

## FEDERAL ESTATE TAX CHANGES TAKING EFFECT ON JANUARY 1, 2009

### *The Estate Tax Law Change*

On **January 1, 2009**, the **Federal Estate Tax Exemption Amount** increases to **\$3.5 million dollars** (from \$2 million in 2008) for a **decendent dying during calendar year 2009**, pursuant to the provisions of the **Economic Growth and Tax Relief Reconciliation Act of 2001 (“EGTRRA”)**.

**EGTRRA** also **repeals the Federal Estate Tax** completely for decedents dying during **calendar year 2010**. In **2011**, the **Federal Estate Tax Exemption Amount** decreases to **\$1 million**.

In addition, the **maximum estate tax rate** remains at **45%** for decedents dying in calendar year **2009**.

The **United States Generation Skipping Transfer Tax Exemption** rises to **\$3.5 million** for decedent's dying during calendar year 2009.

The **Lifetime Gift Tax Exemption Amount** remains at **\$1 million** for calendar year **2009**.

The **Annual Gift Tax Exclusion Amount** in **2009** will be **\$13,000**.

### *What this Means to You*

For persons dying during calendar year 2009, the first \$3.5 million of assets owned by them will be exempt from Federal Estate Tax. This means that more estates of persons dying during 2009 will either not be subject to a federal estate tax or a greater amount of assets in the estate will pass to such person's heirs free of federal estate tax.

### *Formula Credit Shelter Trusts*

In order to save estate taxes for their children, many married couples have signed Wills which provide for the funding of a Credit Shelter Trust (also called a Bypass Trust), upon the death of the first of a husband and wife to die, based upon a formula tied to the Federal Estate Tax Exemption Amount then in effect.

The advantage of this type of estate planning is that any assets passing into a Credit Shelter Trust will **NOT** be subject to federal (or state) estate taxes upon the death of the surviving spouse.

Thus, the rise in the Federal Estate Tax Exemption Amount to \$3.5 million in 2009 provides an opportunity for married persons to reduce the amount of estate taxes ultimately payable by their children when both married persons have died. In order to take advantage of this opportunity, married persons with these type of formula clauses contained within their Wills, must be sure that they have a sufficient amount of assets titled in either their individual names or held jointly between them.

For example, if “Husband A” dies in 2009 with \$1 million of assets titled in his name alone, while his surviving spouse, “Wife B”, has \$6 million of assets titled in her name alone, then, upon the death of Husband A, only \$1 million dollars of assets will pass into the Credit Shelter Trust created under the Will of Husband A and \$2.5 million of Husband A’s \$3.5 million Federal Estate Tax Exemption Amount will have been wasted. If, instead, Husband A had \$3.5 million of assets titled in his name alone at his death, and Wife B had \$3.5 million of assets titled in her name alone, then, upon Husband A’s death, the full \$3.5 million of assets in his name would have passed into the Credit Shelter Trust created under his Will, and upon Wife B’s later death, the full \$3.5 million of assets (or such amount as might have then remained in the Credit Shelter Trust) would pass to their children estate tax free.

### **Overfunding of a Formula Credit Shelter Trust**

It is important to note, however, that the rise in the Federal Estate Tax Exemption Amount in 2009 can inadvertently, by reason of the formula clause in their Wills, cause a greater amount of assets to pass into a Credit Shelter Trust than a married couple might have anticipated when they originally set up their Wills. If a greater amount of assets passes into the Credit Shelter Trust upon the death of the first spouse, then, less assets will pass to the surviving spouse outright. The risk here is that a surviving spouse might not possess control of as many assets as they thought, upon the death of their spouse, since assets passing into the Credit Shelter Trust are managed by Trustees (who can nevertheless be “friendly”) and not by the surviving spouse independently.

### **Married Persons with Disclaimer Wills (rather than Formula Clauses) can likewise benefit from the Increase in the Estate Tax Exemption Amount**

Many married couples do not have Wills which contain the aforementioned formula clause, but instead have “Disclaimer Wills”. A Disclaimer Will allows a surviving spouse to determine, within nine (9) months after the death of a spouse, how much, if any, assets, should pass into a Credit Shelter Trust. The amount of the assets which can pass into a Credit Shelter Trust is likewise tied to the then amount of the Federal Estate Tax Exemption in effect. These couples must also be sure that they have a sufficient amount of assets titled in either their individual names or held jointly between them so as to take advantage of the increased amount of the Federal Estate Tax Exemption Amount in the event of the death of either of them during calendar year 2009.

### **Increase in Federal Estate Tax Exemption Amount May Cause a Greater State Estate Tax to be Paid Upon Death**

Decedents who die in 2009 and who have an estate whose value does not exceed \$3.5 million will not be required to pay a Federal Estate Tax upon death, but their Estates may be required to pay a State Estate Tax.

The reason for this is that many states, such as New York, Connecticut and New Jersey, have their own Estate Tax Exemption Amount, which differ, in amount, from the Federal Estate Tax Exemption Amount. For example, New York State currently exempts only the first \$1 million of assets upon the death of an individual who is domiciled in New York. Therefore, if a New York domiciliary dies in 2009 and the value of their assets do not exceed \$3.5 million in value, their Estate will not be required to pay a Federal Estate Tax, but their Estate will owe a New York State Estate Tax on the value of the assets exceeding \$1 million.

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Likewise, when assets pass into a Credit Shelter Trust, pursuant to either a formula clause or a disclaimer provision in a Will, the Estate of a person who has died in 2009, will owe a State Estate Tax if the assets passing into the Credit Shelter Trust exceed the then amount of the State Estate Tax Exemption Amount in effect.

For example, if a person dies during 2009, and \$3.5 million of assets pass into the Credit Shelter Trust created under their Will, then their Estate will owe a New York State Estate Tax in the amount of \$229,200 because the assets passing into the Trust exceeded the New York State Estate Tax Exemption Amount of \$1 million.

### Conclusion

In light of the increase in the Federal Estate Tax Exemption Amount taking effect on January 1, 2009, it is extremely important for everyone to now carefully review the terms of their Wills, as well as the titles and current values of their assets, so that it can be determined how this increase in the Federal Estate Tax Exemption Amount might effect their Estate Planning.



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