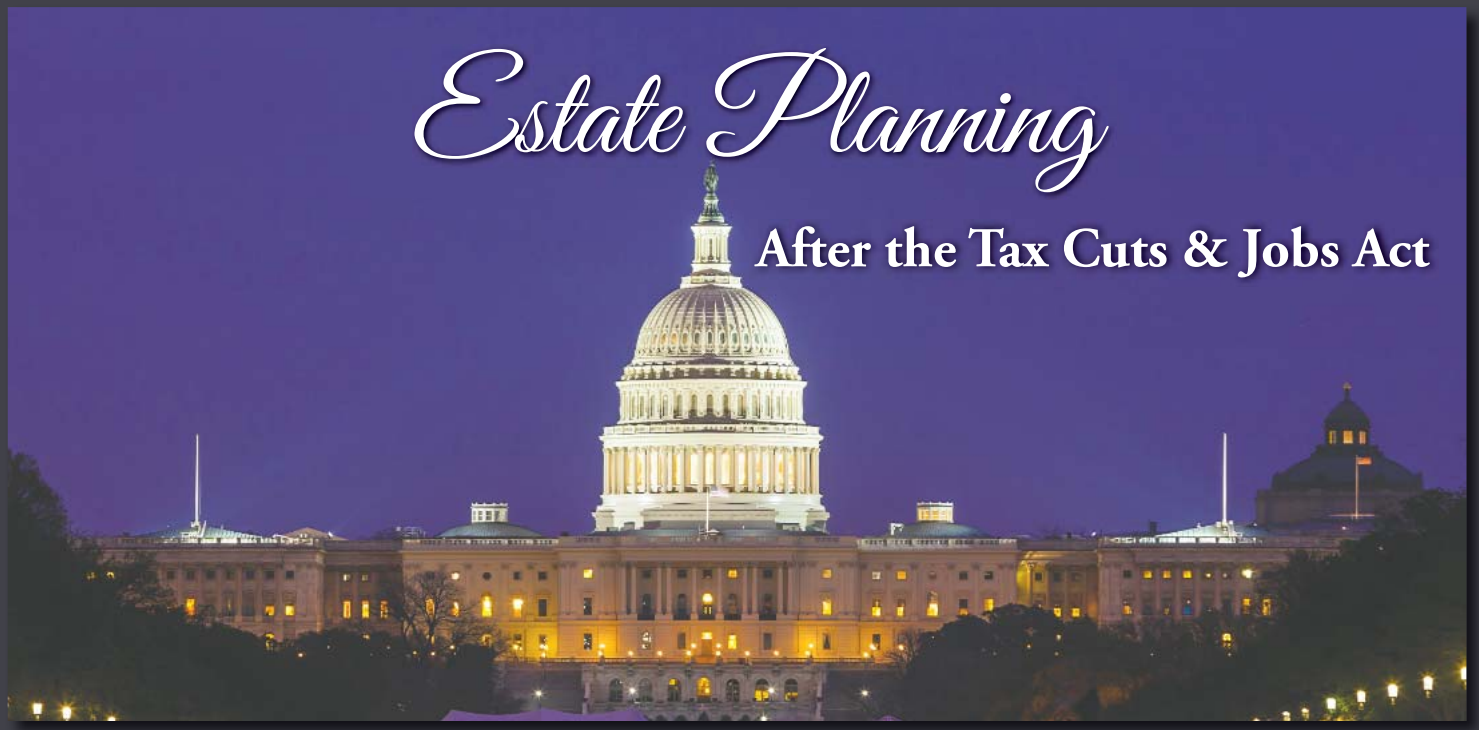
SUMMER 2018

First Covenant Trust & Advisors



Estate Planning

After the Tax Cuts & Jobs Act

On December 22, 2017, President Donald Trump signed the Tax Cuts and Jobs Act (TCJA), which went into effect on January 1. While the TCJA made sweeping changes to the tax landscape, this article focuses on its impact on estate planning. Before the TCJA, the federal estate, gift, and generation-skipping transfer tax exemption was $5 million ($5.49 million inflation-adjusted) for each individual. The TCJA increased that exemption to $10 million ($11.18 million inflation-adjusted) for each individual for years 2018 to 2025. The federal exemption is scheduled to return to 2017 levels in 2026, so these eight years provide a limited window in which to consider transferring wealth before the exemption potentially returns to its 2017 level.

Taking advantage of this time frame is especially crucial for those whose estates are above $5 million per individual or $10 million per couple, and the TCJA's increased exemption provides opportunities to combine income tax planning and estate tax planning. Now taxpayers can "have their cake and eat it, too" by making gifts and using the credit, by accessing assets and income, by avoiding estate tax, and by generating income tax savings. Please read on to learn a few ideas and considerations that may be helpful in the planning process.

