WILMINGTON TRUST

2017 Tax Cuts and Jobs Act

May 2018

2017 Tax Cuts and Jobs Act

The most significant changes in tax law—since the 1986 tax reform—were enacted in December 2017. The following charts detail the provisions most relevant to high income and high-net-worth taxpayers.

Significant Provisions of the Act

Most of the provisions of the Act are effective for tax years beginning after 2017, with many of the individual income tax provisions expiring after 2025.

Individual income tax highlights

- The Act replaces the current seven individual tax brackets with rates ranging from 10% to 37%
- The Act nearly doubles the standard deduction for taxpayers and eliminates personal exemptions
- Itemized deductions are mainly limited to home mortgage interest; state and local income, sales, and property taxes; and charitable contributions
  - The Act limits the deductions for state and local income, sales, and property taxes to $10,000
  - The Act retains the home mortgage interest deduction for new mortgages for principal and second residences, but limits the interest deduction to a $750,000 mortgage. The deduction for home equity interest is eliminated
  - The Act slightly increases the allowable deduction for cash contributions to public charities and otherwise retains the current charitable contribution deduction rules
- For divorce decrees and separation agreements entered into after 2018, alimony would no longer be deductible by the payor and would not be taxable to the payee
- The Act retains the individual alternative minimum tax (AMT) with increased exemption amounts
- The Act contains many other provisions that affect numerous other deductions and credits for individuals
- The Act repeals the individual mandate of the Affordable Care Act
- The Act changes the method for calculating inflation indices so amounts indexed for inflation will grow more slowly

Significant Provisions of the Act

Continued

Wealth transfer tax highlights	• The Act retains the estate, gift, and generation-skipping transfer (GST) tax and doubles the exemptions for the period 2018-2025 • Heirs will continue to have a fair market value basis in inherited assets, and the gift tax remains in place • Portability of a deceased spouse's unused exemption is retained
Corporate and business tax highlights	• The Act reduces the corporate tax rate to a flat rate of 21% • The Act provides a deduction of 20% of qualified business income from a partnership, S-Corporation, or sole proprietorship, which results in an effective top rate of 29.6%, subject to a phase-out • The Act allows 100% first-year expensing of certain depreciable assets for assets placed in service by September 27, 2017, along with a limitation on interest expense deductions • The Act increases Section 179 expensing limits • The Act repeals the corporate AMT • The Act limits net operating loss deductions • The Act imposes a one-time repatriation tax of 15.5% on earnings and profits (liquid) and 8% on illiquid
Provisions with no changes	• No change made to the specific identification method for sale of stock (or donative transfers to family or charity), so transfers of stock are not required to be made on a first-in, first-out (FIFO) basis • The contribution limits for IRAs and 401(k) plans are unchanged • The Act does not change the capital gains tax, net investment income tax, or Medicare surtax

Strategic Wealth Planning Under the New Tax Law

The Act is voluminous and complex, and attorneys, accountants, financial advisors, and taxpayers will be grappling with its impact for many months. But we do see some emerging themes and opportunities to consider in 2018.

Estate tax planning

For individuals with assets greater than the 2017 exemption amount ($5,490,000), the Act now creates an opportunity to shelter almost double that amount from federal estate, gift, and GST taxes

- For individuals who have already created an irrevocable trust, using the exemption can be as easy as adding to the existing trust
- The additional exemption can be used to add to or create a variety of trusts, including long-term dynasty trusts, spousal lifetime access trusts, and life insurance trusts
- In some cases, the exemption can be used to fund a Delaware self-settled domestic asset protection trust
- The Act particularly encourages lifetime gifts, as a way to take advantage of the increased exemption, as the increased exemption is scheduled under the Act to expire after 2025. In 2026, the exemption will drop to $5,490,000, as adjusted for inflation
- The use of the additional exemption amount can be leveraged through techniques, such as sales to intentionally defective grantor trusts, taking advantage of the current low interest rate environment
- Lifetime gifts that use the exemption amount can be made without any federal transfer tax cost, and they also have the advantage that future appreciation of the assets is also outside the taxable estate

Strategic Wealth Planning Under the New Tax Law

Continued

Income tax planning with trusts

Although the Act lowered income tax rates, it also eliminated or limited many deductions, including the state and local income and property tax deduction (SALT). As taxpayers become more sensitive to the costs of state and local taxes (now limited to a $10,000 deduction), there may be some income tax planning opportunities.

