Wrap Up Lecture: Planning after the Tax Cut and Jobs Act of 2017
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Introduction

In lieu of a more traditional “wrap up” lecture summarizing highlights and planning nuggets from the week’s proceedings, this wrap up will instead explain several new planning opportunities and key planning points based on the Tax Cut and Jobs Act of 2017 (“TCJA”) practitioners in all disciplines should consider.

TCJA includes sweeping provisions that affect almost every aspect of tax, estate and other planning. More specifically, on December 20, 2017, the House of Representatives passed, as the Senate had a few days earlier, legislation initially called (and still referred to by many as) the Tax Cuts and Jobs Act of 2017. That short title was deleted in the reconciliation process so that the official name became: “an Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018” President Trump then signed the Act into law on December 22, 2017. The law was numbered Public Law 115-97.

The TCJA is worrisome, complex, disjointed, nettlesome, and worse. The legislation was formulated and finalized in a very short time frame. Challenges for advisers and clients include:

- Many changes turn upside down traditional tax treatments advisers and clients have long been accustomed to (e.g., C corporation rates lower than individual rates, alimony not being deductible, etc.).
- The complexity is daunting (e.g. new IRC Sec. 199A).
- Tax provisions changed from the House, to the Senate, and again to the Conference Report. And if that wasn’t confusion enough, there were even three more changes made by the Parliamentarian.
- There are at least several inconsistencies between the Conference Report and the statute enacted.
- The array of sunset provisions is disconcerting.

Wrap Up Topics

While the scope of the TCJA is incredibly broad, this wrap up will endeavor to address 5 topics:

1-Planning for increased temporary exemption.
2-Large estate planning during the current window of opportunity.
3-Trusts to capture income tax deductions.
4-199A – some additional thoughts.
5-Miscellaneous planning ideas post TCJA.

Increased Temporary Exemption
TCJA doubled the transfer tax exemption from $5M to $10M but this increase sunsets after 2025. This presents an incredible planning opportunity for many clients. The nature of this change, how it should be used, present unique challenges as will be explained.

The new increased exemption is a “use it or lose it” benefit. Practitioners should explain this to clients so they can plan to take action. The “lose it” is not only the 2025 sunset. What if a future administration takes legislative action to change the law before the sunset date?

Both clients and practitioners need to understand the broader implications of the exemption. Many will dismiss planning for moderate wealth clients as their net worth may be sufficiently below the new high exemptions that they may not perceive a need to plan. But it would be a mistake to only compare the client’s current net worth to the current exemption. Consider the client’s current wealth but also potential future wealth. A net worth of $5M might be $10M+ in 2026 when the increased exemption sunsets. So, planning before exemption declines is important for a far wider array of clients. Asset protection and other goals remain vital for many clients. But asset protection, as one example, has been affected in surprising ways that practitioners should consider, as will be discussed below.

Using the new exemption will have different implications for ultra-high net worth (“UHNW”) client the for more moderate wealth clients. Critically, planning for moderate wealth clients, perhaps from $5M to $50M of net worth, will in many instances be more complex and require novel planning approaches. Given the large size of current exemptions planning for “moderate” wealth clients will have to balance competing goals of: access to assets transferred, income tax issues resulting from the TCJA, and completed gift challenges to use the new temporary exemption.

For UHNW clients planning in many respects might proceed “business as usual.” The new exemptions may be modest relative to their estates and thus be readily used to augment existing plans. For example, a UHNW client might simply gift discounted interests in entities to existing irrevocable trusts to use their new exemption. But there are several new planning ideas that might be added to the practitioner’s quiver for these clients, as discussed below.

**Common Plans to Use Doubled Exemptions**

For moderate wealth clients using the exemption will require more access to assets to achieve a sufficient level of comfort to make gifts. Several options exist to meet this goal post-JCJA.

