



TAX & ESTATES DEPARTMENT

ALERT

NEW ESTATE TAX RULES FOR DEATHS THAT OCCURRED IN 2010

In December 2010, we issued an alert informing you of the passage of the Tax Relief Unemployment Insurance Reauthorization and Job Creation Act of 2010, which directly impacted income, gift, estate and generation skipping transfer (GST) taxation for 2010, 2011 and 2012. In the coming weeks, Fox Rothschild attorneys will be issuing specific alerts on a number of issues relating to the Act. This is the first in the series and will focus on the Act's impact on 2010 estates.

The Tax Relief Act presents new challenges to executors (and their advisors) of estates involving 2010 decedents. The Act empowers executors to make significant tax decisions that could impact both income and estate tax consequences for various beneficiaries as well as the disposition of estate assets under certain wills. Careful analysis of the various decisions is required, as well as adherence to new filing date requirements for estate tax returns, the reporting of GST and allocations of (or elections out of) GST exemptions.

Default Rule: Federal Estate Tax in Effect

The federal estate and GST tax applies to 2010 deaths as if the estate tax and GST tax had never been repealed but with an increased exemption and decreased rates retroactive to January 1, 2010. Therefore:

- 2010 estate tax exemption of \$5 million, with a flat 35 percent rate.
- 2010 GST tax exemption of \$5 million, with a rate of zero percent on 2010 GST transfers (i.e., direct skip transfers, taxable terminations, and taxable distributions).

Optional Rule: No Estate Tax (But Carryover Income Tax Basis)

Executors may elect to have zero estate tax and a modified carryover basis under IRC Section 1022 for assets "acquired or passing from" the decedent. The new basis will equal the **lower** of the decedent's adjusted basis or fair market value at date of death. The Act allows the executor to make the carryover basis election and determine the assets to which a basis increase of \$1,300,000 will be allocated and which beneficiaries may benefit. An additional \$3,000,000 basis increase is permitted to assets passing to or for the benefit of a surviving spouse under certain qualifying trusts. While the decision to elect carryover basis in large estates and to use the default rule in estates under \$5,000,000 is easy, significant planning and analysis is required for moderate estates.

In some cases, immediate judicial intervention will be needed (1) to guide an executor's decision as to whether to elect out of the estate tax; and (2) if the carryover basis election is made, to obtain a judicial order as to which assets to allocate to the basis increase (and

which will determine the beneficiaries who will benefit from the basis increase). Intervention may also be required to construe marital deduction formula wills of 2010 decedents in light of a carryover basis election (where exemption equivalent or marital deduction language may not apply). Marital deduction formula wills drafted prior to the Tax Relief Act did not take into account the lack of federal tax and the possibility of a carryover basis election, creating uncertainty as to a testator's intent. If a family is not able to timely resolve issues, judicial intervention and a final determination will have to be obtained prior to the due date for filing the return.

Tax Returns and Filing Dates

Federal Estate Tax Return (Form 706):

- Due Sept. 17, 2011, for decedents dying prior to the Act's date of enactment of Dec. 17, 2010. (However, actual due date is Sept. 19, 2011, as Sept. 17 is a Saturday). For 2010 decedents dying after Dec. 17, 2010, due date is nine months following death.
- Form 706 must be filed if decedent's assets plus adjusted taxable gifts exceed \$5,000,000 and default rule is chosen by the executor.
- Portability of the estate tax exemption not available for 2010 decedents.

GST Reporting (Form 706)

- Due Sept. 19, 2011, for GST prior to Dec. 17, 2010.
- The Tax Relief Act does not provide an extension for making timely allocations of GST exemption (or electing out of automatic GST exemption allocation). This may be corrected in subsequent legislation, regulation or IRS announcement.
- If carryover basis is elected, unclear where the

GST transfers or exemption allocations are reported.

Carryover Basis Return (Form 8939) – Only a Draft Is Currently Available

- To be filed only if the estate elects out of the estate tax into the carryover basis regime.
- Due date is the date of filing the decedent's last income tax return, including extensions (i.e., April 15, 2011, for any decedent dying in 2010, or Oct. 15, 2011, if the decedent's last income tax return is placed on extension). The draft form does not contain a different due date, and it appears that the nine-month extension period granted for Form 706 does not (at the moment) extend to Form 8939.
- Due date may be extended by the IRS for all 2010 estates. The ABA Section of Real Property, Trust & Estate Law, in a letter to the IRS dated Jan. 31, 2011, requested a minimum extension of six months.

Impact of Act on Professional Advisers and Executors

Executors of 2010 estates may require counseling to minimize the impact of both income and estate tax to estates and their beneficiaries. Factors to consider include the executor's need to timely notify beneficiaries involving potential will construction issues in the case of certain formula wills; the timing of the executor's disposition of estate assets; the age of the surviving spouse; and the character of estate assets.

The members of the Tax and Estates Department of Fox Rothschild LLP are available to assist in this complex new area created by the provisions of the Tax Relief Act. We encourage you to contact your relationship lawyer at Fox Rothschild or a member of the firm's [Tax and Estates Department](#) in the state in which you maintain your permanent residence.



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