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Estate Planning in Light of No Estate Tax in 2010 ©

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Disclaimer: the following is general information and is **not** legal or tax advice. Competent legal and tax counsel should be obtained **before** taking any action.

I. Important Points

- A. In 2001, Congress enacted the Economic Growth and Reconciliation Act which is coming back to haunt us. For the years 2001 – 2009, the law provided for periodic increases in the estate tax exemption as follows:

Years	Estate Tax Exemption Section 2010(c)	Highest Estate Tax Rate Section 2001 Section 2001(c)(2)
2001	\$ 675,000	55%
2002	\$1,000,000	50%
2003	\$1,000,000	49%
2004	\$1,500,000	48%
2005	\$1,500,000	47%
2006	\$2,000,000	46%
2007	\$2,000,000	45%
2008	\$2,000,000	45%
2009	\$3,500,000	45%

2010 **No Federal Estate Tax or Generation-Skipping Tax; Carryover basis is generally used with two exceptions**

2011 Revert back to \$1 mil exemption 55%

- B. Many people automatically assume that no estate tax means no taxes!
1. **Actually the new law in effect now may cause taxes to increase due to the no step-up in basis general rule. See Section 1014(f) and Section 1022.**

2. Section 1022(a) provides that property acquired from a decedent dying after December 31, 2009 shall be treated as transferred by gift and shall have a basis of the **lesser of**: (a) the adjusted basis of the decedent; or (b) the fair market value of the property at the date of the decedent's death.
 3. Basis can be increased as provided in Section 1022 (b) and (c), noted below.
- C. Most people thought Congress would have acted before now to enact legislation that made 2009's rules permanent or revise them slightly.
1. Various proposals have been made to amend the estate and gift tax rules.
 2. Some have suggested that any revised rules will be made retroactive to January 1, 2010; others have opined that a retroactive provision would be unconstitutional and would be challenged.
 3. Others have suggested Congress will not act so the estate tax rules will revert back – an automatic tax increase without Congress taking more action.
 4. How long will this period of uncertainty last?

II. What are the Problems?

- A. With a potential estate tax liability, a common estate plan would provide for the creation of a residuary trust, to be funded to the extent of the exemption amount. The residuary trust may be referred to as the credit shelter trust, the bypass trust, the family trust, or the B trust. Any portion of a taxable estate in excess of the exemption amount would pass to the surviving spouse, either outright or in trust and qualify for the marital deduction so the estate of the first spouse to die will incur no estate tax.
1. With no federal estate tax and no step-up in basis, would the testator-decedent still want the common estate plan?
 2. Note the specific language used in the Will or trust. Does it refer to tax concepts used in the Internal Revenue Code? Without a federal estate tax, how will/should such words be interpreted?
 3. Does the Will or trust contemplate the repeal of the federal estate tax?
- B. In 2010, carryover basis is now the general rule. See Section 1022. However, it does provide a couple of exceptions.
1. Basis of other property can be increased by \$1.3 million. See Section 1022(b). For a "decedent nonresident not a citizen of the United States," \$60,000 is to be substituted for \$1.3 million.

2. Another exception allows basis of “qualified spousal property” to be increased by another \$3 million. See Section 1022(c). **“Qualified spousal property” means “outright transfer property” or “qualified terminable interest property.”** Will there be a surviving spouse?
3. The \$1.3 million, \$60,000 and \$3 million amounts are to be adjusted for inflation. See Section 1022 (d)(4).
4. Consider how the basis increase should be allocated among various assets. **The executor will allocate the step-up in basis allocation** in accordance with Section 6018 in effect for 2010. See Section 1022(d)(3).
5. Section 6018(c) requires the executor to report to the IRS:
 - a. The name and TIN of the recipient of the property;
 - b. An accurate description of the property;
 - c. The adjusted basis of such property in the hands of the decedent and its fair market value at the time of death;
 - d. The decedent’s holding period for such property;
 - e. Sufficient information to determine whether any gain on the sale of the property would be treated as ordinary income;
 - f. **The amount of basis increase allocated to the property under subsection (b) or (c) of section 1022;** and
 - g. Such other information as the Secretary may by regulations prescribe.
6. Section 6018(e) requires the executor to report to each person (who was reported to the IRS by the executor) both the name, address and phone number of the executor and the information required by Section 6018(c). Such information shall be furnished not later than 30 days after the date the return required by Section 6018(a) is filed.
7. Any change in the allocation of basis increase reported to the IRS may be changed on as provided by the Secretary. See Section 1022(d)(3)(B).

