HELPING YOU UNDERSTAND THE COMPLEXITIES OF WEALTH MANAGEMENT AND PROVIDING SOLUTIONS AS UNIQUE AS YOUR GOALS

# WEALTH MANAGEMENT NEWSLETTER

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## WHAT ARE THE GIFT AND ESTATE TAX RULES AFTER TAX REFORM?

The Tax Cuts and Jobs Act, signed into law in December 2017, approximately doubled the federal gift and estate tax basic exclusion amount to $11.18 million in 2018 (adjusted for inflation in later years). After 2025, the exclusion is scheduled to revert to its pre-2018 level and be cut approximately in half. Otherwise, federal gift and estate taxes remain the same.

**Gift tax**. Gifts you make during your lifetime may be subject to federal gift tax. Not all gifts are subject to the tax, however. You can make annual tax-free gifts of up to $15,000 per recipient. Married couples can effectively make annual tax-free gifts of up to $30,000 per recipient. You can also make unlimited tax-free gifts for qualifying expenses paid directly to educational or medical service providers. And you can make deductible transfers to your spouse and to charity. There is a basic exclusion amount that protects a total of up to $11.18 million (in 2018) from gift tax and estate tax. Transfers in excess of the basic exclusion amount are generally taxed at 40 percent.

**Estate tax.** Property you own at death is subject to federal estate tax. As with the gift tax, you can make deductible transfers to your spouse and to charity; there is a basic exclusion amount that protects up to $11.18 million (in 2018) from tax, and a tax rate of 40 percent generally applies to transfers in excess of the basic exclusion amount.

**Portability.** The estate of a deceased spouse can elect to transfer any unused applicable exclusion amount to his or her surviving spouse (a concept referred to as portability). The surviving spouse can use the unused exclusion of the deceased spouse, along with the surviving spouse's own basic exclusion amount, for federal gift and estate tax purposes. For example, if a spouse died in 2011 and the estate elected to transfer $5 million of the unused exclusion to the surviving spouse, the surviving spouse effectively has an applicable exclusion amount of $16.18 million ($5 million plus $11.18 million) to shelter transfers from federal gift or estate tax in 2018.



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# DON'T WAIT TO ASK AGING PARENTS THESE IMPORTANT QUESTIONS

It's human nature to put off complicated or emotionally heavy tasks. Talking with aging parents about their finances, health and overall well-being might fall in this category. Many adult children would rather avoid this task, as it can create feelings of fear and loss on both sides. But this conversation—what could be the first of many—is too important to put off for long. The best time to start is when your parents are relatively healthy. Otherwise, you may find yourself making critical decisions on their behalf in the midst of a crisis, without a road map.

Here are some questions to ask them that might help you get started.

## Finances

- What institutions hold your financial assets? Ask your parents to create a list of their bank, brokerage and retirement accounts, including account numbers, name(s) on accounts, and online user names and passwords, if any. You should also know where to find their insurance policies (life, home, auto, disability, long-term care), Social Security cards, titles to their house and vehicles, outstanding loan documents, and past tax returns. If your parents have a safe-deposit box or home safe, make sure you can access the key or combination.
- Do you need help paying monthly bills or reviewing items like credit card statements, medical receipts or property tax bills? Do you use online bill pay for any accounts?
- Do you currently work with any financial, legal or tax professionals? If so, ask your parents if they want to share contact information and whether they would find it helpful if you attended meetings with them.
- Do you have a durable power of attorney? A durable power of attorney is a legal document that allows a named individual (such as an adult child) to manage all aspects of a parent's financial life if the parent becomes disabled or incompetent.
- Do you have a will? If so, find out where it is and who is named as executor. If the will is more than five years old, your parents may want to review it to make sure their current wishes are represented. Ask if they have any specific personal property disposition requests that they want to discuss now.
- Are your beneficiary designations up-to-date? Beneficiary designations on your parents' insurance policies, pensions, IRAs and investment accounts will trump any instructions in their will.
- Do you have an overall estate plan? A trust? A living trust can be used to help manage an estate while your parents are still living. If you'd like to learn more, consult an estate planning attorney.