A planning structure that has become relatively common will serve as good foundation for many moderate wealth clients post-TCJA. That plan is the use of non-reciprocal, grantor, dynastic, GST exempt, spousal lifetime access trusts (“SLATs”). SLATs have and continue to serve many clients well as a means to use exemption, but nonetheless preserve access to the assets transferred to the trusts. A planning issue for SLATs has always been to avoid the reciprocal trust doctrine which might be used by the IRS to uncross the trusts causing estate inclusion, or be creditors to pierce the plan. Post-JCJA avoiding the reciprocal trust doctrine might be more difficult in light of the larger portion of wealth moderate wealth clients may commit to such

For single clients the use of domestic asset protection trusts (“DAPTs”) or variations of a self-settled trust, will be more common to facilitate single clients utilizing more of their exemptions. Because of the concern some commentators have over the use of DAPTs variations, which might collectively be referred to as “almost-DAPTs” may be more popular. For almost-DAPTs the settlor is not named as an immediate beneficiary but rather a person in a non-fiduciary capacity is given the power to add settlor as beneficiary. Another approach might be to provide for distributions to the settlor (or to descendants of the Settlor’s grandparents) in the discretion of a non-fiduciary.

A power to loan has traditionally been used to achieve grantor trust status. Perhaps that power should be revisited and strengthened for the purpose of permitting the settlor access to assets. Perhaps the power to loan to beneficiaries should generally be evaluated so that if a much greater portion of moderate family wealth is transferred to irrevocable trusts another option to access those assets will exist.

In addition to assuring access to trust assets, steps should be considered to facilitate basis inclusion. Consider, for example, adding an IRC Sec. 2038 power to the trust to create a mechanism to cause the trust estate to be included in the client’s estate to achieve a basis step up.

**Asset Protection and Irrevocable Trust Planning**

The TCJAs large use it or lose it exemptions will encourage some clients to gift larger portions of their wealth to secure those temporary exemptions. This will have significant impact on planning and the actions different types of planners might consider.

Some trust companies and other advisers have rules of thumb they have long used as to what portion of a client’s asset could be transferred to a DAPT or other irrevocable trust structure. Should advisers and trust companies loosen old rules of thumb on percentage of wealth that can be transferred? If not, those old rules of thumb, created when exemptions were not only smaller but perhaps when exemptions were perceived as permanent (acknowledging the similar fear of exemption decline that existed in 2012), are not loosened, those rules could prove the limiting constraint preventing a client from maximizing the use of the new temporary exemption. What other types of assurances, and what new benchmarks, will trust companies and other planners accept?

Should solvency affidavits and other due diligence be used more with greater portions of wealth transferred? Perhaps even if state law does not require these items they should be used given the larger percentages of wealth moderate wealth client may and often should transfer post-TCJA.

Access to transferred assets if more of wealth transferred is critical. Does this change the calculus of using long term care and life insurance to protect transferors? Perhaps more insurance should be used to backstop planning to use the exemption, regardless of the fact that the large
exemption might on initial reaction suggest less need for insurance. Perhaps the need for insurance coverage is not less, just different.

**A Few Planning Ideas for UHNW Clients**

While, as noted above, for many UHNW client planning as usual will continue. There might be a few new approaches or spins on traditional planning that might be considered.

Sale to Non-Grantor Trust: Note sale to grantor trusts have been and will remain foundations of many UHNW plans. But what about note sales to non-grantor trusts? Many UHNW clients have large existing irrevocable trusts that once the client has died are obviously no longer grantor. Those non-grantor trusts might be useful in note sale transactions. The loss of grantor trust status will accompany the death of the settlor. So, the assets passing from the estate of the settlor/decedent will have a basis step up and current value. Perhaps the risk of selling those assets to a non-grantor trust may not be intolerable. Because the assets received a stepped up basis on death no gain might be realized on the sale. Perhaps this type of sale could be combined with a more traditional note sale to a grantor trust, e.g. by the surviving spouse, to fractionalize ownership of a controlling equity position as between sales to the grantor and non-grantor trusts.

If the assets pass on first spouse’s death to QTIP that QTIP should have sufficient flexibility to permit the distribution of the equity to the surviving spouse to consummate the sale. If that QTIP has a HEMS standard or limitation on principal will that prevent the plan from proceeding? Not necessarily.