- A Delaware Incomplete Non-Grantor Trust ("DING Trust") can be an attractive vehicle to minimize state tax earned by the trust. The DING Trust provides for some interest, dividends, and capital gains to be taxed in another jurisdiction that has no state income tax on trust assets. Delaware does not tax this type of income that is held in a DING Trust if the beneficiaries are not residents of Delaware. The creation and funding of the DING can be accomplished without using any of the gift tax exemption
- Take a look at existing grantor trusts that were created so that the creator of the trust is taxed on the income of the trust. One way to reduce state income taxes is to "turn off" the grantor trust feature of a grantor trust. By removing this feature from an existing trust so that it becomes a non-grantor trust, the trust becomes its own taxpayer. With the new higher estate tax exemptions, some of the pressure on estate tax minimization may be relieved. If the trust is administered in a tax-friendly state such as Delaware, it may be possible to turn off payment of state taxes on the trust's income
- Irrevocable trusts can be specifically drafted to grant an individual the power to swap assets of the trust with assets that the grantor holds individually. Low cost basis trust assets can be substituted for high cost basis assets held by the grantor individually. The low cost basis assets now held by the grantor would be eligible for a step up in basis upon the grantor's death

(continued)

Strategic Wealth Planning Under the New Tax Law

Continued

Income tax planning with trusts (continued)	• With the reduction of the corporate tax rate and the enactment of a new deduction for pass-through entities, business owners should reexamine whether it is more beneficial to operate a C corporation than a pass-through entity. Owners should revisit their operating structures and, if appropriate, change their type of entity. They should also consider taking advantage of the increased gifting exemption to move assets into trust • Another way to reduce state income taxes would be to establish residency in a state that does not have a state income tax. This might be available to taxpayers who already spend a significant amount of time in a non-tax state, such as Florida
Charitable planning	Although the Act eliminated or dramatically reduced most itemized deductions, it retained the charitable contribution deduction. The deduction for cash contributions to public charities was even enhanced, permitting cash contributions up to 60% of adjusted gross income, rather than 50% under prior law. However, for many donors the tax advantages of charitable giving will be impacted by rate reductions and other changes. As a consequence of the increased standard deduction and the elimination of many itemized deductions, many donors will no longer be able to itemize deductions, losing many (but not all) of the tax incentives for charitable giving. But for those donors who can still itemize, itemized deductions are no longer subject to the itemized deduction phase-out. And for very high-net-worth donors who are still subject to the federal or state estate tax, the charitable deductions from estate, gift, and generation-skipping transfer tax still apply (continued)

Strategic Wealth Planning Under the New Tax Law

Continued

Charitable planning (continued)

For donors who still itemize

- Lifetime charitable gifts made outright to public charities, private foundations, and donor advised funds can provide both income and estate tax advantages
- Gifts can also be structured to benefit both family and charity through charitable remainder and lead trusts, and for smaller gifts, charitable gift annuities
- Gifts can be made even more tax efficient by donating appreciated property, such as publicly traded stock and, in some cases, closely held businesses and collectibles

For donors who can no longer itemize

- A donor over age 70½ can take advantage of the special rule permitting up to $100,000 of IRA distributions directly to a qualified charity. This has the same impact as a charitable deduction, because the amount of the IRA distribution to charity is not included in income
- While not generating a deduction for non-itemizers, gifts of appreciated property still save the capital gains taxes that would have been due if the asset were sold. For low basis assets, that can still provide significant tax savings
- Some donors will be able to bunch their deductions, making larger deductible gifts every few years, possibly into a donor advised fund

