The Countdown Begins: Will We Keep the $10 Million Exemption?

The year 2026 is quickly approaching, bringing substantial changes that may affect your estate tax situation. The Tax Cuts and Jobs Act (TCJA) in 2017 significantly increased the federal estate tax exemption to $10 million adjusted for inflation. This is the amount you can gift or leave to your loved ones at your death without incurring a gift or estate tax liability. Any portion of the exemption used during lifetime reduces the total exemption amount available at death for estate tax purposes.

However, the countdown has begun for the potential sunset of this generous exemption by the end of 2025. Adjusting for inflation, the Congressional Budget Office estimates the new exemption amount will be $6.4 million in 2026.[1] There are strong arguments for and against the changes in legislation. Whether the current exemption amount remains or is reduced to roughly $6.4 million, valuable insights from professional advisors can prepare you for either scenario. What is not taxable today might be taxable tomorrow.

History of the Estate Tax Exemption

The federal estate tax was first enacted in 1916 to generate revenue for the government. Over the years, it has undergone various changes in exemption limits and rates.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) gradually increased the estate tax exemption and reduced the tax rate until it reached zero in 2010.[2] However, the estate tax was set to return to the 2001 amounts for deaths occurring in 2011 unless further legislative action was taken.[3] In 2011, the estate tax exemption was reinstated at $5.0 million.[4]

In 2017, the TCJA doubled the estate tax exemption from $5.49 million to nearly $11 million to stimulate economic growth and create jobs.[5] The exemption continues to adjust for inflation, offering individuals an unprecedented opportunity to pass on substantial wealth free from federal estate tax.

The TCJA's Sunset Provision

A sunset provision was embedded within the TCJA to limit how long the higher estate tax exemption could continue. Without legislative intervention, it will be cut in half to $5 million adjusted for inflation in 2026, creating a potential estate planning crisis for people with considerable estates on December 31, 2025. Adjusting for inflation, the Congressional Budget Office estimates the exemption amount will be $6.4 million in 2026.[6]

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[1] *Understanding Federal Estate and Gift Taxes*, Cong. Budget Off., https://www.cbo.gov/publication/57272 (last visited Jan. 2, 2024).

[2] Darien B. Jacobsen et al., *The Estate Tax: Ninety Years and Counting*, SOI Bull. 124, https://www.irs.gov/pub/irs-soi/ninetyestate.pdf (last visited Jan. 2, 2024).

[3] *Id*.

[4] Mark Luscombe, *Historical Look at Estate and Gift Tax Rates*, Wolters Kluwer (Mar. 9, 2022), https://www.wolterskluwer.com/en/expert-insights/whole-ball-of-tax-historical-estate-and-gift-tax-rates.

[5] *Tax Cuts and Jobs Act (TCJA)*, Tax Found., https://taxfoundation.org/taxedu/glossary/tax-cuts-and-jobs-act (last visited Jan. 2, 2024).

[6] *Understanding Federal Estate and Gift Taxes*, *supra* note 1.

If We Keep the Current Estate Tax Exemption

Maintaining or increasing the already high estate tax exemption amount could be seen as a move that benefits the wealthy, broadening the tax burden for others. It can also be seen as maintaining the status quo. And the current law ensures that most people will not be subject to federal estate taxes.

A higher estate tax exemption was expected to foster economic growth and capital investment by allowing wealthier individuals and families to reinvest in businesses and job creation.[7] Yet the federal government relies on estate tax revenue to fund various programs and therefore would not want to reduce a lucrative revenue source. Without the estate tax, other revenue sources would have to foot the bill for these programs and potentially face cuts in the benefits and services provided.

For the estate tax exclusion to remain at the higher amount beyond 2025, Congress will need to take action.

Why the Estate Tax Exemption May Revert Back

The TCJA was part of a short-term tax cut package. Lawmakers had to make room in the budget for the tax cuts introduced by the legislation.[8] They did this by temporarily increasing the estate tax exemption.

Reverting to a lower exemption amount is believed to generate more revenue by increasing the number of people who pay the tax and increasing estate tax exposure to those with net wealth above the current exemption amount. Estate tax revenues are projected to increase sharply after 2025, when the exemption amount is scheduled to drop. From 2021–2031, the combined estate and gift tax revenues are projected to total $372 billion.[9]

Preparing for Potential Estate Tax Changes

As we move into 2024, it is crucial to review estate planning goals and strategies that may be affected by potential changes in the federal estate tax exemption law. By working together with your other trusted advisors, we can reevaluate your current estate plan, investments, and property to ensure that you are protected and your financial legacy is preserved.

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[7] *Id*.

[8] *How Did the Tax Cuts and Jobs Act Change Personal Taxes?*, Tax Pol'y Ctr., https://www.taxpolicycenter.org/briefing-book/how-did-tax-cuts-and-jobs-act-change-personal-taxes (last visited Jan. 2, 2024).

[9] *Understanding Federal Estate and Gift Taxes*, *supra* note 1.