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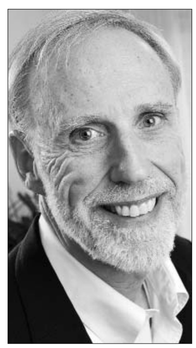
EstatePLANNING

Answers to common estate tax questions

The "Bush tax cuts," adopted in 2001, gradually increased the federal estate tax exemption while lowering the estate tax rates. On Jan. 1, 2010, the estate tax was temporarily repealed and replaced by a "carry over basis" tax regime. Late last month, the estate tax was resurrected with higher exemptions and lower tax rates.

The purpose of this article is to provide a brief overview of the changes that affect the estates of individuals who died in 2010, as well as estates of those persons who die in 2011 and 2012.



By DAVID PETTIG

Daily Record Columnist

What is "basis"?

"Basis" is the cost of an asset purchased by an individual. If I purchase one share of stock for $30, my basis in that stock is $30. If I sell the stock for $50, I must pay a capital gains tax on the $20 increase. If I sell the stock for $20, I can claim a capital loss on my income tax return.

How is basis affected when there is an estate tax?

If I die when the stock is worth $50, the basis in that stock automatically increases to $50 and my heirs do not have to pay a capital gains tax on the $20 increase when they subsequently sell the stock.

How is basis affected when the "carry over basis" law applies?

If I die when the stock is worth $50, the basis remains at what I paid for it ($30) and my heirs must pay a capital gains tax on the $20 increase when they subsequently sell the stock.

Why is George Steinbrenner still smiling?

Assume that George's basis in the Yankees was $5 million and that his interest in the team was worth $50 million at his death. If George had died in 2009, a $22.5 million federal estate tax (45 percent) would have been due. George died in 2010 and his estate did not incur any federal estate tax. On the other hand, the basis of George's interest will remain at $5 million under the carry over basis rules, so his heirs will be subject to a capital gains tax when they sell their interest in the team.

What is the current federal estate tax exemption?

$5 million per person. $10 million for a married couple.

Is the exemption fixed or will it be adjusted for inflation?

It will be adjusted for inflation beginning in 2012. The base exemption amount from which the adjustment is made is 2010 and the increments will be rounded to the nearest $10,000.

What is the federal estate tax rate?

35 percent.

Do these changes apply to 2010 estates?

Yes. The default provision of the new law is that an estate tax return must be filed for decedents dying prior to Dec. 17, 2010. The new exemptions ($5 million per person; $10 million per couple) and the tax rate (35 percent) apply. This is not true for gift taxes (see below).

Notwithstanding this default rule, the executor may elect for the carry over basis rules to apply, in which case additional forms will have to be filed on the decedent's final income tax return. It seems likely that Steinbrenner's executor will make this election.

When must the federal estate tax return be filed?

No later than Sept. 17, 2011 for decedents dying between Dec. 31, 2009, and Dec. 17, 2010. The former filing deadline of nine months from the date of death applies to decedents dying on or after Dec. 17, 2010.

Does a couple get a $10 million exemption or does each spouse get a $5 million exemption?

The couple gets a $10 million exemption. For example, if the first spouse only has a $2 million estate, the survivor will have an $8 million exemption, and vice versa. This concept is known as portability.

How is the portability exemption ensured?

The estate of the first spouse to die must file an estate tax return and irrevocably elect to qualify for portability even if that spouse's estate is not otherwise required to file an estate tax return, i.e., has a taxable estate of less than $5 million.

Is the gift tax affected?

Yes. The gift tax and the estate tax will be unified once again ... in 2011 when the exemption will be $5 million per person and the tax rate will be 35 percent. The exemption remains at $1 million per person for 2010 gifts.

Continued ...

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Continued ...

Is the generation skipping transfer tax (GST) affected?

Yes. As with the gift tax adjustment, both the exemption amount ($5 million per person) and the tax rate (35 percent) are unified with the estate tax.

Does that mean that a GST tax must now be paid for 2010 gifts?

No. There is a special rule for 2010. If a GST tax would have otherwise been payable for a 2010 transfer, the law provides that the tax rate is zero.

Is that all?

No! The planning implications and the tax reporting requirements are far more complex.

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