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MEMORANDUM

TO: Estate Plan Clients

FROM: Kurt D. Panouses, Esq.

DATE: January 21, 2011

RE: 2010 Tax Act (Tax Relief, Unemployment Insurance Re-Authorization and Job Creation Act of 2010)

President Obama signed new tax law legislation on Friday, December 17, 2010. The “2010 Tax Act” made significant changes in the estate, gift, and generation-skipping transfer tax areas.

Under the 2010 Act, the estate tax exemption has now been increased to \$5 million for both 2010 and 2011 with the top estate tax rate at 35%. Beginning in 2012, the estate tax exemption will be \$5 million and indexed for inflation, but the top tax rate will remain at 35%. In addition, assets included in a decedent’s estate will receive a full “step-up” in basis, equal to their value on date-of-death as was traditionally the law since 1981.

Prior estate tax law provided an increase in the estate tax exemption from 2001 through 2009. For 2010 there was a complete estate tax repeal. That law was set to sunset on December 31, 2010. Moving into 2011 there was to be an estate tax exemption of \$1 million with a top estate tax rate of 55%. The 2010 Act provides new rules for 2010, 2011, and 2012. However, once again, the laws will revert to pre-2001 levels unless Congress acts again, prior to December 31, 2012.

For decedents who passed away in 2010 (under the prior law) there was no estate tax and decedents had certain basis adjustments that, depending on their circumstance, could increase the basis up to \$4.3 million. Those basis adjustments needed to be allocated by the Personal Representative. However, the 2010 Act allows for decedents who passed away in 2010 to have the option to apply the new law or the previous law. A decision would need to be made based on the value of the estate. For those estates \$5 million or less, the new law would, in most cases, provide the best of all worlds by providing a \$5 million exemption and a complete step-up in basis of assets for income tax purposes.

The 2010 Act also reunified the gift tax and estate tax exemption beginning in 2011. Thus, the lifetime gift tax exemption for 2011 would be \$5 million with a matching gift-tax rate of 35%. For those individuals who previously used their \$1 million life-time gift tax exemption, an additional gift of up to \$4 million can be made without additional gift tax, beginning in 2011. This appears to provide a planning opportunity for those individuals who wish to make significant gifts. The new Act expires at the end of 2012. Individuals can choose to make gifts in 2011 and 2012 up to \$5 million (in life) in order to lock-in that exemption from gift tax.

The 2010 Act also makes changes to the generation-skipping transfer tax (the GST tax). The GST tax was repealed, along with the estate tax, in 2010. The new Act provides for the GST tax rate to be zero for transfers that occurred in 2010. For the years 2011 and 2012 the GST tax rate is equal to the maximum federal estate tax rate and, therefore, is a flat 35%. The exemption is also tied to the exemptions for estate tax and thus, a \$5 million exemption now exists for 2011 and 2012.

Finally, the 2010 Act provides an additional planning opportunity through its “portability” provisions. This new concept of portability allows for any unused estate tax exemption to pass to a surviving spouse. Thus, if a husband passes away in 2011 using only \$2 million of his \$5 million estate tax exemption, his surviving spouse would then have \$8 million in federal exemptions, consisting of her \$5 million and the \$3 million of her deceased husband’s unused exemptions. However, this portability provision must be elected, or it will be lost. It is elected on the estate tax return (Form 706) when the first spouse passes away.

SUMMARY OF NEW PROVISIONS

NEW 2010 ACT			
CALENDAR YEAR	ESTATE TAX EXEMPTION / RATE	GIFT TAX EXEMPTION / RATE	GST EXEMPTION / RATE
2010*	\$5 MILLION / 35%	\$1 MILLION / 35%	\$5 MILLION / 0%
2011	\$5 MILLION / 35%	\$5 MILLION / 35%	\$5 MILLION / 35%
2012	\$5 MILLION / 35% (indexed for inflation)	\$5 MILLION / 35% (indexed for inflation)	\$5 MILLION / 35% (indexed for inflation)
2013**	\$1 MILLION / 55%	\$1 MILLION / 55%	\$1 MILLION / 55%

*** In 2010, there is an option to be exempt from federal estate tax with a carry-over basis for income tax purposes.**

**** Congress must act before December 31, 2012 or we go back to pre-2001 levels.**

Note: There are different rules for resident and non-resident aliens and their spouses.

REVIEWING AND UPDATING YOUR ESTATE PLAN HAS NEVER BEEN MORE IMPORTANT.