APRIL 4, 2018

NP

What’s trending on NP Trusts & Estates

Why you need an estate plan regardless of wealth, tax benefits for parents, deductions for charity-related travel expenses, special tax breaks for members of the military and more. Here’s what’s trending in estate planning and wealth management.

Estate Planning

Does one have to have a large estate to need an estate plan?

There are a variety of reasons to have a well-thought-out estate plan. Here are reasons our experienced estate planners find that estate plans are needed regardless of a client’s wealth.

Does one have to have a large estate to need an estate plan?

“While there is some modest cost to put together even a very simple estate plan, nothing is so expensive as the administration of an unplanned estate.”—*Jay D. Rosenbaum*

“Although it can be tempting to rely on intestate law rather than establish an estate plan, the law is not designed to grow and change with your family as an estate plan is. For example, intestate law may fail to protect any children who have spendthrift or addiction issues that inform their ability to handle money. Even a simple estate plan can avoid unnecessary complications and achieve a more desirable result for families based on the individual’s unique insight into his or her family dynamic. Once in place, an estate plan can easily be revisited and revised based on life events making it well worth the initial time and effort.”—*Sarah M. Roscioli*

“An estate plan can do more than provide tax benefits for individuals with large estates and net worth. No matter the size of your estate, having a simple estate plan—a will, health care proxy and durable power of attorney—in place can give your loved ones peace of mind in knowing that your personal wishes will govern in the event of expected and unexpected life events.”—*Kaitlyn Barnett*

“For parents of minor children, an estate plan allows them to appoint guardians to care for their children as well as set up a structure, which is typically a trust, for the management of their financial assets until their children are older.”—*Sarah T. Connolly*

“A family member may have special needs or may be a spendthrift. In those cases, a trust is an ideal vehicle to provide for the prudent and safe management of the beneficiary’s inheritance, while protecting him or her from the reach of creditors.”—*Evelyn V. Moreno*

“There is a frequent misconception that trusts are only useful for the wealthy. However, leaving your inheritance in a properly structured trust rather than outright, will protect the inheritance from your children’s future creditors, including a divorcing spouse. And if the trust is properly drafted, the child can still have a large degree of control, without risk of attacks from creditors.”—*Kenneth F. Hunt*

“It’s important that an estate plan is coordinated in all respects. I have experienced a number of cases in which a client, in an effort to “avoid probate,” has utilized techniques such as holding title to assets in joint name or registering securities in “transfer on death” format, only to decimate a distribution plan contemplated in their will. For example, in one case a client had titled virtually all of his assets in joint name with his wife, leaving insufficient assets to pass under his will where substantial bequests to his children were intended.” —*John L. Garrett*

The 2018 Estate, Gift and GST tax lifetime exclusion is $11,180,000 per taxpayer

The *Tax Cut and Jobs Act* of December 2017 increased the amount that a U.S. citizen or resident can transfer to another individual free of estate, gift or Generation-Skipping Transfer taxes (collectively, the “transfer taxes”).

What is the transfer tax exemption for 2018?

The lifetime exemption amount for all three transfer taxes is computed with reference to a base amount of $10,000,000 per taxpayer plus an annual inflation adjustment. The inflation adjustment is determined yearly by the Internal Revenue Service. On March 2, 2018, the IRS announced that the 2018 transfer tax exemption amount is $11,180,000.

The tax rate applicable to transfers above the exemption is currently 40%.

What does the sunset provision of the Act mean?

The Tax Cuts and Jobs Act provided that the higher exemption levels are effective through 2025, and revert to prior law (with the exception of retaining the formula for computing the inflation adjustment) on January 1, 2026.
Unless the tax law changes between now and then, the exemption amount per taxpayer will be back to $5,000,000, plus the inflation adjustment, on January 1, 2026.

How has the federal transfer tax exemption amount changed over the years?

The transfer tax exemptions (and the highest marginal transfer tax rates) have undergone several sweeping changes in the last two decades. The exemption amounts have been fully unified only since 2011.

