

Estate Planning and the 2010 Tax Act

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On December 17, 2010, President Obama signed into law the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (the "Act"). The enactment of this legislation resulted in several important changes for federal estate and gift tax law. While there was no federal estate tax for 2010, in 2011 the federal estate tax was scheduled to return with a \$1 million exemption and a maximum marginal rate of 55%. The Act reduces the 2011 and 2012 maximum federal estate tax rate to 35%, and increases the exemption to \$5 million per person. In addition, the pre-2010 rules concerning the step up in basis for assets at death are reinstated, and the Act provides for estate tax exemption "portability", which means that a deceased spouse's unused estate tax exemption can be utilized at the death of the surviving spouse.

Notwithstanding the favorable estate tax rates and estate tax exemption in 2011 and 2012, after 2012 the federal estate tax increases to a maximum marginal rate of 55% and the unified credit reduces to \$1 million per person, with no portability.

The Act provides significant planning opportunities during the next two years because the \$5 million exemption applies on a unified basis to both the gift and estate taxes, with gifts made during lifetime exceeding the annual exclusion amount reducing the amount of the \$5 million exemption available at death. This means that individuals can make gifts to the next generations of up to \$5 million per person over the next two years, and avoid the consequences of a possible return to the \$1 million exemption and 55% maximum federal estate tax rate. While we do not advise that clients immediately start gifting assets to the next generations, as 2013 approaches, we will need to keep a careful watch on what direction Congress appears to be heading with respect to 2013 estate and gift tax legislation.

The \$5 million exemption does raise some possible issues for those with older estate plans that use a formula for determining the amount that funds what is usually called the unified credit or credit shelter trust. These formulas were designed under the assumption that the federal estate tax exemption would remain in the range of \$1-\$2 million. Therefore, if your estate plan has not been updated during the past ten years, or if it contains a formula funding a unified credit or credit shelter trust, you should be talking with your estate planning advisor for the purpose of updating your documents. In addition, if your powers of attorney were done prior to the year 2000, those too should be updated, because changes in state law concerning powers of attorney has resulted in changes to the form documents used for those purposes.

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