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Trusts & Estates Alert

2010: The Year of No Estate Tax and Carryover Basis

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The Federal estate tax and the income tax "step-up" in basis at death have been eliminated for persons dying in 2010. In addition, there is no generation-skipping transfer tax this year for gifts and bequests, although the gift tax remains in effect.

A review of your planning may be appropriate due to these changes, especially if

- You own property with an income tax basis much lower than its current value.
- Your estate planning documents divide assets among beneficiaries by using a tax-based formula that is predicated on the existence of a Federal estate tax.
- You continue to control low-income tax basis property which does not pass under the terms of your Will (e.g., you transferred property to a revocable trust).
- You appoint one or more of your beneficiaries as your executor.

What makes things less certain is that Congress may pass estate tax legislation this year, and attempt to make it retroactive to January 1. Although retroactive legislation may be unpopular and raise constitutional issues, such action is possible and may be permissible.

Without new legislation this year, the current law will reinstate the Federal estate tax on January 1, 2011, with an exemption amount of \$1 million and a 55% tax rate.

What Does The Temporary Repeal Mean to You:

- Under the law in effect prior to, and after, 2010, the income tax basis of an asset changes to its current value when its owner dies. Income tax basis is the value from which gain or loss on assets sold is measured. For persons dying in 2010, this automatic change in basis will not occur. Rather, the deceased owner's income tax basis in assets will "carry over" to those who inherit the assets, subject to an ability to allocate up to an additional \$1.3 to \$4.3 million of basis (plus unused losses) to assets owned or acquired by the decedent (different basis allocation rules apply for estates of non-resident aliens). Documents should include basis allocation provisions.
- For people who die this year, there is no Federal estate tax and generation-skipping transfer tax; but New York State's estate tax remains in place. Since there is no Federal estate tax, if definitions in your documents reference the Federal estate tax, there may be some question as to how your property will pass at death.
- The Federal gift tax continues to be in effect with a 35% rate and a \$1 million lifetime exemption; a \$13,000 annual per-donee gift-tax exclusion is also available.

Unique Planning Opportunities May Be Available for a Limited Period of Time:

- You may want to review your lifetime planning to determine if holding on to assets you have had for many years continues to meet your planning goals, and to review your record-keeping of existing assets.
- There may be a short window of time to make gifts to grandchildren and more remote generations free of generation-skipping transfer tax.
- Planning opportunities for wealth-shifting techniques continue to be available while current law applies, and asset values and interest rates remain low. We do not know what techniques Congress will restrict or eliminate in new legislation.