Since 1997, the estate, gift tax and Generation-Skipping Transfer tax lifetime exemption amounts have changed as follows:

	Estate & Gift* lifetime exemption:	GST lifetime exemption:
1997	$600,000	$1,000,000
1998	$625,000	$1,000,000
1999	$650,000	$1,010,000
2000	$675,000	$1,030,000
2001	$675,000	$1,060,000
2002	$1,000,000	$1,100,000
2003	$1,000,000	$1,120,000
2004–2005*	$1,500,000	$1,500,000
2006–2008*	$2,000,000	$2,000,000
2009*	$3,500,000	$3,500,000
2010*	$5,000,000**	***
2011	$5,000,000	$5,000,000
2012	$5,120,000	$5,120,000
2013	$5,250,000	$5,250,000
2014	$5,340,000	$5,340,000
2015	$5,430,000	$5,430,000
2016	$5,450,000	$5,450,000
2017	$5,490,000	$5,490,000
2018	$11,180,000	$11,180,000

Notes: * Between 2002 and 2010, the lifetime exclusion for gifts was capped at $1,000,000

**In 2010, estates had the option to choose between a "no estate tax" system that afforded limited step-up in tax cost for the decedent's assets, or a $5,000,000 federal estate tax exemption with full step-up in tax cost.

***In 2010, the GST tax exemption was $5,000,000, but the GST tax rate was 0.

How does the gift tax annual exclusion work with the lifetime exemption?

The gift tax annual exclusion, which is also adjusted for inflation and set by the IRS annually, allows taxpayers to make certain gifts without eroding the taxpayer's lifetime exemption amount. For more on the gift tax annual exclusion, click here.

What does this mean for you?

The changing landscape of the federal transfer taxes has led to challenges and opportunities in estate planning. In view of the recent changes and the scheduled sunsetting of the estate, gift and Generation-Skipping Transfer tax exemption amounts, please consult with your Nixon Peabody LLP attorney about your estate plan.
— *Sarah M. Richards*

Two Provisions in the Tax Reform Bill enhance savings options for those with ABLE accounts

In 2014, Congress created 529 ABLE accounts via the passage of the Achieving a Better Life Experience (ABLE) Act. As a result of the new Tax Cuts and Jobs Act signed into law by President Trump on December 22, 2017, ABLE accounts now have greater flexibility when it comes to planning for those with special needs.

As we discussed in one of our previous posts, ABLE accounts allow individuals with disabilities or their families to set aside money in tax-advantaged savings accounts for disability-related expenses, while remaining eligible for means-tested government benefits such as Medicaid or Social Security benefits. Individuals who accumulate less than $100,000 in these accounts will not jeopardize any sort of government benefit, while Medicaid eligibility is not affected by any amount of funds in the account. However, total annual contributions for a single individual's account may not exceed the annual gift tax exclusion ($15,000 in 2018).

A new provision in the tax bill (Section 11024), which has been sought by advocates since 2016, allows beneficiaries of ABLE accounts who earn income from employment to make additional contributions above the $15,000 annual cap—up to the lesser of the beneficiary's compensation for the year or the federal poverty level, which is currently $12,060 for an individual. However, this applies only to individuals who do not participate in their employer's retirement plan.

The other new provision (Section 11025) allows families who have accumulated funds in a 529 savings account benefiting a disabled individual's education, to roll over to an ABLE account an amount not to exceed the overall contribution limit (currently $15,000 a year). Both accounts must have the same beneficiary or an immediate family member as the beneficiary (for example, moving assets from one child's 529 account to another child's ABLE account is now allowed).

With ever-increasing expenses needed to support those with special needs, these two new provisions offer the ability to further improve the lives of disabled individuals and their families, while reducing the constant stress and worry that so many of them experience.—*Thomas A. Stedman*

Income Taxes

2017 traditional IRA contributions allowed until April 17, 2018

Even if you did not make a contribution to your traditional individual retirement account (IRA) in 2017, you may still be able to make a 2017 contribution to your traditional IRA

When can contributions be made to an IRA?

