

Estate Tax Relief, For Now

2010 was the year without a federal estate tax; a real boon to the fabulously wealthy, but not really a concern for the rest of us. However, the reversion to the \$1 million exemption, scheduled to go into effect on 1/1/11, would affect many more people. Couple that with the Massachusetts estate tax on estates in excess of one million dollars, and you could be looking at taxes taking a large bite out of your estate.

Have no fear; the government is here- once again adding anything but stability and consistency to the tax code. For two years only, the federal estate tax will only affect estates over \$5 million dollars. Curiously, the exemption is indexed for inflation beginning in 2012, the year before the provision is set to expire.

The estate and gift tax exemptions are once again unified, meaning that regardless of whether you give away \$5 million while living, or die with it, your tax would be the same. Last year, you could only give away \$1 million dollars without incurring a transfer tax, despite the fact that there was no estate tax. Confused? Let's say you had a \$3.5 million estate and gave away \$1.5 million in 2010 and then died later that year with \$2 million dollars. You would pay no estate tax on the \$2 million, but would have paid tax on the \$500,000 (above the million) transferred during life. Had you died with the entire \$3.5 million estate, there would also be no estate tax. Obviously, the person who chose not to gift made out better.

Basis is Back- Last year, in a trade off to having no estate tax; the "step-up" in basis for inherited property had been eliminated. Now, once again, people receiving property from a decedent will take the date of death value as their tax cost. But, wait, there's more. The 2010 rule of no step-up in basis was changed retroactively. Now, only for decedents dying in 2010, executors can choose to pay estate tax at the 2011 level (35% on estates over \$5 million) in exchange for a step up in basis for all assets. Estates under \$5 million will automatically receive step up treatment. Executors will really have to run the numbers for estates over \$5 million with low basis assets to see which calculation yields the best result.

Portability of Estate Tax Exemption For the first time since the enactment of the estate tax, an exemption amount not used in the estate of the first spouse can be used in the estate of the second spouse. The thought of "wasting" one's credit has led to the sophisticated trust planning that many people have. For the next two years, a married couple can transfer \$10 million dollars tax free to their kids, regardless of who holds title to the property. However, in order to take advantage of this provision, both spouses must die in the next two years, and the exemptions cannot be stacked. In other words, if you were to be widowed twice in the next two years and then die, your executor can only use the exemption of your first spouse. The government wanted to be sure that the wealthy

were not killing off spouses in order to receive multiple tax exemptions. You are perhaps thinking that the chances of someone going through two spouses in two years and dying themselves would be slim, but who are we to second guess the government?

All of the scrambling to stop the so-called “Bush Era” tax cuts from expiring on 1/1/11 has led to a reprieve of two years only. Chances are, as December 2012 approaches, we will again have to deal with the uncertainty of whether the current changes will be extended, or will the estate tax exemption revert to one million dollars. Given the government’s track record, 2012 will be another interesting year. Stay tuned.