

Spring 2018

Tax and Estate Planning Update

On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act. This Tax and Estate Planning Update focuses on the federal estate tax changes and touches on other aspects of federal and state tax law which may affect your estate plan.

Federal and Connecticut Estate Tax

The federal estate tax exemption for the 2018 tax year is approximately \$11.2 million. If a decedent's taxable estate exceeds this amount, the excess will be taxed at a flat rate of 40%. For married couples the exemption can total approximately \$22.4 million in 2018, because the option of "portability" can be elected at the first death to transfer any unused portion of the deceased spouse's exemption to the surviving spouse.

As noted in our December newsletter, the Connecticut estate tax exemption for 2018 is \$2.6 million. The Connecticut estate tax exemption will rise to \$3.6 million in 2019, and current law will raise the state exemption to match the federal exemption in 2020. (The Connecticut law was passed before the federal exemption was so substantially increased in December, so the legislature may revisit the 2020 state exemption.)

Formula clauses

Clients who have not recently reviewed their estate planning documents should consider what effect the shifting federal and state estate tax laws have on the disposition of their assets, particularly when the documents include a "formula clause." A formula clause in a will or trust agreement is language that determines how assets will be divided at death. It is generally used for married clients, but formula clauses can also be used in other instances, such as gifts to charities or lifetime trusts for children.

A common formula clause funds a residuary trust (also known as a credit shelter trust) for the benefit of the spouse and descendants with the maximum amount that can pass free of state and federal estate tax, and then directs the trustee to distribute the balance to the surviving spouse. The amount passing to this trust increases as the Connecticut estate tax exemption increases. This can result in nothing passing to the spouse outright, which may not be what the decedent intended. In addition, some estate plans pass the amount that is not subject to state and federal estate tax directly to children or grandchildren, with the balance passing to the spouse outright or in trust. Under these scenarios, the surviving spouse could be disinherited altogether unless the documents are revised to address the new estate tax laws.

In particular, formula clauses in estate planning documents that have not been amended since 2006 can have significant unintended consequences, because up to \$11.2 million could be allocated to the residuary trust before any property is allocated to a marital trust for the spouse's benefit or distributed outright to the surviving spouse or to a charity.

Section 529 Plans

The new federal law expands qualified tuition programs, also known as “Section 529 plans.” Effective January 1, 2018, qualified expenses include tuition at an elementary or secondary public, private, or religious school, up to a maximum of \$10,000 per year.

Changes to the “Kiddie” Tax

The new federal law changes the income tax rates that apply to the unearned income of a child. Prior to January 1, 2018, unearned income of a child in excess of \$2,100 was taxed at the higher of the child’s tax rate or the parent’s tax rate. Effective January 1, 2018, the new income tax rates are:

Up to \$2,550:	10%
\$2,550 to \$9,150:	24%
\$9,150 to \$12,500:	35%
Over \$12,500:	37%

Next steps

If you would like to know how the new tax rules affect your estate plan, or if you think it is time to have your documents reviewed, please contact us. We recommend that you review your estate planning documents at least every five years, and more frequently when you have significant assets that are affected by the tax law changes or you have a change in family circumstances that could affect your plan.

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Readers are urged not to act on this information without consultation with their counsel. We carefully customize estate plans to our clients’ individual circumstances and personal objectives.

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