

Estate tax turmoil

How to take advantage of tax planning opportunities now **Interviewed by Clare DeCapua**

At the end of last year, it was assumed that Congress was going to effectively keep the 2009 estate tax rules in play and we would all know where we stood for 2010. But more than a quarter of the way through 2010, Congress has yet to even address the issue, leaving a number of estate and tax planning matters in question.

"There are tax opportunities and pitfalls that we're faced with, and people need to address these issues today," says Thomas J. Sigmund, a director with Kegler Brown Hill & Ritter. "They shouldn't be sitting back waiting for Congress to do something."

Smart Business discussed with Sigmund the importance of not missing out on planning opportunities in the midst of this complex environment.

What is the current status of estate tax law?

The status could be summarized as turmoil. Since the Economic Growth and Tax Relief Reconciliation Act of 2001, the estate tax law landscape changed considerably. The federal estate tax exemption increased from what was then \$675,000 to \$3.5 million in 2009. We all knew that, come 2010, we would have a repeal of estate taxes for one year with carry-over basis and then the regimen that we had in 2002 would come back into play in 2011, meaning that the exemption would drop down to \$1 million, and many of the same rules we had before would apply, including stepped-up basis. However, everyone expected Congress to take action to reinstate estate taxes for 2010; no one thought we'd actually be faced with repeal for any period of time.

What is Congress debating?

There is speculation that, more likely than not, the 2009 rules will come into play retroactive to January 1, 2010. But let's face it; we've had a lot of people die between Jan. 1 and today. If members of Congress were to try to reinstate the 2009 laws retroactively, they would be telling these estates that even though there were no estate taxes when the person died, there are now. They would likely face a constitutional challenge if they did that.

Congress is debating whether or not to allow Grantor Retained Annuity Trusts



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(GRATs) with terms that are less than 10 years. Normally, we utilize GRATs with two-year terms, rolling assets in and out of these GRATs to effectuate maximum wealth transfer without gift taxes.

They're also talking about portability of exemptions between spouses and eliminating discount planning when putting assets into a family partnership.

I don't think Congress is going to come back with a grandiose piece of legislation that covers all of those things. More than likely their first task is to deal with this repeal in 2010, and either fix it going forward or fix it retroactively. However, it is also possible in this political climate that Congress will do nothing in 2010 and just let the law play out.

What opportunities should people be taking advantage of now?

There are some great opportunities out there for the larger estates if they want to be aggressive.

Since there's no generation-skipping transfer tax as we speak right now, a direct transfer of unlimited amounts to a grandchild will not be subject to this tax, albeit subject to gift taxes if the transfer exceeds \$1 million.

If you transfer property in excess of \$1 million to somebody this year, the tax

rate is only 35 percent, which is a far cry from the estate tax rate that was in place in 2009, which was 45 percent. It's a further far cry from the 55 percent that's likely to be in place in 2011 if Congress doesn't change the law. So there's an opportunity to make some tax effective gifts this year. The risk is that Congress could reinstate generation-skipping transfer taxes retroactive to January 1, 2010 and reinstate the higher gift tax rate retroactively as well. However, for the most part, taxable gifts might still be a good plan to effectuate. If done properly, the taxpayer could actually straddle the fence waiting for what Congress does and make elections to effectuate or not effectuate a gift.

Finally, discounted gifts with use of family partnerships should be explored.

What pitfalls should people be aware of?

The worst-case scenario that we've seen is with clients in a second marriage who decide to leave the exemption amount to their children and the balance of their estate to the spouse. The thinking is that they won't have to pay any estate taxes on the property that went to their children and on the property that was in the trust for the second spouse through a combination of using their exemption and the marital deduction. But if you look at that document today, depending on how it's drafted, it could be interpreted to say that all their property is going to the children and nothing is to be left to the spouse. It may very well say, 'Transfer to my children what can be transferred without any estate taxes being associated with the transfer,' and in 2010 that would mean everything.

What should be done now?

Sit down with your tax adviser right now to revisit your documents and make sure they will work as you've intended them to, and make sure that your estate and your estate planning documents are in good order to maximize the tax savings that can potentially be had if death occurs in 2010. Even the administration of a decedent's estate for the period of time that we have this repeal may have to be addressed differently. <<

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