Tax Cuts and Jobs Act (TCJA) 2017

US Estate Tax reform – US citizens & domiciliaries

The Issue?

The US Tax Cuts and Jobs Act which was signed into law on 22 December 2017 by President Donald Trump effectively doubled the existing lifetime Estate and Gift tax exclusion amount. Prior to the tax reform, an individual's lifetime Estate and Gift tax exclusion was $5.49 million (2017 tax year), with the new exclusion amount from 1 January 2018 increasing to $11.2 million including inflation adjustment.

For a married couple, this could potentially shelter up to $22.4 million of assets from Estate tax given the portability that allows a surviving spouse to use a deceased spouse's unused Estate tax exclusion. The increased exemptions will only remain in effect through to 2025, at which point they 'sunset' and return to the 2017 exemption amounts.

Who does it affect?

All US citizens are potentially subject to US Estate and Gift taxes on transfers of assets owned worldwide. Additionally, citizens of other countries who are 'domiciled' in the US are also subject to US transfer taxes on their worldwide assets. To the extent that any Estate or Gift tax is payable (i.e. they have made gifts or hold assets on death that are in excess of the exclusion amount) a tax rate of 40% is applied.

However where an individual is neither a US citizen nor has a US 'domicile' for Estate and Gift tax purposes, the exclusion amount is usually limited to $60,000. There was no increase to this amount in the Tax Cuts and Jobs Act and it is not indexed for inflation. Certain countries, such as the UK, have an estate tax treaty with the US which may provide some relief in the event of double taxation.

Furthermore some US States impose their own transfer tax regimes running parallel to federal Estate Tax, therefore whilst an individual may now effectively be removed from Estate tax for federal tax purposes, Estate or Gift tax may still be imposed by the local State tax authority.

Opportunities?

The increased Estate and Gift tax exclusion amounts expire on 31 December 2025. Assets that are expected to appreciate significantly in future should be given sooner rather than later as means to remove future growth from potential taxation.

It is worth noting that there is a possibility of a clawback of the increased exclusion amount (for example, changes in Congress with the mid-term elections could theoretically undo the increased exclusion amounts). Clients should be aware of this if making large lifetime transfers.

Individuals who are neither US citizens nor US domiciles for Estate and Gift tax purposes should continue to plan for US transfer taxes on their US assets. Given the limited $60,000 Estate tax exclusion amount available to these individuals, they should consider how the ownership of US situated assets including but not limited to real estate and US stocks should be arranged.

Particular care should also be given to individuals who are married to non-US citizen spouses or who have complex family situations, to make sure their estate plans and Wills are reviewed in light of the recent reforms.

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