

New estate tax laws

Legislative redux

By Steven A. Schurkman Esq.
Keane & Beane, P.C.
White Plains, N.Y.

Last year at this time, I wrote an article in this Journal titled "Estate Tax Planning in an Uncertain Legislative Environment" in which I outlined several estate tax planning considerations in light of the impending sunset of the estate tax legislation adopted in 2001. One year later we have a legislative response. On Dec. 17, 2010 President Obama signed into law the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (the "Tax Act of 2010"). The Tax Act of 2010 sets forth some new bold initiatives in the estate-planning arena but unfortunately fails to remove the pale of uncertainty for estate planners as the legislation only applies to individuals dying in 2011 and 2012

The Tax Act of 2010 increased the amount, which may be exempted from federal estate tax to \$5,000,000 per person (or \$10,000,000 for a married couple) and reduced the federal estate tax rate on the amount over that exemption from 45 percent to 35 percent. In addition, for the first time in estate tax history, the Tax Act of 2010 allows the surviving spouse to use any unused portion of the estate tax exemption amount of the predeceased spouse as part of the surviving spouse's exemption when such survivor dies. Thus, for example, if a spouse dies after Jan. 1, 2011 and only uses \$3 million of his or her \$5 million estate tax exemption, the surviving spouse may take advantage of the unused \$2 million portion of the estate tax exemption thereby allowing such surviving spouse to automatically have a \$7 million exemption.

In addition, another significant change fostered by the Tax Act of 2010 is that the \$1 million per person gift tax exemption, which existed under the prior law has also been increased to \$5 million per person making the gift and estate tax exemptions unified for the first time in almost 10 years. As a result each person may now make up to \$5 million of gifts before being subject to gift tax. Making gifts over \$13,000 per person per annum will result in a dollar-for-dollar reduction in such donor's estate tax exemption. However,



the ability to make larger gifts without paying up-front gift tax combined with the ability to continue to do minority and other discount planning in a low-interest rate environment will result in the ability to transfer large sums of wealth to succeeding generations without being subject to gift or estate tax.

Simply stated, the lower interest rates fall, the better the environment to transfer assets with little or no gift or estate tax consequences. This is true because many techniques rely on assets outperforming the IRS' rates of return. Two common techniques, which become significantly more valuable in a

low-interest environment are sales to "defective" grantor trusts (IDGTs), and the use of grantor retained annuity trusts (GRATS). In addition to IDGTs

and GRATs, the low IRS rates present real opportunities to allow you to assist your family while shifting wealth between generations with little or no gift tax implications. Intrafamily loans, for example, can provide a significant benefit to a younger generation family member with relatively modest tax implications to the senior generation family member. Not only can intra-family loans be made at rates lower than others commercially available, but the payment terms can be designed to fit the specific needs and resources of the borrower.

However, notwithstanding the significant tax advantages outlined above, as stated previously, unless Congress and the President act prior to Jan. 1, 2013, the Tax Act of 2010 will expire.

One significant adverse consequence of such expiration is that the federal estate tax exemption at that time will return to only \$1 million per person. This fact, combined with the fact that New York state has its own separate estate tax, which only exempts \$1 million per person from estate tax makes it very clear that estate planning documentation must continue to remain very flexible. In particular, planning for married couples may best be accomplished by making sure that at least \$1 million of a family's assets are titled in the ownership of each spouse (and more, if the family's net worth is valued at more than \$5 million) and that Wills or Revocable Trusts be prepared such that decisions about the amount of assets to

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be retained or disclaimed by the surviving spouse can be made at the time of the death of the first spouse.

Thus, in many instances estate planning documents for married couples should state that all assets are bequeathed to the surviving spouse with a further provision that states that if the surviving spouse wants to disclaim a portion of these assets (which decision by law must be made within nine months of the death of the first spouse), such survivor may do so and have such assets not form part of his or her estate for tax purposes. Given that the estate tax laws appear to

be constantly in flux, the use of this type of disclaimer planning would allow a surviving spouse to make a decision as to whether or not to retain assets of the deceased spouse in the context of the prevailing estate tax laws and the family's current financial situation.

In light of the estate tax savings, which can be derived as a result of the Tax Act of 2010 and the potentially short duration of such new tax legislation, it may be appropriate at this time to take a fresh look at your estate planning documents and to discuss proper strategies with your estate planning professional so as to better achieve your objectives while maximizing estate and gift tax savings.