POINTERS

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.

The 2011 edition of this book is going to press shortly after passage of The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (hereafter referred to as The 2010 Tax Act). Despite its title, the impact of this legislation on the practice and art of estate planning will be immediate and far reaching. Unfortunately, because this law sunsets on January 1, 2013, it continues much of the uncertainty regarding the estate tax laws created by EGTRRA for the past ten years.

In a nutshell. Referred to as the "applicable exclusion amount," The 2010 Tax Act provides an estate tax exemption of $5,000,000 per person (by providing a credit of $1,730,800), transfers above this amount are taxed at a rate of 35 percent, and the estate taxes and gift taxes are reunified (in contrast to 2009 when estates up to $3,500,000 were exempt from taxation but gifts in excess of $1,000,000 were taxed). Beginning in 2012, the $5,000,000 applicable exclusion amount will be indexed for inflation. Most importantly, any unused applicable exclusion amount may be carried over to a surviving spouse (see the portability discussion below). The 2010 Tax Act exempts estates up to $5,000,000 from federal estate taxes *whether or not* the estate is properly planned (up to $10,000,000 for a husband and wife). For all but the very wealthy, *this law has effectively repealed the federal estate tax*, albeit for only two years. See also, footnote 6 on page 21.

Portability. The 2010 Tax Relief Act allows any unused exemption to be passed to a surviving spouse without the need to re-title assets and establish complex wills and trusts (e.g., by the use of QTIP, credit shelter, by-pass, or family trusts). If no applicable exclusion amount had been used by the deceased who dies in 2011, $5,000,000 could be carried over to the surviving spouse. However, the surviving spouse can only claim this unused exclusion if the executor of the deceased spouse's estate had previously filed an estate tax return electing to take advantage of any unused applicable exclusion amount. To fully benefit from this portability, under current law both spouses must die within the two-year period 2011-2012. Portability does not apply to generation-skipping transfers. Despite the advent of portability, there remain many non-tax reasons to use trust wills in estate plans. See the further discussion of portability on page 475.

Indexing. Should it remain a permanent part of the estate tax law, indexing would protect the exemption from being eroded over time. To appreciate the value of such projection, refer to the consumer price index table on page 314.

2012 And Beyond. By its very nature, estate planning is intended to provide some degree of predictability over the long-term. Unfortunately, because the provisions of The 2010 Tax Act expire at the end of 2012, the sunset provisions of EGTRRA 2001 will continue to create a degree of uncertainty and confusion. Making predictions about the future of the estate tax is risky business. [Who could have predicted as recently as 2008 that in 2010 the executors of billionaires dying in that year would have the option of opting out of the federal estate tax, or that there would be no generation skipping tax in 2010?] Nevertheless, there are indicators that should not be ignored. Leading up to enactment of The 2010 Tax Relief Act there was little, if any, serious debate about retaining the $1,000,000 exemption; the controversy centered upon whether the exemption should be either $3,500,000 or $5,000,000. More importantly, there was virtually no objection to either indexing or portability. Unlike an increase in the exemption to $5,000,000, the portability and indexing provisions of The 2010 Tax Act appeared to have had widespread bipartisan support. Given this environment, it is most likely that these features will become a permanent part of the estate tax laws. With indexing, portability, and a generous exemption, the vast majority of individuals *can no longer be motivated to do estate planning to save federal estate taxes*. But federal taxes are not the only game in town.

State death taxes. The phase-out of the state death tax credit, and its replacement with a deduction, has resulted in a substantial loss of revenue in many states. The 2010 Tax Act has extended that deduction to the end of 2012. Individual states have not suffered this revenue loss at the hands of Congress, and no matter what happens to the federal estate tax many of your client's estates will continue to be subject to state death taxes that are independent of the federal estate tax (see the discussion of decoupling of state death taxes on page 381).

Gifts. Each and every year, your high net worth clients should continue to take full advantage of the opportunity to make $13,000 "present interest" gifts (chart on page 47).

Grantor Retained Annuity Trusts (GRATs). The 2010 Tax Act did not contain the anticipated restrictions on GRATs as wealth transferring devices (chart, page 59). Relatively low values and low interest rates make this an attractive planning technique for high net worth clients.

Flexibility. In order to adjust to future changes in the uncertain world of estate taxes, increased flexibility should be built into your client's estate plans. Disclaimers offer a surviving spouse the opportunity to adjust to changing circumstances by controlling the amount of property going into the nonmarital trust after your client's death (pages 25 and 389). See also, the discussion of post mortem planning, on page 476.

Estate Planning Is More Than Tax Planning.

Estate planning is primarily about people and their desire to provide for their loved ones! Given proper motivation, most clients will devote the time and energy that is necessary to develop and adopt an effective estate plan.

The Nontax Reasons For Estate Planning. The primary objectives of most estate plans involve estate creation, support and care of a surviving family and the orderly transfer of property during lifetime or at death. This often involves providing for the care of minor children, support for disabled children and elderly parents, and protection of loved ones from creditors. For some individuals the motivation to plan their estates is found in a strong desire to assure the survival of a business, or to provide for their church or a charity.

Life insurance. Are there enough life insurance proceeds, liquid assets, and other sources of income to maintain the current living standards of your client's surviving family? Unfortunately, all too many individuals remain underinsured. In this regard, see Facts About Human Life Value in the Courtroom, on page 96. For those clients needing insurance to pay taxes, delaying the purchase of currently needed life insurance could be disastrous, particularly if your client becomes uninsurable while waiting for Congress to end the uncertainty and confusion of sun-setting tax laws. Where appropriate, convertible term insurance should be used. Some companies are offering permanent policies that give the policyowner the option of surrendering the policy without penalty if the federal estate tax is repealed.

Trusts. In moderate sized estates, QTIP, credit shelter, by-pass, and family trusts *will no longer be used to save taxes*. But with substantial estates a trust will can freeze the value of property during the surviving spouse's lifetime so that future appreciation will not be subject to federal estate taxes upon the surviving spouse's death. However, there remain many convincing nontax reasons to fund a bypass trust at the first death. See the chart on page 25. For many of your clients, the life insurance trust will continue to be an effective means of accomplishing multiple objectives. See the chart on page 51.

Coordination With Business Plans And Employee Benefits.

It is often difficult, if not impossible, to design an effective estate plan without considering your client's business disposition plans and employee benefit programs. Effective planning cannot be achieved unless there is an awareness of the interplay between the various strategies and techniques of estate planning, business planning, and employee benefits. For example, the liquidity needs of a business owner's estate plan are directly influenced by whether the business is to be sold, continued, or liquidated (chart, page 118). If the business is to be *sold*, then a funded purchase agreement may well provide all of the dollars needed for estate liquidity and family income. If the business is to be *continued*, then an employee benefit, such as split-dollar, could provide the necessary funds.