If a sale is consummated to a non-grantor trust, a defined value clause would be used because of the large size of a hard to value asset. But will a traditional defined value mechanism suffice? Perhaps not as a two-tier mechanism may be required as there could be both income and gift tax audits.

Another approach might be integrated into the traditional note sale to perhaps make a challenge more difficult. Perhaps there could be a collateral swap. Assume an existing now no longer grantor trust has substantial assets that have grown over the years. In a typical note sale transaction, the client would sell stock to an irrevocable trust for note and secure that note with the stock sold. But for some older trusts that might not be the only option. Consider using different assets of the old trust as collateral for the note and not the assets sold. Might that reduce the link for challenge?

Another interesting technique for large clients pursuing aggressive planning is the melting GRAT by combining the borrowing of securities from a dynasty trust and gifting those securities, subject to the loan agreement, to a GRAT. See Gooen, Snow and Harris, “The Estate “Melt”: GRATs Are Only the Tip of the Iceberg,” Estate Planning Nov. 2017.

**Asset Protection Planning-Are Non-Grantor Trusts Needed?**

The JCTA provides another wrinkle to traditional asset protection planning. With the new high exemption levels clients who had pursued transfers to irrevocable trusts to facilitate estate tax
minimization and asset protection planning may not have any estate tax concerns post-TCJA. That might leave the asset transfers having little other non-asset protection justification. But some of the new perspective on post-TCJA trust planning below might provide a solution.

A physician wants to pursue asset protection planning. Her net worth is about $14 million. Under prior law she would have faced an estate tax. Thus, creating and funding an irrevocable trust plan would have provided valuable tax as well as asset protection benefits. Under current post-JCTA law there is no estate tax benefit. In fact, the potential loss of a step-up might be viewed as a detriment to the plan. Does that taint planning as solely for asset protection purposes? If use a non-grantor trust plan that provides immediate income tax benefit does that provide a tax cover for the asset protection plan? Consider the planning technique discussed below.

**New Trust Structuring- INGs and Completed Gift INGs**

As discussed above clients post-TCJA will require several goals be met: using the new high exemption, assuring access to the assets transferred, and for many clients, especially those in high tax states, addressing the new restrictions the TCJA placed on state and local taxes (“SALT”). That will require a different spin on trust planning and drafting. Might it now be worth considering the limited use of non-grantor trusts to shift investment income out of the client/settlor’s high tax state reach considering that those income taxes won’t be deductible on the federal return in excess of a non-inflation adjusted $10,000 amount? Might the tax benefit of a non-grantor trust be further enhanced by salvaging substantial portions or all of the client’s home and vacation home property tax deductions?

Might these clients be able to structure completed gift (unlike the ING trusts), non-grantor (like the ING trusts) trusts to achieve both goals? Perhaps the traditional SLAT can be reformulated into a non-grantor trust to achieve the above state tax goals, without sacrificing the other post-TCJA goals.

Moderate wealth clients won’t make gift transfers they cannot access. So how can they use their temporary exemptions and save the SALT? To provide access to assets in trusts like SLATs might it be feasible to have the spouse as a named beneficiary (or the grantor if in a jurisdiction that permits self-settled trusts) only to receive distributions with the consent of an adverse party to avoid grantor trust status?

Would such trusts, if feasible from a federal income tax planning standpoint, be able to be planned around New York’s anti-ING legislation and avoid grantor trust status for New York purposes? NY just passed legislation permitting deductions of certain itemized deductions limited by TCJA on the client’s New York personal income tax return. With that new regime a traditional ING will be grantor trust under New York law, although it will remain a non-grantor trust on the federal income tax level. This should permit the settlor to deduct property taxes on her New York return, but remaining a non-grantor for federal purposes. As a non-grantor trust on the federal return the trust should be entitled to deduct $10,000 of property taxes leaving the client/settlor with $10,000 of other SALT deductions on her personal return.
How would a completed gift ING be structured? A trust may distribute income to the client/settlor’s spouse, or accumulate it for future distribution to the settlor’s spouse, all subject to the required consent of adverse party, and not be characterized as a grantor trust. IRC Sec. 672(a). An adverse party is a person having a substantial beneficial interest in the trust which would be adversely affected by the exercise or non-exercise of the power. This might include trust beneficiaries, such as an adult child (Consideration must be given, of course, to whether an adverse party consenting to the gift would be making a gift.). IRC Sec. 2514. A default remainder beneficiary is an adverse party.

