

2010 Tax Relief Act: Important Elections for 2010 Decedents' Estates

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Under the federal tax laws in effect since 2001, the federal estate tax was repealed for estates of decedents who died in 2010 ("2010 Estates") and the "stepped up basis" rules that previously resulted in avoidance of income (capital gains) tax liability on the pre-death appreciation of most assets were suspended. Suspension of the stepped-up basis rules meant that the assets of 2010 Estates would retain the decedent's basis for income tax purposes (known as "carryover basis") in calculating taxable gains when those assets are later sold. Special basis rules contained exceptions to the carryover basis which allow the executor of the decedent's estate to step-up the basis of assets passing to beneficiaries other than the spouse by up to \$1,300,000 and the basis of assets passing to the surviving spouse by up to \$3,000,000. The election for this "limited stepped-up basis" was to be made no later than the filing deadline for the decedent's final income tax return.

In the final weeks of 2010, the estate tax laws were modified by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 ("2010 Tax Relief Act"), which was signed into law on December 17, 2010. Some changes in the 2010 Tax Relief Act were made retroactively to specifically effect decedents who died in 2010. The new law provides 2010 Estates with an option: 1) the executor may (do nothing and) choose to accept the new federal estate tax rules for 2010 Estates; or 2) elect to accept the rules in effect prior to the 2010 Tax Relief Act.

This election must be made no later than September 19, 2011. These new rules provide a \$5 million estate tax exemption, a 35% estate tax rate and a full stepped-up basis for most assets included in the gross estate.

It is anticipated that most 2010 Estates with taxable values of less than \$5 million will accept the federal estate tax in order to obtain a full stepped-up basis for its assets. On the other hand, the executor may choose to have the rules in effect before the 2010 Tax Act apply: no federal estate tax for 2010 Estates, in which case the estate will forego full stepped-up basis treatment for income tax purposes and accept limited stepped-up basis treatment. In that event, the executor may elect specific assets to receive a stepped-up basis subject to the limitations provided under the law in effect for 2010 Estates prior to the 2010 Tax Relief Act (as reflected above).

While it may be advisable for larger 2010 Estates to elect out of the estate tax applicability, each executor should carefully consider all aspects of the tax law before making an election. Beneficiaries of 2010 Estates should be aware of the potential impact that the executor's election may have, and may wish to address with the executor the analysis that the executor has undertaken. The attorneys in the Probate, Trust & Personal Planning Group at Partridge Snow & Hahn LLP are available to assist executors and beneficiaries of 2010 Estates in analyzing these complex rules in order to make the most advantageous election.

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