Federal Income Tax—Individuals

	Law in 2017	Tax Cuts and Jobs Act
Rates on ordinary income	Seven brackets: 10%, 15%, 25%, 28%, 33%, 35%, and 39.6% for income above $418,400 (single); $444,550 (head of household); $470,700 (married); $235,350 (married filing separately); Indexed for inflation	Seven brackets:10%, 12%, 22%, 24%, 32%, 35%, and 37% for income above $500,000 (single); $500,000 (head of household); $600,000 (married); $300,000 (married filing separately); Indexed for inflation after 2018 Reverts to current law after 2025
Standard deduction	$6,350 (single and married filing separately); $9,350 (head of household); $12,700 (married); Indexed for inflation Additional standard deduction for elderly and the blind	$12,000 (single and all other taxpayers); $18,000 (head of household); $24,000 (married); Indexed for inflation after 2018 Reverts to current law after 2025 Retains current additional standard deduction for elderly and the blind
Itemized deductions and personal exemption	• State and local property taxes fully deductible; state and local income tax or sales tax fully deductible • Home mortgage interest deduction for up to two residences, $1,000,000 debt limit; $100,000 debt limit for home equity • Charitable contribution deductions for cash gifts to public charities up to 50% of AGI • Allows medical expense deduction for expenses in excess of 10% of AGI • Allows student loan interest deduction • Personal exemption $4,050/person • Itemized deductions phase-out for adjusted gross income (AGI) over $261,500 (single); $313,800 (married)	• Limits combined deductions for state and local income, sales and property taxes to $10,000 • Limits home mortgage interest deduction for new mortgages from 2018-2025 to $750,000 of indebtedness (grandfathers existing mortgages and some refinancings); repeals deduction for home equity interest unless used to purchase or improve home • Increases charitable contribution deduction for cash gifts to public charities to 60% of AGI • Retains medical expense deduction for expenses in excess of 7.5% of AGI for 2017 and 2018. Reverts to 10% in 2019 • Eliminates miscellaneous itemized deductions subject to 2% floor • Retains investment interest deduction • Eliminates personal casualty loss except for disasters • Eliminates tax preparation expense • Eliminates investment fees and expenses • Retains student loan interest deduction • Eliminates personal exemption • Eliminates the itemized deduction phase-out Reverts to current law after 2025

Federal Income Tax—Individuals

Continued

	Law in 2017	Tax Cuts and Jobs Act
Alternative minimum tax (AMT)	26% and 28% rates, with exemption amount of $54,300 (single); $84,500 (married); $42,250 (married filing separately); $24,100 (Trusts); Indexed for inflation	Increases exemption amount to $70,300 (single); $109,400 (married); $54,700 (married filing separately) Exemption phases out at $1,000,000 (married); $500,000 (all others) Indexed for inflation after 2018 Reverts to current law after 2025
Trust income tax	15%, 25%, 28%, 33%, and 39.6% for estate or trust income over $12,500	10%, 24%, 35%, and 37% for estate or trust income over $12,500
Like-kind exchanges	Tax-deferred exchanges of like-kind property permitted for real property and tangible personal property held for use in a trade or business or investment	Tax-deferred exchanges of like-kind property limited to real property not held primarily for sale
Alimony deduction	Above-the-line deduction for payor; included in the recipient's income	Eliminates deduction for payor; not treated as taxable income to recipient; applies to divorce and separation agreements after 2018
Section 529 Plans	Allows 529 Plans for higher education; allows Coverdell savings accounts	Permits distributions of $10,000 per year for elementary and secondary schools Allows rollover to ABLE accounts
Affordable Care Act – individual mandate	2.5% of AGI up to $2,085 maximum	Eliminates after 2018

Federal Income Tax—Individuals

Continued

	Law in 2017	Tax Cuts and Jobs Act
Accounting methods for sale and other transfers of stocks	Specific identification method allowed in computing capital gains on sale or transfer of part of a stock holding	No change
Retirement accounts – 401(k)	No limit on lifetime contributions; $18,000 maximum annual contribution; over age 50 may make annual catch up contribution of $6,000, as indexed for inflation	No change
Gain on sale of principal residence	May exclude gain on the sale of principal residence up to $500,000 (married); may be used every 2 years; must be principal residence for 2 of the 5 previous years	No change
Rates on capital gains / dividends	Top rate of 20% 1-year holding period	No change
Surtax on net investment income	3.8%, above $200,000 AGI (single); $250,000 (married); Trusts with income over $12,500	No change

Federal Transfer Taxes

	Law in 2017	Tax Cuts and Jobs Act
Estate tax rate and exemption	Top tax rate of 40% $5,490,000, as adjusted for inflation	Retains estate tax Increases exemption to $10,000,000, indexed for inflation after 2011, approximately $11,200,000 for 2018 Reverts to current law after 2025
Lifetime gift tax rate and exemption	Top tax rate of 40% $5,490,000, as adjusted for inflation	Retains gift tax Increases exemption to $10,000,000, indexed for inflation after 2011 Reverts to current law after 2025
Generation-skipping transfer tax rate and exemption	Flat rate of 40% $5,490,000, as adjusted for inflation	Retains generation-skipping transfer tax Increases exemption to $10,000,000, indexed for inflation after 2011 Reverts to current law after 2025
Portability of estate and gift tax exemption	Unused exemption of deceased spouse available (with limitations)	No change
Basis of inherited assets	Stepped up to fair market value at death	No change
Gift tax annual exclusion	$14,000 per donee as indexed for inflation	No change in law $15,000 per donee for 2018 as indexed for inflation