Some high earning UHNW clients used incomplete non-grantor trusts to shift income out of the reach of state tax authorities. These trusts were funded with incomplete gift transfers and were structured to avoid grantor trust status. The idea was that income, e.g. a large capital gain on the sale of stock, might be earned inside the ING and avoid high SALT in a high tax state. This technique had become so successful that New York enacted legislation to treat such trusts as grantor trusts subject to New York taxation. This will be a great tool for ultra-wealthy clients that have used all of their exemptions and who do not need to access assets in irrevocable trusts. For a large swath of clients this will not be the optimal trust structure.

Clients with moderate (relative to the new high exemption amounts) wealth, who reside in high tax states, a different variation of all the above planning might be preferable if feasible to achieve. These clients, perhaps in a wealth stratum of $5-$40 million may be so wealthy that estate tax planning should continue because the higher doubled exemptions may be rolled back in the future. But these taxpayers may not be so very wealthy that they can afford to give up access to those trusts. Further, with the SALT deduction restrictions or elimination it may be prudent to shift investment income to a different low/no tax jurisdiction if feasible. Strip out powers given to grantor in ING trust. A forthcoming article will describe which and why.

**New Trust Structuring- SALTy SLATs**

Clients facing significant SALT limitations, including loss of property tax deductions, might consider a non-grantor variant of the traditional SLAT, referred to as a “SALTy SLAT.” That non-grantor trust may own the client’s homes multiplying the $10,000 SALT deduction. This planning might proceed as follows:

- Transfer the house and/or vacation home each into a separate limited liability company (“LLC”).
- Be certain SALTy SLAT has enough income to offset property tax deduction – perhaps transfer substantial portion of non-retirement investment assets if working and not in need of funds today.
- The LLC will be taxed as a partnership as it will be owned by at least two trusts, e.g. two non-reciprocal non-grantor SLATs. To avoid the partnership tax filing consider having the LLC election out of partnership status.
- The client and spouse would each gift LLC interests to non-grantor trusts - SALTy SLATs.
- Each trust should qualify for a $10,000 property tax deduction.
Consider loss of Sec. 121 home sale exclusion. Perhaps convert the SALTy-SLAT back to a more traditional grantor SLAT if the SALT rules are modified in future or if planning to sell house becomes important. The client will want the conversion done sufficiently in advance to start home sale 2 out of 5-year ownership period.

Some might question whether the multiple trust rules would derail the above plan. IRC Sec. 643(f): “…under regulations prescribed by the Secretary, 2 or more trusts shall be treated as 1 trust if— (1) such trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and (2) a principal purpose of such trusts is the avoidance of the tax imposed by this chapter. For purposes of the preceding sentence, a husband and wife shall be treated as 1 person…” But the regulations under 643(f) have never been issued. If no regulations are issued under such a situation, then the provision should have no enforcement power. SIIH Partners, 150 TC No. 3.

How might a SALTy SLATs be drafted? Consider the following suggestions:

- Start with a form for a beneficiary defective irrevocable trust (“BDT”).
- The trust should intentionally omit the swap power, and all other powers, that might make it grantor as to the settlor.
- Delete the Crummey power that is included in the typical BDIT to make the BDIT grantor trust as to the beneficiary.
- Add a requirement for approval (or provide veto power) to a non-adverse party on distributions to the spouse.
- Form the SALTy SLAT in trust friendly jurisdiction.