## Health

- What doctors do you currently see? Are you happy with the care you're getting? If your parents begin to need multiple medical specialists and/or home health services, you might consider hiring a geriatric care manager, especially if you don't live close by.
- What medications are you currently taking? Are you able to manage various dosage instructions? Do you have any notable side effects? At what pharmacy do you get your prescriptions filled?
- What health insurance do you have? In addition to Medicare, which starts at age 65, find out if your parents have or should consider Medigap insurance, which is a private policy that covers many costs not covered by Medicare. You may also want to discuss the need for long-term care insurance, which helps pay for extended custodial or nursing home care.
- Do you have an advance medical directive? This document expresses your parents' wishes regarding life support measures, if needed, and designates someone who will communicate with health care professionals on their behalf. If your parents do not want heroic life saving measures to be undertaken for them, this document is a must.

## Living situation

- Do you plan to stay in your current home for the foreseeable future, or are you considering downsizing?
- Is there anything I can do now to make your home more comfortable and safe? This might include smaller projects such as installing handrails and night lights in the bathroom, to larger projects such as moving the washing machine out of the basement, installing a stair lift or moving a bedroom to the first floor.
- Could you benefit from a weekly or monthly cleaning service?
- Do you employ certain people or companies for home maintenance projects (e.g., heating contractor, plumber, electrician, fall cleanup)?

## Memorial wishes

- Do you want to be buried or cremated? Do you have a burial plot picked out?
- Do you have any specific requests or wishes for your memorial service?

## MIDYEAR PLANNING: TAX CHANGES TO FACTOR IN

The Tax Cuts and Jobs Act (TCJA), passed in December 2017, fundamentally changes the federal tax landscape for both individuals and businesses. Many of the provisions in the legislation are permanent, while others (including most of the tax cuts that apply to individuals) expire at the end of 2025. Here are some of the significant changes you should factor in to any midyear tax planning. You should also consider reviewing your situation with a tax professional.

### New lower marginal income tax rates

In 2018, there remain seven marginal income tax brackets, but most of the rates have dropped from last year. The new rates are 10 percent, 12 percent, 22 percent, 24 percent, 32 percent, 35 percent and 37 percent. Most, but not all, will benefit to some degree from the lower rates. For example, all other things being equal, those filing as single with taxable incomes between approximately $157,000 and $400,000 may actually end up paying tax at a higher top marginal rate than they would have last year. Consider how the new rates will affect you based on your filing status and estimated taxable income.

### Higher standard deduction amounts

Standard deduction amounts are nearly double what they were last year, but personal exemptions (the amount that you could deduct for yourself, and potentially your spouse and your dependents—in 2017, the amount was $4,050) are no longer available. Additional standard deduction amounts allowed for the elderly and the blind remain available for those who qualify. If you're single or married without children, the increase in the standard deduction more than makes up for the loss of personal exemption deductions. If you're a family of four or more, though, the math doesn't work out in your favor.

### Itemized deductions—Good and bad

In the TCJA, the overall limit on itemized deductions that applied to higher-income taxpayers is repealed, the income threshold for deducting medical expenses is reduced for 2018 and the income limitations on charitable deductions are eased. That's the good news. The bad news is that the deduction for personal casualty and theft losses is eliminated, except for casualty losses suffered in a federal disaster area, and miscellaneous itemized deductions that would be subject to the 2 percent adjusted gross income threshold, including tax preparation expenses and unreimbursed employee business expenses, are no longer deductible. Other deductions affected include:

- State and local taxes — Individuals are only able to claim an itemized deduction of up to $10,000 ($5,000 if married filing a separate return) for state and local property taxes and state and local income taxes (or sales taxes in lieu of income).
- Home mortgage interest deduction — Individuals can deduct mortgage interest on no more than $750,000 ($375,000 for married individuals filing separately) of qualifying mortgage debt. For mortgage debt incurred prior to Dec. 16, 2017, the prior $1 million limit will continue to apply. No deduction is allowed for interest on home equity loans or lines of credit unless the debt is used to buy, build or substantially improve a principal residence or a second home.