PLANNING IDEAS

- Use up one complete exemption. If a married couple plans to give away significant amounts, one spouse can make an $11.18 million gift outright or to trusts. One exemption gets locked in at the $11.18 million level. And even if the amount reverts back to $5.49 million, at least one spouse got to take advantage of the $11.18 million exemption.
- Set up a spousal lifetime access trust (SLAT). Since the spouse is the beneficiary, this ensures that funds are available to at least one of the spouses. Be sure to avoid reciprocal SLATs, which could be "uncrossed" and put back into the grantors estates.
- Set up a non-grantor trust for concerns based around itemized deductions.
    - An individual can put his house in an LLC and then transfer the LLC interests into non-grantor trusts. The property is outside of the estate, the property is protected from creditors, the trusts deduct the property taxes, and the property tax deduction on Schedule A is no longer an issue.

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- Individuals who consistently give to charitable organizations may no longer itemize because of the increased standard deduction. The taxpayer can transfer investments into a non-grantor trust. When the trust earns income and then contributes it to a charitable organization, the trusts deducts the contribution, and the charitable contribution on Schedule A is longer an issue.

OTHER CONSIDERATIONS

- Give away assets with a high basis to individuals or non-grantor trusts. Since assets transferred during life retain the donor's basis, a lifetime gift of low-basis assets may result in capital gains taxes being payable by the done on the subsequent sale of the transferred asset, which would reduce the value of the gift. If, however, low-basis assets are gifted to a grantor trust, the donor will pay the capital gains tax, including the capital gains tax associated with pre-gift appreciation, on the sale of the assets as long as it occurs during the donor's lifetime.

- Give away entity interests. Gifts of a partial interest in a partnership, corporation, or other entity can transfer ownership and receive the benefit of a valuation discount based on lack of marketability and/or control.

- Older wills and trusts might not be optimal in this new environment; in fact, existing estate plans may have unintended negative consequences. An old plan may state that the children receive the amount that can pass free from federal estate tax and that the remaining amount should pass to the spouse. If that is the case, the spouse could be completely disinherited.

- Consider adding testamentary general powers of appointment based on a formula. This allows, for example, basis step-up for a bypass trust at the death of the surviving spouse without triggering additional transfer taxes.

- It is unclear what will happen if an estate elects portability in the 2018 – 2026 window and the exemption decreases by the time the second spouse dies. Will the Internal Revenue Service "clawback" the unused exemption of the first-to-die spouse?

What will happen to estate taxes when the next administration arrives? There is no certainty. Now is the time to review your current plan, implement new strategies, and take advantage of the new opportunities for gifting.

Brandy Bradley, CPA is a manager in the Tax Department at BCS. She has over 10 years of experience in tax planning and compliance for individuals, trusts and estates.

BEING MORTAL REVIEW

Being Mortal: Medicine and What Matters in the End is a 2014 non-fiction book by American surgeon and professor Atul Gawande. *Being Mortal* grapples with the competing interests that emerge when medicine collides with end-of-life issues.

If a person has a serious illness for which Medicine has a cure, the medical culture is well equipped to handle that. What about an illness for which there is no cure? How should the medical machine address the inevitability of impending death? "The fact that we have had no adequate answers to this question is troubling and has caused callousness, inhumanity and extraordinary suffering." Treatment at all costs has been the paradigm, but that paradigm is flawed. So Gawande argues the paradigm should be to enable well-being, not simply to prolong life. The medical system should promote, rather than prevent, a good end of life.

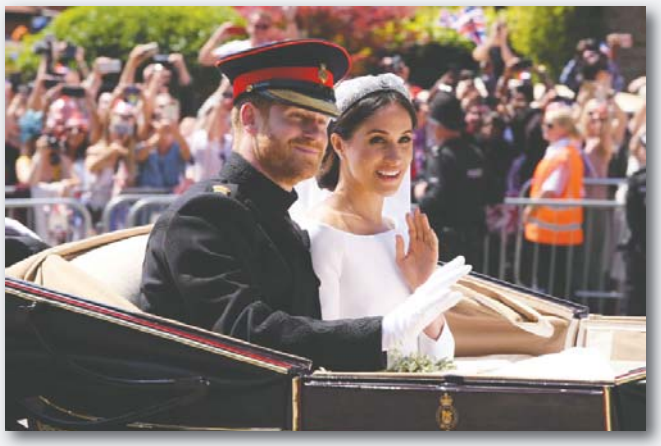
The book surveys Dr. Gawande's search for methods to help people live well as opposed to just living longer. I discussed this book with my brother who is a physician and who grapples daily with these issues, and largely agrees with Gawande about the importance of giving these questions consideration in advance. He recommends "anyone with a parent should read this book."