**Trusts Structuring- BDITs**

Might a variation of the Beneficiary Defective Trust (“BDT”) be used to achieve new planning goals to address the SALT restrictions of the Act? A BDT is an irrevocable trust that is a grantor for trust for income tax purposes as to the beneficiary and not as to the settlor. For example, parent may set up a trust for child, and that trust could be crafted to exclude provisions that would make the trust grantor as to the settlor. The trust would include an annual demand or Crummey power making the trust grantor as to the child/beneficiary.

In the traditional BDT (BDIT) the parent may create a BDT for a wealthy child with a $5,000 initial gift, so that the child could sell assets to the trust without triggering capital gain because the BDT would be grantor as to the child. A good plan, but how can this be spun for the Act? If the parent lives in a high tax state and the child in a no tax state, might a variation of the typical BDIT approach be used by the parent to shift income to a lower SALT environment to save SALT when they are no longer deductible?

Mom gifts $5,000 to a BDIT that is grantor to son in a low tax state. Mom then directs business opportunity to the trust which has no discernable gift tax value. Bross Trucking. The income generated will be reported by son in the no-tax state. The value of the business opportunity
would be grown outside the parent and child’s estate in contemplation of the sunset of the estate tax repeal.

**Charity, Tithing and New Standard Deduction Regime**

Most taxpayers won’t beat the standard deduction threshold thereby losing tax benefits of charitable giving. Consider forming a simple local non-grantor trust with a non-compensated family member serving as trustee. Include IRC Sec. 642(c) language so that the trust can qualify for a charitable contribution deduction. Gift sufficient investment assets to this trust to generate sufficient income annually to pay intended charitable contributions. Name heirs as well as charities as beneficiaries and give trustee power to allocate or distribute in his or her discretion. This will permit clients to donate to charities and still obtain a full tax deduction. Because children and other heirs are included as permissible beneficiaries this trust structure can provide or direct distributions to heirs in a given year.

Other charitable considerations might include:

- Fund donor advised funds (“DAFs”).
- Bunch deductions.
- Using IRAs after 70.5.

**IRC Sec.199A - Is it an SSB?**

IRC Sec. 199A for the first time requires the bifurcation of income along new never before used divisions: SSB income and non-SSB income. Consider the following example.

**Example:**

- A physician operates a practice. An FLP, separate from the practice entity, owns the buildings where the practice operates and leases the facilities to the practice entity.
- Another FLP, independent from the practice and the real estate entity, was created by various family trusts and hired a graphics designer and marketing firm. Those contractors created a practice name, logo, slogan, consumer facing website (i.e., one without client data), and related marketing materials that were licensed to the practice. The practice operates under the licensed name, uses the licensed logo and marketing materials on all letterhead, advertisements, signage, website and more.
- Equipment was purchased and held in a third FLP (this approach was common in pre-LLC days, nonetheless many such structures continue to exist). The equipment FLP leased equipment to the practice.
- These ancillary entities would all seem to be non-SSB’s independent of the medical practice. Further, so long as the prices are arm’s length for the rents and license fees the earnings in those entities should qualify for the IRC Sec. 199A deduction.

Consider gifting ownership interests to irrevocable trusts non-grantor trusts each of which has its own threshold amount.

**199A and 704(e)**
A client wants to maximize 199A deduction but has high taxable income. So, she gifts business interests to heirs who are in lower income tax brackets below the threshold amount. Does it work?

For a partnership (LLC taxed as partnership, GP or FLP) will IRC Sec. 704(e) and the requirement that capital be a material income producing factor impede the effectiveness of the gift?

**199A and Real Estate Developers or Fund Managers**

Client wants to maximize 199A deduction but all employees for real estate empire (or investment fund group) are housed in separate management company. Can the property LLCs (separate fund entities) contract with the management entity and pursuant to the terms of that contract characterize the management entity as an agent for each property entity (can the management entity opt to be a disregarded entity) and each property entity report a pro-rata (or other appropriate) share of payments for employees and treat those as W2 wages?

**199A and Large Law and CPA Firms**

Large professional practice firms might consider forming a REIT with leasehold interests. Smaller firms might band together and do the same. Leasehold interests are intangibles and cannot qualify for 2.5% calculation (that only applies to tangible property). REITs automatically qualify for 20% deduction.

