
New Tax Law

Provides New Opportunities



By Attorney Keith J. Pilger

At the end of 2010 we saw many changes, extensions and revisions to the federal tax law, which include changes to the estate tax law. The new law essentially does three things with respect to the estate and gift tax: (1) it retroactively provides estates for decedents that died in 2010 with an option of choosing which estate tax rules to apply, the 2010 rules or the 2011 rules; (2) it brings back the estate tax for 2011 and 2012; and (3) it reunifies the gift and estate tax.

Option for 2010

The new law provides heirs of decedents dying in 2010 with the option of which estate tax rules to apply. While there was no estate tax in 2010, some inherited assets are subject to higher capital gains tax under the 2010 rules, a situation that actually raises the tax burden for some heirs. Inherited assets under the 2010 rules have a “carry-over tax basis” (meaning the same tax basis as they had in the hands of the decedent) rather than a “stepped-up tax basis” (meaning the tax basis would be the value of the asset at death). Under the 2011 rules, estates would be subject to a \$5 million exemption and maximum 35% tax rate, but the inherited assets would have a stepped-up basis in the hands of the heirs. If the executor of the estate does not elect to have the original 2010 rules apply, the estate tax return would be due nine months following the date of the enactment of the new law.

Estate Tax for 2011 and 2012

For 2011 and 2012, the top estate tax rate will be 35%. The exemption amount for 2011 will be \$5 million per individual and will be indexed for inflation after 2011. Inherited assets will have a stepped-up basis in the hands of the heirs. In addition, the new law introduces the concept of portability of unused exemption between spouses (discussed in further detail below).

Gift Tax

For gifts made after December 31, 2010, the gift tax will be reunified with the estate tax. Under the new law, the estate and gift tax exemptions are reunified for 2011 and 2012, which means that the \$5 million estate tax exemption will also be available for gifts. Under prior law, the estate and gift tax were not unified, so while the estate tax exemption rose to \$3.5 million, the gift tax exemption remained at \$1 million. The gift tax rate under the new law is 35% for 2011. In addition, the generation-skipping tax (GST) exemption will also rise to \$5 million with a tax rate of 35%.

Wisconsin Estate Tax

As a result of the new law, there is no Wisconsin estate tax for deaths in 2011 and 2012, unless action is taken by the Wisconsin legislature to impose an estate tax. The credit for state death taxes paid has been eliminated for deaths in 2011 and 2012, which would have been the basis for Wisconsin’s estate tax. The new law allows for a deduction for state death taxes paid.

Planning Opportunities

The new tax law provides a multitude of new planning opportunities that individuals can take advantage of to transfer more of their estates to their heirs free of estate taxes.

Increased Exemption and Portability

As discussed above, the new law raises the estate tax exemption amount for each individual to \$5,000,000 and makes the exemption portable between spouses. As a result, with the proper planning, a married person who dies during 2011 or 2012 can ensure that any unused portion of his or her \$5,000,000 estate tax exemption can be transferred to the surviving spouse allowing him or her to shield the maximum amount possible from estate taxes upon his or her death. It is also important to note that in order for the portability rules to apply, an executor or administrator of the estate must make an election on a timely-filed estate tax return.

Increased Gift Tax Exemption

Potentially, the most significant aspect of the new law is the reunification of the estate and gift tax and the resulting increase in the gift tax exclusion to \$5,000,000. The increased exclusion creates a number of opportunities during the next two years for individuals to gift significant amounts to their heirs. This provides the dual benefit of removing assets from the donor's estate for estate tax purposes, as well as sheltering future growth in the assets gifted from estate and gift taxes.

Use of Trusts

Many of the above-referenced planning opportunities can be utilized through the use of trusts. Trusts are flexible planning tools that can be tailored to each individual situation.

It is important to keep in mind that the new law is only a two-year "patch" and that the estate and gift tax exemptions are scheduled to return to \$1,000,000 on January 1, 2013. It is likely that Congress will delay in dealing with the issue until late 2012, as was the case last year. As a result, it is important to take advantage of the current opportunities that the new law affords.

If you would like to discuss the new law in more detail and the potential planning opportunities that may be right for you, please contact one of our estate planning attorneys.



ATTORNEYS AT LAW
Est. 1886

1257 Main Street
Stevens Point, Wisconsin
715-344-0890
www.andlaw.com

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