Dr. Gawande is an artful storyteller. Among the possibilities he advocates are a greater emphasis on geriatric training for medical students, a return to the independence-focused objective for assisted living facilities, and the importance of palliative care and hospice once the certainty of death draws near. He encourages loved ones to speak with each other about their priorities that make life meaningful, and the trade-offs that they are willing to make. "Our ultimate goal, after all, is not a good death but a good life to the very end."

David Greene, JD, CPA is the Senior Trust Officer at First Covenant.

WHEN *Harry* MET *Meghan*

On May 19, 2018 romantics from all over the world followed the coverage of the fairy tale wedding of Britain's Prince Harry to Meghan Markle, an American actress. In fairy tales, the prince and princess always live happily ever after. Sadly, in real life, the "ever after" is not always as happy as the beginning. The reality is though that 40-50% of marriages now end in divorce. Harry and Meghan—now known as the Duke and Duchess of Sussex—despite their considerable wealth, probably didn't enter into a premarital agreement before their fairy tale began.



Nothing says romance like a signed contract spelling out who gets what in the event of divorce. Lack of romance, however, is not why the royals do not invoke such contracts. Unlike in America, prenuptial agreements are not enforceable under UK law. Much of the work of asset protection for divorce is done by trusts.

A famous example of this occurred in Prince Harry's royal family. His parents had a nasty public divorce that ended when Princess Diana settled with Prince Charles for £17 million—a princely sum in 1996, but much less than the £75 million she reportedly demanded at the outset. "So much" of the royal family's assets "are owned by something else or someone else" according to Joe Little, managing editor of Majesty. Trusts play a large part in these structures. Because of this, Charles was not left destitute after his divorce. Prince Charles' Highgrove House and Birkhall are both estates that are trust owned. The Duke and Duchess of Sussex live rent-free in Nottingham Cottage at Kensington Palace, and other artwork and furnishings are available to them as members of the royal family, despite these assets not being owned by either one of the couple personally.

Bringing this a bit closer to home, trust ownership of assets provides creditor protection under US law as well. And trust ownership of assets is arguably more advantageous than relying exclusively on a prenuptial agreement. Not only does trust ownership protect assets in the event of a divorce, but also from anyone who wants to get their hands on the trust assets. A prenup's scope is limited to disputes between the spouses. Additionally, unlike prenuptial agreements, you don't need to interrupt the romance to negotiate—an asset protection trust can be established without the consent of a fiancé or anyone else.

In many American states, these trusts can be established by a person for his or her own benefit. They also provide an excellent mechanism to give gifts or leave inheritance to children or grandchildren, insulating that inheritance from the dangers of the outside world—including nasty villains masquerading as handsome princes or wicked witches in disguise.

Rachel Lyons is First Covenant's Account Manager.

MEET OUR NEWEST *Team Member*

Dee Ann Lechner is an administrative assistant at First Covenant Trust and Advisors. She has many years of loan processing experience and most recently worked as an administrative assistant in a Gift Planning and Trust Services Department in Minnesota. Dee Ann is married to Rob Lechner and they have two grown children, Austin and Hannah. She enjoys reading, cross-stitching, and helping her husband in church ministry.

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NAMING FIRST COVENANT AS EXECUTOR/TRUSTEE

It is our goal to serve as a resource to the planning community. First Covenant's advisors assist other professionals with various aspects of client service. Examples include brainstorming estate plans for challenging fact patterns, discussing income taxation of retirement plans, answering questions about existing trusts and duties of fiduciaries or income/gift/estate tax preparation support. First Covenant is also available for presenting on various topics, including estate planning, tax legislation and planning, trust planning and charitable giving. Feel free to contact us for assistance with anything related to our services or to schedule a presentation. To name First Covenant Trust in a document, please use: First Covenant Trust and Advisors, LLC, currently located at 801 Sunset Dr., Johnson City, TN 37604.

UNITED WAY WEEK OF CARING: FIRST COVENANT AT THE SALVATION ARMY

Recently, a group of volunteers from First Covenant, BCS Wealth Management, and the accounting firm of Blackburn, Childers and Steagall took part in the United Way Week of Caring at the Salvation Army Center of Hope in Johnson City. The volunteers cleaned the parking lot, weeded and filled in cracks and painted lines on the parking spaces. They also spent time with the patrons that frequent the Center for Hope. They really spruced the place up and made it very welcoming.