WISEMAN BRAY PLLC

ATTORNEYS AT LAW

ESTATE PLANNING NEWSLETTER

Volume 7, Issue 1

Winter 2011

At Long Last...Gift and Estate Tax Legislation

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After quite a wait, the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 ("the 2010 Tax Act") was signed into law on December 17, 2010. Although we in the estate planning community had been awaiting legislation for over a year regarding the estate tax, many of us were starting to think Congress was not going to act and let the provisions of the prior act, referred to as "EGGTRA", sunset.

The 2010 Tax Act includes not only significant estate and gift tax changes but also an array of continued income tax breaks for individuals and business as well as other economic incentives. While an intense look at all of the provisions of the 2010 Tax Act is beyond the scope of our discussion, we wanted to focus on the highlights relating to estate, gift and generation skipping transfer taxes.

The previous estate tax legislation, EGGTRA, provided for an increasing estate tax exemption amount from 2001, when the legislation was passed, until 2009. Pursuant to EGGTRA, there was to be no federal estate tax in 2010 and then the law was set to sunset. In the absence of this new legislation, the sunset provision meant that the federal estate tax exemption was set to return to $1 million with a top rate of 55% as of January 1, 2011.

The history and the prior legislation regarding the gift and estate tax is important because one of the first and most important things to note about the 2010 Tax Act is that the vast majority of the provisions apply for **two years only.** Under this legislation, these rules only apply through the end of 2012, at which time many of them expire and the sunset provisions of EGGTRA come back into play absent additional legislation. Thus, while most of the provisions are favorable to taxpayers, they are certainly not guaranteed for a long period of time.

Secondly, the 2010 Tax Act **reunifies** the gift and estate tax exemption amount and sets that exemption amount at **$5 million** per person. Under prior law, the lifetime gift tax exemption remained at $1 million while the estate tax exemption increased. Under the new legislation, any gifts made after December 31, 2010 in excess of the annual exclusion amounts (currently $13,000) will be subject to the applicable gift tax exclusion amount of $5 million per person, and any decedents dying in 2011 or 2012 will be subject to an estate tax exemption amount of $5 million per person. Use of the gift tax exclusion amount during your lifetime continues to offset the amount available for exemption at death against the estate tax, which means that you still do not get to give $5 million away during your lifetime using the gift tax exclusion and then use a $5 million exemption at death. In other words, you do not get both.

A third and interesting new feature of the 2010 Tax Act is the concept of **portability** of the estate tax exemption amounts between spouses. Under prior law, you had to claim the exemption of the first spouse to die (continued on back page)

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after the death of that spouse and could not simply add the exemption amount at the death of the second spouse to die. We often used the illustration of a coupon that, if not used at the death of the first spouse, was wasted. The 2010 Tax Act allows any unused exemption at the death of the first spouse to die to be available for use at the death of the second spouse to die. In order to do this, there are still some technicalities that must be properly addressed, but the idea is that the exemption amount that is unused at the first death can be carried over and used at the death of the survivor.

Fourth, the generation skipping transfer tax exemption amount is also $5 million. The 2010 Tax Act allows for GST tax allocation for gifts made during 2010 for up to this $5 million exemption amount but provides that the rate is 0% so there is no retroactive application of the GST tax for the year 2010.

Fifth, the top tax rate for gift, estate and generation skipping transfer tax is **35%**, which means that estates or gifts that exceed the $5 million exemption amount will be subject to a maximum 35% tax rate on those transfers. Under prior law, the maximum tax rate was 55% so again, this legislation is more favorable for the taxpayer than prior law.

Finally, the 2010 Tax Act **repeals the carryover basis** rules that applied under EGTRRA for decedents dying in 2010. This change means that we will go back to the fair market value basis (often referred to as "step-up in basis") in determining the basis that beneficiaries will have when they inherit property from a decedent. Estates of decedents dying in 2010 have some options and elections to make regarding carryover basis and the applicable exclusion amount.

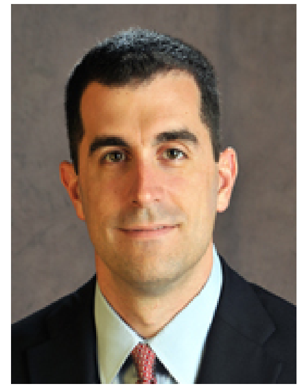
In summary, the 2010 Tax Act provides many favorable provisions for taxpayers, albeit for a relatively short period of time. In Tennessee, we still have the Tennessee inheritance tax with a $1 million exemption amount and rates of 5.5%-9.5% that remains unaffected by this new federal legislation.

Please contact our office to schedule an update appointment to see if your current estate plan can be simplified and still accomplishes your objectives in light of this new legislation.

COMMUNITY PROPERTY TRUSTS

The Tennessee Community Property Act of 2010 was recently enacted and allows for community property ownership of assets in a Tennessee Community Property Trust. Although community property ownership of assets between a husband and wife is not always beneficial, it can provide significant advantage in the right circumstances, especially for property with a very low tax basis.

Provided the Community Property Trust meets certain requirements, the property owned by the trust will be treated as community property. The most significant advantage of community property ownership is that both spouses' interests receive a step-up in basis up to the fair market value of the property upon the death of the first spouse to die. In contrast, if the property was owned jointly or owned as tenants by the entireties, only half of the property would receive a step-up in basis at the first death. Thus, community property ownership can significantly reduce or even eliminate capital gains upon the death of a spouse. **Please contact our office to learn more about whether a community property trust may be beneficial for you and your spouse.**



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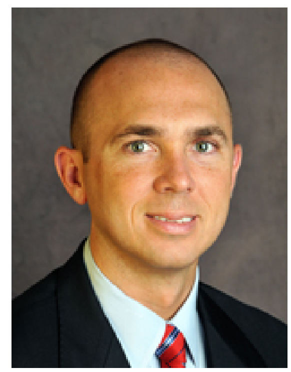

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