Contributions can be made to traditional IRAs at any time during the calendar year or by the due date for filing your federal income tax return for that year (not including extensions).

What is the last date that a traditional IRA contribution can be made as a 2017 contribution?

April 17, 2018 is the last date that you can make a contribution to a traditional IRA for it to be treated as a 2017 contribution.

What is the traditional IRA contribution limit for 2017?

Generally, eligible taxpayers can contribute up to $5,500 to a traditional IRA for 2017. If the taxpayer is over 50 years of age (by the end of 2017), the limit is increased from $5,500 to $6,500.

However, if a taxpayer is covered by a workplace retirement plan, then the deduction for a contribution to a traditional IRA may be reduced depending on the taxpayer's filing status and adjusted gross income. See Publication 590-A for determining contribution and deduction amounts.

Is there an age limit for contributions to a traditional IRA?

Taxpayers cannot make contributions to a traditional IRA in the year in which they reach 70 ½ and subsequent years.

— *Mary-Benham B. Nygren*

Tax benefits for parents

For those that choose this path, being a parent offers a multitude of benefits. The love and compassion you share with your children are feelings like no other, despite the tough times and hard work that come along with the job. Aside from the "feels," parents may also be eligible for certain tax benefits. The good news is that most of the credits available to parents remain unchanged with the Tax Cuts and Jobs Act (TCJA) signed into law in December 2017, and some even got better.

Claim Dependents

Hurry! Don't wait! The personal exemption will only be available for your 2017 income tax returns, as it was recently suspended with TCJA. For now, parents are eligible for a $4,050 per person exemption for themselves and their children that qualify and are claimed as dependents. For example, if you are married filing a joint return (MFJ) and have three minor children, you may be able to claim personal exemptions of $20,250 in 2017 ($4,050 x 5 = $20,250), which means your taxable income will be reduced by this amount. However, for MFJ returns, a phase-out of personal exemptions begins when income exceeds $313,800. Starting in 2018, personal exemptions will be suspended through 2025.

Child and Dependent Care Credits

If you have children under 13 and you pay someone to watch them so you can work (or look for work), you may be able to claim a dependent care credit. The credit also applies for the care of persons over the age of 13 (including adults) who are unable to care for themselves, so long as they qualify as your dependent for purposes of the credit. Up to $3,000 in expenses for one dependent may be eligible for the credit (or up to $6,000 for two or more dependents), and a percentage rate is applied depending on your income level (subject to phase-out limitations). These credits are unchanged under TCJA.

Education Credits

For parents paying the college expenses of their children, you may be eligible to claim the American Opportunity Tax Credit (AOTC) or the Lifetime Learning Credit (LLC). The AOTC offers a credit of up to $2,500 per eligible student for the first four years of higher education. The AOTC is completely phased out at $90,000 for single filers and $180,000 for

MFJ filers.

The LLC offers a credit of up to $2,000 per tax return for qualified tuition and related expenses paid for undergraduate, graduate and other professional degree courses for dependents. There is no limit to the number of years the LLC may be claimed. In 2017, the LLC is completely phased-out at $66,000 single/$132,000 MFJ. Note that the LLC and AOTC cannot be claimed in the same tax year for any one student. Both credits are unchanged under TCJA.

Child Tax Credit

For 2017, parents may claim $1,000 per qualifying child under the age of 17. The phase-out starts at $75,000 for single taxpayers and $110,000 for MFJ taxpayers. Starting in 2018 (through 2025), the credit increases to $2,000 per child, and the phase-out begins at $200,000 single/$400,000 MFJ.

Adoption Credits

For parents who adopted a child in 2017, a maximum credit of $13,570 per child is available for qualified adoption expenses paid. The guidelines for claiming this credit are a bit more in-depth, so you should reach out to your tax advisor for assistance if you've paid adoption expenses in the last year. There were no changes to this credit under TCJA.— *Andrea M. Ells*

Deducting charity-related travel expenses

Taxpayers often wonder if they may deduct some of their expenses when they are traveling to take part in charitable activities. As with anything connected with individual income taxes, the easy answer is yes and no!

