

# ALERT

January 2010

## **2010 - A ONE YEAR REPEAL OF THE FEDERAL TAX & THE GENERATION-SKIPPING TRANSFER TAX**

**F**or those of us who practice in the Trusts and Estates Department of Moritt Hock Hamroff & Horowitz LLP, the beginning of 2010 has brought a surprise: **The Repeal of the Federal Estate and Generation-Skipping Transfer (GST) Taxes for 2010.**

### **DETAILS OF THE NEW LAW**

#### ***NO FEDERAL ESTATE TAX IN 2010/NO GST TAX IN 2010***

For 2010 only, the Federal Estate Tax is repealed for all persons dying during calendar year 2010. In addition, the GST tax (which is a separate tax assessed on assets passing to grandchildren) has also been repealed for transfers occurring during calendar year 2010.

#### **“STEP-UP” IN INCOME TAX COST BASIS IS ELIMINATED FOR 2010 & CARRYOVER INCOME TAX COST BASIS RETURNS FOR 2010**

As with most tax law changes, Congress “giveth” with one hand, and “taketh away” with the other. It is no different with the news that the Federal Estate Tax has been repealed for 2010. In past years, when an individual passed away, the heirs of that individual could always count on receiving a “step-up” in income tax basis (to the date of death value) with respect to any inherited asset. The impact of this to the heirs was a reduction in the amount of capital gains tax paid when that asset was later sold.

In 2010, “step-up” in income tax basis is eliminated. Instead, heirs will inherit a new income tax basis equal to the lower of the decedent’s existing income tax basis (called “carryover” basis) or the fair market value of the asset as of the date of the decedent’s death. However, to mitigate some of the capital gains tax consequences upon a later sale of the asset inherited by the heirs, an Executor of an estate may allocate: (i) up to \$1.3 million to increase the income tax basis of a decedent’s assets among any beneficiaries, and (ii) up to \$3 million to increase the income tax basis of a decedent’s assets which pass to a Surviving Spouse, either outright or in certain marital trusts.

#### **FEDERAL ESTATE & GST TAXES RETURN IN 2011**

Unless Congress acts, on January 1, 2011, the Federal Estate and GST Taxes will return with only a \$1 million exemption and a top taxable estate tax bracket of 55% (above \$1 million).

#### **THE FEDERAL GIFT TAX REMAINS IN EFFECT**

Still in effect, however, for 2010, is the Federal Gift Tax. Also, the Federal Gift Tax Exemption Amount (that amount which may be transferred free of federal gift tax during a person’s lifetime) remains at \$1 million. However, the top gift tax bracket for lifetime gifts transferred in excess of \$1 million has been reduced to 35% (down from 45% in 2009) for gift transfers made during calendar year 2010. In 2011, the top gift tax rate will climb to 55%, with the \$1 million exclusion still in effect.

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Any questions concerning the matters raised in this Alert should be addressed to the members of our Tax and Trusts and Estates practice groups.

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## **INADVERTENT STATE ESTATE TAX MAY RESULT ON THE DEATH OF THE FIRST TO DIE OF SPOUSES**

An unintended consequence of the elimination of the Federal Estate Tax for 2010 may be the payment, to a decedent's state of residence, of a State Estate Tax upon the death of the first to die of spouses residing in certain states, such as New York and New Jersey. For example, if a New York or New Jersey decedent created a Qualified Terminable Interest Property (QTIP) Trust in his or her Will for their spouse, New York and New Jersey will subject that trust to an estate tax upon the death of the first to die in 2010. You should consult with your Estate Planning attorney to discuss whether this issue impacts you and your family.

### **STEPS YOU SHOULD TAKE**

- (1) **Review your estate planning documents (i.e.: Wills and Revocable Trusts) for language to see if the following types of tax concepts are utilized in your documents:**
  - **Applicable Credit Amount**
  - **Minimum amount necessary to reduce my Federal Estate Tax to Zero**
  - **The Amount required as a Marital Deduction to reduce to zero the Federal and State estate tax**
  - **Maximum Marital Deduction**
  - **Unused GST Amount**

These types of tax concepts are no longer applicable for persons dying during calendar year 2010. As a result, the interpretation of these tax concepts is currently unknown. Therefore, your estate planning documents may no longer dispose of your assets in the manner you intended when your documents were drafted. Also, potentially unintended estate tax may now have to be paid to your state of residence upon the death of the first of two spouses to die.

- (2) **Be aware that at some time later in calendar year 2010, Congress could retroactively reinstate the Federal Estate and GST Taxes for persons dying during 2010. Congress could also reinstate "step-up" in income tax basis.**
- (3) **Gather and permanently maintain all Cost Basis Information for all of your assets.**
- (4) **Please consult with your Estate Planning Attorney as to whether or not changes are needed in your estate planning documents.**

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### **IRS Circular 230 Disclosure**

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