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Estates and Trusts Tax Alert

Reducing the Impact of Transfer Taxes on Your Family

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Scott S. Tate
410.347.7341
sstate@ober.com

Victoria Z. Sulerzyski
410.347.7304
vzsuleryski@ober.com

For the remainder of 2010 there is no federal Estate Tax and no Generation-Skipping Transfer Tax ("GST"). Both taxes are scheduled to be reinstated as of January 1, 2011, with lifetime exemptions of $1 million. Congress is currently in session and is debating a bill that could change the law substantially. However, as the close of 2010 approaches, there may still be some planning opportunities available to reduce the impact of transfer taxes on your family. If you would like to discuss any of the options presented, please give us a call.

Gift Tax

The federal Gift Tax is still in effect for 2010 and continues in 2011 and beyond with a lifetime exemption of $1 million. There is also an annual exclusion for gifts which is currently $13,000 for each donee. Until December 31, 2010, the gift tax rate is 35 percent. On January 1, 2011 the rate is scheduled to go back up to 55 percent, which means that there is a window of opportunity available to make taxable gifts prior to year end and pay tax at what is currently a historically low rate. Paying gift taxes is, in effect, prepaying taxes that will be due at death. It also has the benefit of reducing the taxable value of your estate and removes appreciation on gifted assets from future transfer taxation.

The proposal currently under debate in Congress would set the estate and gift tax rates at 35 percent for the next two years, which would eliminate the effectiveness of this strategy if it passes.

Generation-Skipping Tax

There are also planning opportunities available for those who wish to make gifts to grandchildren. The GST, which is scheduled to reappear on January 1, 2011, is a tax on gifts to grandchildren and others who are more than one generation younger than a donor. Gifts to grandchildren are advantageous because they "skip" the imposition of estate tax at your children's generation. This year may prove to be a good year to make gifts to grandchildren in order to realize less overall transfer tax on your family. Also, if a trust already in existence is not exempt from GST, there may be an opportunity to transfer assets from the trust to grandchildren without the imposition of the GST, which would otherwise be payable down the road when the trust makes distributions to the grandchildren.

The proposal currently in Congress would set the GST rate at 35 percent for 2011 and 2012 and the exemption at $5 million.

Roth IRA

This year taxpayers can convert a traditional IRA account to a Roth IRA without any limitation based on income. Normally, a Roth conversion can only be done if a taxpayer's income is below $100,000. Also, for this year only, the tax on the conversion is spread out over the next two years.

A Roth IRA has several advantages over a traditional IRA. Distributions from a Roth are not taxable, whereas, all distributions from traditional IRAs are taxed. In addition, distributions are required for traditional IRAs after the age of 70 ½, but the minimum distribution rules do not apply to Roth IRAs. This rule provides an opportunity to accumulate wealth in a Roth IRA that can be passed on to your heirs to enjoy free of any income taxes.
