

Trusts and Estates Group Client Alert: Federal and State Tax Update

THE IMPLICATIONS OF FEDERAL TAX REFORM

On Friday, December 22nd, President Trump signed the tax reform legislation into law. The legislation makes sweeping changes to the tax code: It caps the state and local tax deduction at \$10,000 per taxpayer, lowers the top marginal rate for individuals and trusts from 39.6% to 37%, scales back the alternative minimum tax, eliminates miscellaneous itemized deductions (including the deduction for investment-related expenses), requires that carried interest be held for at least three years in order to be treated as long-term capital gains, and cuts the corporate rate from 35% to 21%. The legislation also allows individuals to deduct up to 20% of (1) certain real estate investment trust dividend income, (2) certain income from publicly traded partnerships (including master limited partnerships), and (3) qualifying business income from a pass-through entity, such as an LLC or a trust. “Qualifying business income” is defined as the net income or gain from a U.S. “qualified trade or business” (a category that excludes most service businesses as well as investment, investment management, and securities or commodities trading businesses), less any compensation or passive-type income (such as capital gains). The deduction for qualifying business income cannot exceed the greater of (a) 50% of wages paid or (b) 25% of wages paid plus 2.5% of capital assets.

The legislation increases the estate, gift, and generation-skipping transfer (“GST”) tax exemptions. Before the legislation’s passage, the exemption was \$5 million per person, indexed for inflation experienced since 2010. The exemption is now \$10 million per person, indexed for inflation experienced since 2010. The exemption will revert to the prior level, adjusted for inflation, on January 1, 2026. The legislation does not change estate, gift, or GST tax rates or repeal the estate tax. The legislation preserves the step-up in income tax basis for assets owned at death.

Many estate planning documents use “formula dispositions” that are equal to the federal exemption amount. The higher exemption amount may affect how these documents function, potentially triggering unanticipated state-level tax or changing the amounts that different beneficiaries receive. Individuals should review their estate plans to make sure their documents continue to reflect their wishes.

STATE TAX CHANGES

New York's estate tax exemption is not affected by the federal tax legislation. The New York exemption is \$5.25 million per person but, in 2019 onward, will be \$5 million per person, indexed for inflation experienced since 2010. As a result of the federal tax legislation, a significant number of New York estates will be subject to state estate tax but not federal estate tax.

New Jersey's estate tax was repealed on January 1. (New Jersey still has an inheritance tax, which applies to certain beneficiaries inheriting property but not to the estates themselves.) Delaware's estate tax was also repealed on January 1.

Pursuant to a recent budget agreement, Connecticut's estate and gift tax exemption rose to \$2.6 million per person on January 1 (up from \$2 million per person) and will rise to \$3.6 million in 2019 and then match the federal exemption in 2020. (The District of Columbia, Hawaii, Maine, and Maryland also have estate tax exemptions that are tied—or will soon be tied—to the federal exemption.) As part of the budget agreement, the cap on total Connecticut estate and gift tax liability for an individual, which is currently set at \$20 million, will decrease to \$15 million in 2019.

Please feel free to contact us if you have any questions regarding how these changes affect your current estate planning documents or create possible planning opportunities for you, or if you would like income tax advice from our Tax Group.

**TRUSTS AND ESTATES
GROUP**

Please feel free to discuss any aspects of this Client Alert with your regular Milbank contacts or any of the members of our Trusts and Estates Group.

If you would like copies of our other Client Alerts, please visit our website at www.milbank.com and choose "Client Alerts" under "News."

This Client Alert is a source of general information for clients and friends of Milbank, Tweed, Hadley & McCloy LLP. Its content should not be construed as legal advice, and readers should not act upon the information in this Client Alert without consulting counsel.

© 2018 Milbank, Tweed, Hadley & McCloy LLP.

All rights reserved.
Attorney Advertising.
Prior results do not guarantee a similar outcome.

NEW YORK
28 Liberty Street, New York, NY 10005

Georgiana J. Slade	gslade@milbank.com	+1-212-530-5616
James S. Sligar	jsligar@milbank.com	+1-212-530-5839
David J. Stoll	dstoll@milbank.com	+1-212-530-5880
Henri S. Benaim	hbenaim@milbank.com	+1-212-530-5269
Sean Imfeld	simfeld@milbank.com	+1-212-530-5322
Mohineet K. Khosla	mkhosla@milbank.com	+1-212-530-5601
Katie Lynagh	klynagh@milbank.com	+1-212-530-5435
Bich-Nga H. Nguyen	bnguyen@milbank.com	+1-212-530-5886
Leah Socash	lsocash@milbank.com	+1-212-530-5386
Marceline B. Tempesta	mtempesta@milbank.com	+1-212-530-5887
Peter J. Tucci	ptucci@milbank.com	+1-212-530-5582
Stephanie L. Vara	svara@milbank.com	+1-212-530-5588
