to the end of his life. A discount for lack of marketability was permitted. However, the Court accepted the IRS expert's analysis of an 18% discount rather than the estate expert's more generous 27.5% discount.

— Streightoff, Estate of Frank D. et al. v. Commissioner, T.C. Memo. 2018-178

COMMENT: When the Streightoff estate plan was executed, the federal estate tax exemption was just $2 million. The estate tax would disappear in 2010, but then return with a much lower exemption in 2011. As it turned out, Congress instead raised the exemption to $5 million in the year of Streightoff's death. Had he survived until 2018, his estate apparently would have had no federal estate tax obligation at all.

Extension granted for basis allocation election

Husband died in 2010, the year without a federal estate tax. Wife was the executor of his estate, and she hired an attorney to handle the tax matters. Estates of 2010 decedents had the option to have the estate tax apply after all, which would have the happy consequence of delivering a stepped-up basis to all estate assets. The election was made by filing Form 8939, which was initially due by November 15, 2011. Additional time was granted when the due date was extended to January 17, 2012 *[Notice 2011-76].*

Wife's attorney failed to prepare or file Form 8939. No reason for the failure is provided, but Wife would now like to make the election after all. The IRS holds that in relying on the attorney Wife acted reasonably and in good faith, and so it grants the extension of time for making the election.

—Private Letter Ruling 201842004

COMMENT: There appears to be no time limit for requesting an extension for making the basis election, so the IRS may be handling such requests for years to come.

TCJA scorecard

The official revenue scoring of the Tax Cuts and Jobs Act last year by the Joint Committee on Taxation may be found at JCX 67-17. The individual tax cuts were projected to lose $75.3 billion in 2018 alone, the business tax reforms $129 billion, but the international taxation reforms were expected to gain $68.9 billion. The net one-year decline in revenue was forecast to be $135.7 billion.

The final tally for the 2018 fiscal year is in, and it turns out that federal tax revenue did not fall; it rose compared to 2017, reaching $3.329 trillion, some $14 billion ahead of 2017's $3.315 trillion.

Strictly speaking, these numbers are not directly comparable, because JCT's projections were not against the 2017 actual experience but from the higher baseline of expected revenue from continued slow economic growth. Still, few people believed that tax revenue would be higher in absolute dollar terms following the TCJA enactment.

— Mnuchin And Mulvaney Release Joint Statement On Budget Results For Fiscal Year 2018, https://home.treasury.gov/news/press-releases/sm522

COMMENT: The deficit grew in fiscal 2018 because spending increases vastly outpaced the $14 billion revenue increase. As a percentage of GDP, federal revenue fell from 17.2% to 16.5% (0.7% decline), while spending fell from 20.7% to 20.3% (0.4% decline).

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