### Other important changes

- Child tax credit — The credit has been doubled to $2,000 per qualifying child, refundability has been expanded and the credit will now be available to many who didn't qualify in the past based on income; there's also a new nonrefundable $500 credit for dependents who aren't qualified children for purposes of the credit.
- Alternative minimum tax (AMT) — The TCJA significantly narrowed the reach of the AMT by increasing AMT exemption amounts and dramatically increasing the income threshold at which the exemptions begin to phase out.
- Roth conversion recharacterizations — In a permanent change that starts this year, Roth conversions can't be "undone" by recharacterizing the conversion as a traditional IRA contribution by the return due date.

## GOING PUBLIC: AN IPO'S MARKET DEBUT MAY NOT LIVE UP TO THE HYPE

An initial public offering (IPO) is the first public sale of stock by a private company. Companies tend to schedule IPOs when investors are feeling good about their financial prospects and are more inclined to take on the risk associated with a new venture.

Thus, IPOs tend to reflect broader economic and market trends. And not surprisingly, 2017 was the busiest year for the global IPO market since 2007.[1]

Company insiders who have been waiting for the opportunity to cash out may have the most to gain from an IPO. The higher the price set on IPO shares, the more money the company and its executives, employees and early investors stand to make.

The IPO process is important to the financial markets because it helps fuel the growth of young companies and adds new stocks to the pool of potential investment opportunities.

1 Global IPO trends: Q3 2017, Ernst & Young, 2017.

## IPO market trends

Newer, smaller companies have traditionally used IPOs to raise capital for expansion. However, some companies are relying on private capital to fund their early growth and development, so they can wait longer to test public markets. These companies often become larger, more mature and more valuable before they are publicly traded.

This trend may help explain why the amount of money raised through IPOs has increased over the past decade, even as the number of new IPOs has waned. From 2007 to 2016, for example, the number of corporate IPOs averaged 164 per year, down 47 percent from the previous decade. But average annual IPO proceeds rose 82 percent over the same period to $284 million.[2]

A privately held company with an estimated value of $1 billion or more is often called a "unicorn" because of how unusual such success is, and it's estimated that there are now more than 200 of them in the technology sector alone.[3]

Since the term was first coined in late 2013, unicorns have received most of the media's attention, even though they still make up a relatively small part of the IPO market. The proceeds of 18 unicorn IPOs accounted for 5 percent of the capital raised from 2014 through 2016.[4]

## Pop or fizzle

When IPO share prices shoot up on the first day of exchange trading, it's referred to as a "pop." A significant first-day gain may suggest that investor demand for the company's shares was underestimated. Of course, this doesn't mean that the company will outperform its peers in the long run.

One catch is that it is often difficult to obtain "allocated" stock. Investors who don't have the opportunity to buy shares at the offering price—the price at which insiders are selling to the market—can buy the stock after it starts trading on the exchange. However, much of an IPO's pop can take place between its pricing and the first stock trade. This means investors who buy shares after trading starts often miss out on a large part of the appreciation.

Investors who buy IPO shares on the first day might even pay inflated prices because that's when media coverage, public interest and demand for the stock may be greatest. Share prices often drop in the weeks following a large first-day gain as the excitement dies down and fundamental performance measures such as revenues and profits take center stage.

## Back to reality

A young company may have a limited track record, and an established one may have to disclose more information to investors after it becomes publicly traded. If you're interested in the stock of a newly public company, you should have a relatively high risk tolerance because shares can be especially volatile in the first few months after an IPO. You might even consider waiting until you can evaluate at least two quarters of earnings.

The return and principal value of all stocks fluctuate with changes in market conditions. Shares, when sold, may be worth more or less than their original cost. Investments offering the potential for higher rates of return also involve a higher degree of risk.

2 The Global Unicorn Club, CBInsights
3 The Global Unicorn Club, CBInsights
4 Global IPO trends: Q3 2017, Ernst & Young, 2017.