DEDUCT: Charitable contributions may be claimed as an income tax deduction if the taxpayer itemizes deductions on Schedule A. Given the increase in the standard deduction for 2018 ($12,000 for single filers and $24,000 for joint filers), many taxpayers may not itemize and consequently may not be able to claim a deduction for charitable contributions.

DEDUCT: The charity for which the taxpayer is volunteering must be recognized by the IRS as a qualified charity (churches are generally qualified and do not need to apply to the IRS). If the taxpayer is not sure of the charity's status, the "Exempt Organizations Select Check" tool at www.IRS.gov contains a searchable database of qualified charities.

DEDUCT: The charitable work has to be "real and substantial" throughout the trip for expenses to be deducted. The taxpayer may not deduct expenses if not engaging in charity-related activities for significant parts of the trip.

DEDUCT: The taxpayer may deduct travel expenses that are unreimbursed, directly connected with the charitable work and incurred only because the taxpayer was engaged in charitable work while traveling.

DEDUCT: Types of expenses the taxpayer may deduct include air, rail and bus transportation; car expenses; meals; lodging; and transportation costs between airport/station and hotel.

CAN'T DEDUCT: Taxpayers may not deduct the value of time or services given to the charity. In addition, taxpayers may not deduct income lost while volunteering for the charity.

CAN'T DEDUCT: Taxpayers may not deduct personal, living or family expenses. Also, taxpayers may not deduct their travel expenses if a major part of the trip involves recreation or vacation.

As always, it's best to consult with a tax professional to determine if you may deduct your charity-related travel expenses.— *Mary M. Paul*

If you serve in the armed forces, you are eligible for special tax breaks!

Members of the military make many sacrifices. One thing they shouldn't have to worry about is an undue tax burden while they serve our country. Here are some tax breaks that may apply for those in the military:

1. **Combat Pay Exclusion**

If you serve in a combat zone or provide direct support for one, your combat pay may be partly or fully tax-free. This applies to basic pay, reenlistment bonuses, school loan repayments, imminent danger/hostile fire pay, discharge benefits and/or other financial incentives. Keep in mind that there are limits for commissioned officers.

Note that the Tax Cuts and Jobs Act of 2017 retroactively provides that a qualified hazardous duty area is treated in the same manner as a combat zone. Specifically, the Sinai Peninsula of Egypt is determined to be a qualified hazardous duty area for an applicable period (generally for tax years ending after June 9, 2015). This may create an opportunity for some members of the military to file an amended return to claim a refund.

2. **Deadline Extensions**

Certain military members can postpone their tax deadlines. This could result in an automatic extension of time to file your tax return and pay taxes. The deadline is generally extended 180 days after the last day you are in a combat zone or serve in a contingency operation (or the last day of hospitalization as a result of such duty). Among other items, this also extends the deadline to claim a refund or make an IRA contribution. During time in a combat zone, the IRS will also suspend any compliance actions including audits or collection matters.

3. **Signing Joint Returns**

Both spouses must usually sign a joint tax return, but if your spouse is in a combat zone you can sign for them. If your spouse is overseas, you can obtain a power of attorney to sign on their behalf.

4. **Earned Income Tax Credit (EITC)**

If you receive nontaxable combat pay (see #1 above), you may elect to include it in your taxable income in order to increase the amount of the EITC. This could result in a larger refund for you in certain cases, so take the time to compute the credit both ways before you make a decision.

5. **Moving Expenses Deduction**

Unreimbursed moving costs may be deductible on Form 3903 when a move is due to a permanent change of station. Note that the Tax Cuts and Jobs Act temporarily suspends the moving expense deduction for all other taxpayers (i.e., non-military taxpayers) for tax years beginning after December 31, 2017 and before January 1, 2026.

