



# The Wealth Advisor

## Highlights of the New Estate Tax Legislation

Volume 5, Issue 1

On December 17, 2010, President Obama signed into law the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "2010 Tax Act"). In a nutshell, it did five things: extended current unemployment benefits to 99 weeks, extended current income tax rates (the Bush tax cuts) for all taxpayers for two more years, made significant changes to the estate tax applicable to those dying in 2010, 2011, or 2012, modified the gift tax for 2011 and 2012, and modified the Generation Skipping Transfer Tax for 2010, 2011, and 2012.

In this issue of *The Wealth Advisor*, we will look at how these temporary changes can affect your estate planning.

### Estate Tax Exemption and Tax Rate

Your estate will have to pay federal estate taxes if its net value when you die is more than the exempt amount in effect at that time. For 2010, 2011 and 2012, the individual exemption is now \$5 million and the tax rate is 35%. So, if someone dies in 2010, 2011 or 2012 and their taxable estate is less than \$5 million, no estate taxes will be due (assuming none of the exemption was used during life to make gifts). If the taxable estate is more than \$5 million, the excess over \$5 million will be taxed at 35%. Those who are married and have planned ahead can use both exemptions (more on this later).

**Planning Tip:** To determine your current taxable estate, add the value of all your assets, including your home, business interests, bank accounts, investments, IRAs, retirement plans and death benefits from your life insurance policies, and then subtract all of the debts you owe.

It's important to remember two things: These changes are only effective for the next two years. If Congress does not act again before the end of 2012, on January 1, 2013, the estate tax exemption will drop to \$1 million (adjusted for inflation) with a top tax rate of 55%. Also, some

From [Scott Schrader](#)

### Winburn, Mano, Schrader & Shram, PLLC

P.O. Box 242120  
Little Rock, AR 72223  
501-975-6266

Mr. Schrader's practice is concentrated in the areas of estate planning and post-death administration, as well as estate litigation and disputes.



states have their own death tax, so your estate could be exempt from federal estate tax but still have to pay a state death tax.

### **Optional Retroactive Planning for Estates of Those Who Died in 2010**

As noted above, the new law retroactively reinstated the estate tax for all of 2010. However, the Executor for anyone who died in 2010 has the option of electing to use the law as it existed before the 2010 Tax Act and pay no estate tax, but have a "modified carryover basis" instead of adjusting the basis of all assets to the date of death value (including, in community property states, the surviving spouse's interest).

The "basis" of an asset is the value used to determine gain or loss for income tax purposes when the property is sold. If you give someone an asset while you are alive, it keeps your basis (what you paid for it) so the recipient gets what is called a "carryover" basis.

For 2010, under the pre-2010 Tax Act law, limits were placed on the amount of asset basis that could be stepped up in a decedent's estate: only \$1.3 million in asset value increases were allowed, plus an additional \$3 million of basis increases for assets passing to a surviving spouse. In effect, the law substituted paying capital gains taxes for paying estate taxes. Under the 2010 Tax Act, there is a choice for those who died in 2010.

**Planning Tip:** Executors have until September 17, 2011, to decide if the option is better for the estate, file an estate tax return, pay taxes and make any disclaimers. Electing the "no estate tax/modified basis option" would generally be good for those with large estates that would not be covered by the \$5 million exemption. However, each case must be evaluated individually, considering, for example, the amount of estate tax that would be payable now versus income tax that would be due on the gain when the assets are sold at some point in the future; the expected sale date of the assets; and what the capital gains and ordinary income tax rates might be in the future.

### **Portability of Estate Tax Exemptions between Spouses**

The estate tax law provides an unlimited deduction for assets left to a surviving U.S. citizen spouse. Therefore, the first spouse who dies can leave everything to the surviving U.S. citizen spouse and no estate taxes will be due upon the first death. Most married couples like this arrangement because it's easy to administer and all of the assets are available to the surviving spouse. For those who died before January 1, 2011, and for those whose surviving spouses live beyond December 31, 2012, however, a big problem can occur because the estate tax exemption that could have been used at the first death is not available to shield assets in the surviving spouse's estate.

**Planning Tip:** The portability provision may work fine for some couples. But you may still prefer the benefits of the A-B (credit shelter) trust, especially if you have a "blended" family. Also, if you use a living trust and properly fund it (transfer your assets to it), you will avoid probate which, depending on where you live, could save your family thousands more.

...

**Conclusion**

Now is the perfect time to move forward with your estate, retirement and disability planning.

The 2010 Tax Act provides tremendous planning opportunities to transfer vast amounts of wealth for families with estates of all sizes, but it is a limited time opportunity that expires on December 31, 2012. At the same time, individuals with estates of less than \$5 million and married couples with estates of less than \$10 million can focus on planning that concentrates on family goals and objectives without, at least for the next two years, having to jump through hoops to avoid federal estate taxes. Of course, state death taxes and income taxes must still be considered.

We are ready to help you define your personal and financial goals and desires, and take advantage of these unique planning opportunities. Contact our office for a consultation.

*To comply with the U.S. Treasury regulations, we must inform you that (i) any U.S. federal tax advice contained in this newsletter was not intended or written to be used, and cannot be used, by any person for the purpose of avoiding U.S. federal tax penalties that may be imposed on such person and (ii) each taxpayer should seek advice from their tax adviser based on the taxpayer's particular circumstances.*