

2017 Tax Act's \$11.2 Million Estate, Gift, and GST Tax Exemption Will Expire In 2025

Tax Section



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The Tax Cuts and Jobs Act of 2017 doubled the unified exemption for the estate, gift, and GST taxes from about \$5.6 million to about \$11.2 million (adjusted yearly for inflation). This dramatic change means for years after 2017, a married couple can gift during life or pass by their death up to \$22.4 million of assets free of transfer taxes. While many high net worth clients are aware of the doubled exemption, it is less well known that this doubled exemption is set to expire on December 31, 2025.

This is not the first time Congress has used a sunset schedule for the unified transfer tax exemption amount. At the end of 2012, taxpayers faced a similar dilemma when it was uncertain whether Congress would act to prevent the automatic reversion of the unified transfer tax exemption from about \$5.12 million to \$1 million. In that case, Congress did act to keep the exemption at \$5.12 million. It is unclear, however, if the same will occur in 2025, particularly given the rhetoric about "taxing the ultra-wealthy" from presidential candidates and Democratic Senators such as Bernie Sanders and Elizabeth Warren. This uncertainty calls for tax planning designed to take maximum advantage of the Tax Act's increased exemption regardless of what may happen at the end of 2025.

At the time of the 2017 Tax Act, it was unclear how taxpayers who used their increased exemption prior to the sunset would be treated should the sunset occur in 2025. The Treasury Department and the IRS reassured taxpayers in proposed regulations (REG-106706-18) that utilization of the new exemption before the sunset will not result in a claw-back upon the sunset. However, these proposed regulations also made it clear that any use of the exemption will first reduce the pre-2017 Tax Act \$5.6 million before beginning to deplete the 2017 Tax Act's \$5.6 million. Thus, a taxpayer who has used none of his or her total \$11.2 million as of 2018 will need to use more than \$5.6 million of the exemption to begin using the

extra amount provided by the 2017 Tax Act. That must be factored in when advising clients about the benefits and risks of utilizing the exemption prior to the 2025 sunset. While a lifetime gift to an irrevocable trust will likely permanently remove the assets from the transfer tax system, using the estate tax exemption will in contrast result in the beneficial basis step-up provided by Section 1014. Regardless, in balancing the pros and cons of these estate planning techniques, it is vital for practitioners and their clients to understand the risks associated with the December 31, 2025 sunset.