**199A Restructuring**

As clients restructure business entities to capitalize on 199A consider impact on buy sell agreements, estate plans (what if certain interests/entities are owned by a trust and others are not), etc. The ripple effects to address could be significant.

**C Corporations and Accumulated Earnings Tax**

Might C corporations that are accumulating earnings in the 21% C corporation solution use permanent life insurance to justify the funds? Consider revising buy sell agreements funded with term insurance instead with high cash value insurance.

**Kiddie Tax and the NIIT**

Is there a change to the implications of this to the Net Investment Income Tax (“NIIT”)? “The provision simplifies the “kiddie tax” by effectively applying ordinary and capital gains rates applicable to trusts and estates to the net unearned income of a child... Taxable income attributable to net unearned income is taxed according to the brackets applicable to trusts and estates…”
It would seem that the Conference report suggests the application of a trust tax construct such that the threshold amount for NIIT purposes would be the $12,500 figure at which trusts reach the highest tax bracket.

However, the threshold amount in IRC Sec. 1411 does not appear to have changed so that a child would appear to still qualify for the $200,000 threshold amount.

So, trust distributions to a child beneficiary might still facilitate avoiding NIIT.

**Tax Preparation Costs No Longer Deductible**

The Act repealed the deduction for tax preparation expenses. Under the provision, an individual would not be allowed an itemized deduction for tax preparation expenses. The provision would be effective for tax years beginning after 2017. Under current law, these expenses are miscellaneous itemized deductions only deductible in excess of 2% of AGI, so many taxpayers may not have received significant benefit in any event.

This will likely result in taxpayers revisiting allocation of tax preparation fees as between business endeavors and personal returns preparation. Practitioners should be alert to possible ethical considerations if they bill the incorrect taxpayer (e.g. the client’s business instead of the client for personal non-business services).

Practitioners might protect themselves by cautioning clients in retainer agreements or a footer on bills, concerning the improper payment or allocation of fees.

**Sample Provision:** “How you allocate legal fees, to various persons, entities or trusts could affect whether the payment is tax deductible. It is important that you use checks drawn on the appropriate accounts for the appropriate entities or persons when paying legal fees. Paying personal expenses from a business entity could be argued by a claimant or tax authority as evidence of your disregarding the independence and legal integrity of the entity. If you personally, or another entity, pays for legal fees for the services rendered to that person, entity or trust inappropriately, the IRS might argue that the payment is equivalent to an impermissible additional gift and that the tax position of the trust should not be respected.”

**Matrimonial Changes**

Non-deductibility of alimony on divorces after 2018 is a major issue, but there are other minor ones of importance.

- Personal exemptions for children were commonly negotiated now they are gone
- 529 plans can be used for elementary and secondary school. Parties may have contemplated only college. Now what?

**Existing Durable Powers of Attorney**

Revisit gift provisions. Are they useful or necessary considering the exemption doubling? For many clients, the gift provision might warrant elimination by revoking the old power of attorney
(“POA”) and executing a new one that expressly prohibits gifts. For wealthy clients, they might wish to permit transfers of the exemption amounts but only to specified trusts. This might be appropriate if the clients are wary of using the new exemption amounts but want to facilitate further planning in the event they become incapacitated. Consider that an inadequate power of attorney was one of the significant issues in the Powell case.

**What and how to Inform Clients**

Do estate planners have an obligation to inform clients? For attorneys, if the client relationship was terminated, there is no obligation. If the client file is not dormant but active, there may be an obligation. Whatever the lawyer’s view of the status of the client’s file, what is the client’s view?

The steps to take will differ by practice. A planner with 100 clients can and will respond differently than a planner with 5,000 existing clients.

Does email work? Older clients often don’t have. Will that suffice?

Consider a post-card. Extract data from electronic rolodex and email to printing/mailing firm to send. It is inexpensive, visible and can succinctly communicate the point.

**Conclusion**

The TCJA has profoundly changed planning. This wrap up has tried to provide an overview several different planning perspectives considering the TCJA.