



Lawrence L. Lewis
Onebane Law Firm
P. O. Box 3507
Lafayette, Louisiana 70502
337-237-2660
lewisl@onebane.com
www.onebane.com

2010 ESTATE AND GIFT TAX LAW CHANGES

Temporary Relief and Continued Uncertainty

The old adage that nothing in life is certain but death and taxes continues to be challenged by the United States Congress as it continues the uncertainty that has plagued the estate and gift tax law since 2001. In December 2010 Congress passed and the President signed the Tax Relief, Unemployment Reauthorization, Job Creation Act of 2010. This Act broadly changes the estate, gift and generation skipping transfer tax rules for 2010, 2011 and 2012, and then allows the law as it existed in 2000 to be re-established in 2013 unless additional legislation is passed in the interim. If these changes become permanent, they will dramatically change the way in which estate planning is conducted. If they do not become permanent, they will represent a two (2) year window during which several important estate planning opportunities will exist. Unfortunately, Congress has once again chosen to “kick the can down the road” and continue the confusion and uncertainty that has existed in the estate, gift and generation skipping transfer tax arena for the last several years.

KEY PROVISIONS OF THE 2010 ACT

- It lowers the estate tax rate and increases the tax rate exemption for 2011 and 2012. In 2009 the top estate tax rate was 45% and there was a \$3,500,000 exemption. Prior to the 2010 Act the top rate was to revert to 55% for years after 2010 and the exemption was to revert to \$1,000,000. The 2010 Act reduces the top rate to 35% and increases the exemption to \$5,000,000 for 2011 and 2012 adjusted for inflation.

- The 2010 Act reunifies the estate and gift tax law so that they share a single exemption and are subject to the same rates. In 2009 when the estate tax exemption was \$3,500,000 million dollars, the gift tax exemption was only \$1,000,000. In 2011 and 2012 the gift tax and estate tax rates are reunified with a top rate of 35% and overall \$5,000,000 exemption which can be used either for gifts or, to the extent not used during life, at death against the estate tax.
- The 2010 Act lowers the generation skipping transfer tax for 2011 and 2012 by increasing the exemption amount from \$1,000,000 to \$5,000,000 and reduces the rate from 55% to 35%. The GST tax is an additional tax on gift and bequests to persons more than one generation removed from the donor.
- The 2010 Act also introduces a portability feature into the transfer tax area. Any exemption that remains unused as of the death of a spouse who dies after December 31, 2010 and before January 1, 2013 will be available for use by the surviving spouse in addition to the surviving spouse's own \$5,000,000 exemption. Under prior law, the exemption of the first spouse to die was lost if not used. This could happen where the spouse with resources below the exemption amount died before the richer spouse.
- All of the foregoing changes are temporary and continue only through December 31, 2012. On January 1, 2013, the law returns to a 55% top estate and gift tax rate, a flat 55% GST tax rate, a \$1,000,000 estate and gift tax exemption amount, a \$1,000,000 GST exemption and no portability of the first deceased spouse's unused exemption amount.

ALL ESTATES BENEFIT

The more generous \$5,000,000 estate and gift tax exemption benefits clients with estates of all sizes. Individuals with estates under \$5,000,000 and married couples with estates under \$10,000,000 will not have to be concerned with estate taxes and can make gifts in excess of the annual exclusion amount (\$13,000) without worrying about transfer taxes. If the revisions are made permanent, these persons should be able to have simpler and more understandable estate plans at a lower cost.

The real beneficiaries of the new law, however, are the very rich, whose estates are large enough to permit substantial lifetime transfers. The new law not only increases the gift tax exemption from \$1,000,000 to \$5,000,000 for transfers in 2011 and 2012, but it also declined to adopt proposals that had been under consideration that would have restricted the use of family limited partnerships and limited liability companies to produce valuation discounts and the continued use of short term zeroed out gift grantor retained annuity trusts. These vehicles remain available for sophisticated estate planning.

The very wealthy who are inclined to make large taxable gifts are given new reasons to do significant additional gifting in the next two (2) years. Additionally, the increase in the GST exemption to \$5,000,000 should prompt the same donors to create multi-generational trusts of

\$5,000,000 to \$10,000,000 to create an endowment for their descendants that will last without future estate taxes or GST taxes.

PLANNING IMPLICATIONS OF THE 2010 TAX ACT

Estates of decedents who die in 2011 and 2012 will benefit from the increased estate tax exemption. Estate plans can be drafted to take advantage of these exemptions if death occurs in those years, however, the estate plan must also take into account that death may not occur in those years and the exemptions may be smaller or larger. The temporary nature of the relief granted by 2010 Act complicates planning and creates drafting complexity as estate planning documents must be written with sufficient flexibility to deal with the uncertainty of future changes in the transfer tax laws. This is particularly true if formula clauses have been used in current documents that are keyed to the old estate and GST exemption amounts. If a bequest is keyed to the maximum exemption amount and that has changed or it changes in the future, it can have the unintended result of either increasing or decreasing the amount used to fund a gift or bequest to that legatee. Estate planning documents with formula clauses should be reviewed to insure that they continue to produce the results intended.

The most significant planning opportunity presented by the new tax law is the ability to make lifetime gifts utilizing the \$5,000,000 gift and GST exemption in 2011 and 2012. Lifetime gift planning can be enhanced through the use of valuation discounts and leveraged through the use of the increased generation skipping transfer exemption. Clients who have previously entered into transactions involving sales to intentionally defective grantor trusts utilizing their former \$1,000,000 gift tax exemption can now consider additional transactions by making up to \$4,000,000 of incremental seed gifts to the trusts. The time to make lifetime gifts is during this two year period of 2011-2012.