6. **Reservists' Travel Deduction**

If you have to travel more than 100 miles away from home as a reservist, unreimbursed travel expenses may be deductible on Form 2106 even if you don't itemize your deductions. This is an above-the-line deduction for expenses that do not exceed the federal per diem rate, plus standard mileage rate, parking fees, and tolls.

7. **Uniform Deduction**

If you have costs related to uniforms that you aren't allowed to wear while off duty, then you can deduct those costs. You must reduce the deduction by any allowance you receive to purchase the uniforms. The deduction is considered to be a miscellaneous itemized deduction. Note that the Tax Cuts and Jobs Act of 2017 disallows all miscellaneous itemized deductions for any tax year beginning after December 31, 2017 and before January 1, 2026.

8. **ROTC Allowances**

Certain payments to ROTC students in advanced training are not taxable (i.e., allowances for education and subsistence). Active duty ROTC pay is taxable, however.

9. **Transition to Civilian Life**

Keep in mind that you may be able to deduct expenses related to job searches, including travel, résumé and job placement fees. Moving expenses may also be deductible. Note that the Tax Cuts and Jobs Act of 2017 disallows all miscellaneous itemized deductions for any tax year beginning after December 31, 2017 and before January 1, 2026.

10. **Sale of Principal Residence**

The Military Family Tax Relief Act provides eased requirements for the gain exclusion on the sale of a primary residence ($250,000 for individuals and $500,000 if you are married filing jointly). A member of the military on extended duty (a period of 90 days or more) may suspend for up to 10 years the running of the five-year ownership and use period before the sale. Qualified extended duty must be either at a duty station more than 50 miles from your home or while you live in government quarters under orders.

11. **IRA Contributions**

Even though you don't include combat pay in gross income (see #1 above), you do include it in your compensation to determine IRA contribution limits and deductibility.

12. **Maximum Interest Rate for Hardship**

The maximum interest rate you can be charged is 6% per year for liabilities incurred before you joined the military if your service materially impacts your ability to pay them. This rate only applies to interest charged during your military service.

Other Resources

For more information on these tax breaks and other matters related to members of the armed forces, please refer to IRS Publication 3, Armed Forces' Tax Guide. You may also visit the IRS website at www.irs.gov/individuals/military for more information. Many military bases offer free tax preparation and filing assistance during tax season or throughout the year.— *Daniel N. Jones*

What is the child tax credit?

Depending on their modified adjusted gross income (MAGI), taxpayers with one or more qualifying children may be able save up to $1,000 per child by claiming the child tax credit on their federal income tax return. This is a dollar-for-dollar reduction of the tax bill.

A qualifying child for the child tax credit:

• must be claimed as a dependent on the taxpayer's federal tax return
• must be the taxpayer's:
  o son, daughter, stepchild, foster child or descendant of any of them
  o brother, sister, stepbrother/sister, half-brother/sister or descendant of any of them
  o adopted child or foster child lawfully placed by the court or an authorized agency
• must not have attained the age of 17 by the end of the current tax year
• must have lived with the taxpayer for more than half the tax year
• must not have provided more than half of their own support
• must be a U.S. citizen, U.S. national or U.S. resident alien
• must not have filed a joint return unless the reason for filing is to claim a refund

How does the credit work?

• The credit gets "phased out" as your MAGI increases. You will get $50 less in child tax credits for every $1,000 or portion thereof that your MAGI exceeds:
  o $75,000 for head of household, single or qualifying widow/widower taxpayers
  o $110,000 for married filing joint taxpayers and $55,000 for married filing separate taxpayers
• The credit is generally limited to regular tax liability plus alternative minimum tax liability (nonrefundable meaning if no tax liability then no child tax credit)
• Certain taxpayers who owe no tax and received less than the full child tax credit ($1,000 per child) may claim the Additional Child Tax Credit and receive a refund

Child Tax Credit in 2018

For 2018, the Child Tax Credit has been expanded, which may compensate for the loss of personal exemptions:

• Credit is increased from $1,000 to $2,000 for a qualifying child with a valid social security number

