

## **MP&S TAX ALERT FEBRUARY 2010**

### **HOW SHOULD THE ONE-YEAR REPEAL OF ESTATE AND GENERATION SKIPPING TRANSFER TAXES AFFECT PLANNING IN 2010?**

The Federal Estate and Federal Generation-Skipping Transfer (GST) taxes expired on December 31, 2009, due to the failure of Congress to act before adjourning at the end of 2009. Based on current law, there is a one year repeal of the Estate and GST tax for 2010 only. However, the Federal gift tax was not repealed and remains in effect for 2010 but at a reduced rate of 35% for 2010 gifts.

#### **Income Tax on Inherited Property**

In 2009, taxable estates greater than \$3.5 million were subject to Federal Estate tax, with a maximum estate tax rate of 45%; the GST tax rate was also 45%. During the one-year repeal, the long-standing stepped-up basis at death rules will be eliminated and replaced with a modified carryover regime. As a result, there will be substantial income tax planning needed for 2010 with inherited property. The general elimination of the basis step-up this year may cause income tax to be payable by beneficiaries on sales of inherited property in cases where no such tax would have been payable under prior law.

Here is a bit more detail on the basic rules:

- For 2010, the income tax basis of bequeathed property will generally be the lesser of the carryover basis (i.e., the basis of the person who has died), or its fair market value (FMV) at date of death.
- However, as a partial replacement for the repealed step-up, estates will be allowed a \$1.3 million step-up in basis for estate assets (of the executor's choosing), and assets passing to a surviving spouse (or to certain marital trusts) will be allowed an additional \$3 million basis step-up.
- Thus, up to \$4.3 million in basis step-up can be allocated to property received by a surviving spouse. (The basis of an asset, however, cannot be adjusted above its FMV at date of death.)
- Note: A beneficiary inheriting an appreciated asset from a person dying in 2010 and then selling it for Fair Market Value (FMV) will recognize income from such sale equal to the excess at the selling price over the carryover basis or the limited step-up if applicable.

#### **Federal Gift Tax**

The Federal Gift tax remains in effect, but at a maximum rate of 35% for gifts made in 2010 – a reduction from the maximum rate of 45% in 2009. Each individual will continue to have a \$1 million lifetime federal gift tax exemption. The \$13,000 annual gift tax exclusion (\$26,000 where gift-splitting is elected by a husband and wife) per donee will also continue.

#### **Scheduled Changes in 2011 – Restoration of Federal Estate and GST Taxes with 55% Top Estate and Gift Tax Rate**

On January 1, 2011, the Federal Estate and GST taxes, along with the stepped-up basis rules, are all scheduled to revert to the law in effect before the 2001 Tax Act. The Estate and Gift tax lifetime exemption amounts will be reunified at \$1 million, with a top marginal tax rate of 55%; the GST lifetime exemption amount will also be \$1 million.

#### **What Does the One Year Repeal Mean for Estate Planning?**

You should review your wills and other estate planning documents with your advisors to ensure that they still meet your objectives and goals. Specifically, any dispositive formulas used in these documents may

be substantially impacted in 2010 by the one-year estate tax repeal because these formulas often rely on estate tax law provisions that are no longer valid under the law in effect for 2010. In addition, although this environment can make planning difficult, you may want to consider whether making any taxable gifts in 2010 is appropriate, particularly if they would have been subject to the GST. However, it is impossible to predict how Congress will act, and any gift planning should take into account the possibility that Congress will change the law retroactively for 2010 to increase the gift tax rate and restore estate and GST taxes.

## **NEWS TO KNOW**

Congress is expected to act in early 2010 after its return from recess and may retroactively restore the Estate tax in 2010; however, such retroactive legislation may be subject to constitutional challenge. Presently, there has been no indication that congressional tax leaders have agreed on how the Estate tax will be reinstated, and it is unclear how long the current disagreements in Congress over the Estate tax will persist.

Marks Paneth & Shron LLP will be closely monitoring developments in this area. The uncertain situation, given the possibility of superseding and retroactive legislation, makes estate and gift planning quite difficult and challenging. Moreover, state estate and gift tax law considerations still need to be addressed. Our team of experienced tax and estate planning professionals will be pleased to follow-up with you on your particular individual circumstances as well as discuss any questions you may have and any planning opportunities that may be available in 2010, given the one-year Federal estate tax and GST tax repeal and the reduced Federal gift tax rate of 35%.

## **ACCELERATED TAX BENEFIT FOR HAITI EARTHQUAKE RELIEF**

President Obama has signed into law a measure that provides an accelerated tax benefit for taxpayers making charitable cash contributions by February 28, 2010 to the Haiti earthquake relief efforts. This means that taxpayers can choose to claim a charitable deduction on their 2009 returns for qualified Haiti disaster relief cash contributions *made after January 11, 2010 and before March 1, 2010*. Charitable contributions by corporations are also covered under the new law. In addition, the new law allows individuals who make cash contributions through their cellular phones via text message to substantiate their contributions with their telephone bills.

## **FOR MORE INFORMATION**

For more information on how the 2010 repeal of the Federal Estate and Federal Generation-Skipping Transfer Taxes will impact your estate planning, please contact **Steven Eliach, JD, LL.M.**, the Principal-in-Charge of the Marks Paneth & Shron Tax Practice at 212.503.6388 or at [seliach@markspaneth.com](mailto:seliach@markspaneth.com) or **Michael Bekas, CPA**, Partner in the firm's Tax Practice at 212.503.8909 or at [mbekas@markspaneth.com](mailto:mbekas@markspaneth.com).