Federal Income Tax—Business

	Law in 2017	Tax Cuts and Jobs Act
Corporate income tax	Top rate of 35% Flat 35% rate for personal service corporations	Top rate of 21% beginning after 2017 Eliminates the special rate for personal service corporations
Pass-through business income from small businesses (such as Sole Proprietorships, Partnerships, LLCs, and S-Corporations)	Top rate of 39.6%	Allows a deduction equal to 20% of qualified business income which results in an effective top tax rate of 29.6%, with trusts and estates eligible for the 20% deduction Deduction limits based on specific service income and on W-2 wages and capital, phased in at $315,000 (married) Reverts to current law after 2025
Taxation of carried interest	Taxed as capital gains; requires one-year holding for capital gain treatment	Requires three-year holding period for capital gain treatment
International tax	Worldwide tax system	Territorial tax system implemented through 100% exemption for certain foreign source dividends One-time tax on liquid (15.5%) and illiquid (8%) earnings and profits Tax imposed on base erosion payments

Federal Income Tax—Business

Continued

	Law in 2017	Tax Cuts and Jobs Act
Business interest expense	Allowed as a deduction, subject to a number of limitations	Restricts to 30% of adjusted taxable income, business income interest, and floor plan financing interest Businesses with average annual revenue of $25,000,000 or less exempt from limit
Depreciation and expensing	May take additional depreciation in the year property is placed into service; 50% of the cost of qualified property in 2017	Immediately expense 100% of the cost of qualified property acquired after September 27, 2017 Bonus depreciation rates phase-out after January 1, 2023 by 20% per year
Corporate AMT	20% on income greater than the $40,000 exemption; exemption phase-out starting at income greater than $150,000 Corporations with average gross receipts of less than $7.5 million for the preceding three tax years are exempt	Eliminates
Net operating loss deduction	Deduction for losses in excess of income; may carry back two years and carry forward 20 years (with exceptions)	Limited to 80% of taxable income
Section 179	Allows immediate expense of $500,000; reduced for amounts in excess of $2,000,000	Allows immediate expense of $1,000,000; reduced for amounts in excess of $2,500,000

Federal Income Tax—Charitable

	Law in 2017	Tax Cuts and Jobs Act
Deduction for cash gifts to public charities	Charitable contribution deduction for cash gifts to public charities up to 50% of AGI	Charitable contribution deduction for cash gifts to public charities increased to 60% AGI Reverts to current law after 2025
Private Foundations – excise tax on net investment income	2% excise tax on net investment income, which is reduced to 1% for years in which foundation distributions exceed historic level	No change
Private Foundations – excess business holding rules on business ownership	Private foundations are subject to an excise tax on ownership of more than 20% (35% if no control) of the voting stock, profits interest, or beneficial interest of a business enterprise	No change
Taxation of college and university endowments	Traditional endowment income, such as interest, dividends, capital gains, rents, royalties, and annuities, exempt from tax	1.4% excise tax on net investment income of private colleges and universities meeting an assets and student tuition test

Sources: House of Representatives Committee on Ways and Means, H.R. 1 Tax Cuts and Jobs Act, Conference Report, December 15, 2017. Joint Explanatory Statement of the Committee of Conference, December 15, 2017.

Disclosures

Wilmington Trust is a registered service mark. Wilmington Trust Corporation is a wholly owned subsidiary of M&T Bank Corporation. Wilmington Trust Company, operating in Delaware only, Wilmington Trust, N.A., M&T Bank, and certain other affiliates, provide various fiduciary and non-fiduciary services, including trustee, custodial, agency, investment management, and other services. International corporate and institutional services are offered through Wilmington Trust Corporation's international affiliates. Loans, credit cards, retail and business deposits, and other business and personal banking services and products are offered by M&T Bank, member FDIC.

This presentation is for informational purposes only and is not intended as an offer or solicitation for the sale of any financial product or service. This presentation is not designed or intended to provide financial, tax, legal, accounting, investment, or other professional advice since such advice always requires consideration of individual circumstances. If professional advice is needed, the services of your professional advisor should be sought. Third-party information has been obtained or derived from sources believed to be reliable, but no representation is made as to its accuracy or completeness.

IRS Circular 230 disclosure: To ensure compliance with requirements imposed by the IRS, we inform you that, while this presentation is not intended to provide tax advice, in the event that any information contained in this presentation is construed to be tax advice, the information was not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax related penalties under the Internal Revenue Code or (ii) promoting, marketing, or recommending to another party any matters addressed herein.