• A non-refundable credit is allowed for each dependent who is not a qualifying child and no social security number is required (e.g., grandmother, mother-in-law)
• Refundable portion limited to $1,400, indexed for inflation
• Maximum refundable credit limited to 15% of earned income above $2,500
• The credit gets "phased out" as your MAGI increases. You will get $50 less in child tax credits for every $1,000 or portion thereof that your MAGI exceeds:
o $200,000 for head of household, single, qualifying widow/widower or married filing separate taxpayers
o $400,000 for married filing joint taxpayers

— *Alyson Stevenson*

Wealth Management

Market Pulse: March Economic Highlights

What's happening: Highlights from the NP Investment Team

The head of the WTO has stated that a full-fledged trade war between China and the U.S. would have a "severe impact on the global economy." What is driving the U.S. to make these changes to trade policies and how much authority does the President have to implement these changes?

President Trump believes a trade deficit is equivalent to theft and the U.S. deficit with China has ballooned to $337bln in recent years. The President considers winning a trade war to be easy and has broad authority to implement changes unilaterally. The recently proposed tariffs on $60bln worth of Chinese goods announced last week is not material enough to derail the global economy. However, should China retaliate and a full-scale trade war follows, there will be more losers than winners.

Leaders and Laggards: What's Up and Down in the U.S. Stock Market?

ECONOMIC SECTORS	MARCH 2018 THROUGH 3/28/2018	YEAR-TO-DATE 2018 (THROUGH 3/28/18)
Utilities	2.87%	-4.7%
Energy	-0.59%	-8.6%

Telecommunications	-1.12%	-8.7%
Consumer Staples	-1.97%	-8.4%
S&P 500	-4.01%	-2.6%
Technology	-5.99%	1.0%
Materials	-6.21%	-7.7%

Risk-off ("defensive") sectors, including Utilities, Telecommunications and Consumer Staples, have outperformed the overall market for the month of March. Many of the companies/stocks in these sectors are domestically focused (revenues and earnings) and, therefore, relatively insulated from potential trade/tariff issues. At the same time, these companies will likely benefit more from the domestic fiscal stimulus (tax cuts and budget deal) than multi-national companies. As the stock market stalls, bond investments and their proxies (Utilities, Telco and Staples) offer a relative safe haven compared to more cyclical parts of the market.

Conversely, economically sensitive and global companies have struggled as the fear of a trade war becomes reality. The global synchronized growth narrative that has driven recent sector leaders like Technology, Materials and Industrials to highs is at risk of reversing given recent tariff rhetoric. Headline risk, along with macro (trade) risk has also driven Technology stocks lower as regulatory concerns (Facebook, etc.) mount.

Click here for more information about NP's investment capabilities.

— *NP Investment Department*

For more information, please contact:

- Kaitlyn Barnett at kbarnett@nixonpeabody.com or 617-345-6127
- Sarah T. Connolly at sconnolly@nixonpeabody.com or 617-345-6075
- Andrea M. Ells at aells@nixonpeabody.com or 585-263-1016
- John L. Garrett at jgarrett@nixonpeabody.com or 585-263-1271
- Daniel N. Jones at djones@nixonpeabody.com or 585-263-1101
- Evelyn V. Moreno at emoreno@nixonpeabody.com or 617-345-6157
- Mary-Benham B. Nygren at mnygren@nixonpeabody.com or 617-345-6165
- Mary M. Paul at mmpaul@nixonpeabody.com or 585-263-1371
- Sarah M. Richards at srichards@nixonpeabody.com or 617-345-6082

- Sarah M. Roscioli at sroscioli@nixonpeabody.com or 617-345-1045
- Jay D. Rosenbaum at jrosenbaum@nixonpeabody.com or 617-345-1269
- Thomas A. Stedman at tstedman@nixonpeabody.com or 585-263-1029
- Alyson Stevenson at astevenson@nixonpeabody.com or 585-263-1262

NP TRUST & ESTATES BLOG

Achieving success in estate planning, wealth management and tax minimization.