III. What are the Solutions?

- A. Some states are enacting new state statutes that provide that if a Will or trust refers to “unified credit”, “estate tax exemption” “applicable exemption amount,” “applicable credit amount,” “marital deduction,” “maximum marital deduction”,

etc. the Will or trust shall be interpreted to reflect the federal estate tax and generation-skipping tax in effect on December 31, 2009.

1. This is what Georgia did. See SB 461 passed the General Assembly on April 29 and will be sent to the governor for approval. If approved, SB 461 will take effect upon signature (retroactive in effect to January 1, 2010).
2. Georgia law affects the interpretation of Wills and trusts of Georgia decedents. It does **not** change the federal estate tax rules.

B. Wills and trusts should be reviewed and be amended if appropriate

1. With no federal estate tax and no carryover basis (with exceptions), does the common estate plan make sense?
 - a. Should the Will or trust be rewritten completely?
 - b. What if the Will or trust is rewritten, and Congress acts thereafter imposing a federal estate tax similar to the 2009 rules?
 - c. Will any new rules be retroactive or not?
 - (i) Some say yes and any constitutional challenge to the retroactive effect will be rebutted. U.S. v. Carlton, 512 U.S. 26 (1994).
 - (ii) Others say no, especially as more time lapses before a new law is enacted.
 - (iii) Some suggest executors of 2010 estates will be allowed to elect to use either the new law or the law as written.
3. Should a Will or trust be amended to give the executor or trustee power to make distributions as they see fit to minimize taxes?

C. Can disclaimers be used?

1. Possibly in a harmonious family when everyone acts to ensure the decedent's wishes are carried out.
2. Greed and family disputes may not allow disclaimers

D. Action Points

1. Plan for the worse and hope for the best
2. One can sit there and do nothing OR one can be proactive

3. Any planning is only as good as the information and assumptions on which it is based – if the information or assumptions are wrong, the planning may be wrong
 - a. Get the relevant information
 - b. State your assumptions and have clients confirm whether they are accurate or not
4. Document tax basis now before someone dies or memories fade
5. Consider:
 - a. The current fair market value of each asset
 - b. The current built-in gain or loss
 - c. Whether each asset is expected to appreciate or depreciate
 - d. Consider who is likely to receive such asset and the likelihood and timing of them selling it
 - e. Consider the tax brackets of beneficiaries and future tax rates

E. Planning Opportunities

1. Review Wills and trusts as they exist now. Do they make sense now?
2. A Last Will and Testament only governs the distribution of probate assets.
3. Coordinate the distribution of probate assets with the distribution of non-probate assets.
4. What are non-probate assets?
 - a. Jointly owned assets with a right of survivorship
 - b. Assets for which a beneficiary is designated – insurance policies, IRAs, 401(k), pension plan
 - c. Assets within a trust, whether revocable or irrevocable
5. Consider the pros and cons of using a:
 - a. Irrevocable life insurance trust
 - b. Family limited partnership
 - c. Grantor retained annuity trust

IV. Other Important Questions

- A. Regardless of whether an estate tax or generation-skipping tax is imposed, people should consider many important questions including:
1. What do they want to do with their property? What are they trying to accomplish? What is important to them?
 - a. Taking care of their own financial security?
 - b. Helping others?
 - c. Can you help too much?
 - (i) Warren Buffett has said he wants to give his kids so much that they can do anything they want, but not so much that they can do nothing.
 2. Who should receive a bequest? Why?
 3. What should be the amount of the bequest?
 4. How should the bequest be made - outright or in trust?
 - a. If in trust, when should distributions be made?
 - b. Are the trust distributions mandatory or optional?
 - c. Under what circumstances can the trust distributions be cut-off? When can they be resumed?
 - d. Who should be the trustee? Individual or corporate trustee?
 5. Should any amount be given to charity? If yes, how?
 - a. Outright bequest
 - b. Charitable remainder trust
 - c. Charitable lead trust
 - d. Private Foundation
 6. Should any gifts be made during lifetime?
- B. Final Thoughts
1. Watch Congress – will they enact new rules in 2010?

2. Wait broke the wagon. Lead, follow, or get out of the way – do something.
3. Every individual is unique. Every family is different.
4. There is no right or wrong. Forget about what others do.
5. What do your clients and you want to do?

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Dennis Gerschick has a unique background. He is the only individual who is an Attorney, CPA, Chartered Financial Analyst, and Venture Capitalist and has work experience in each field.

Mr. Gerschick graduated Florida Atlantic University in 1978 (major in accounting). He passed the May, 1978 CPA exam on his first attempt. He then worked as a CPA with Ernst & Young, one of the Big 4 accounting firms, before graduating from Drake Law School in 1983.

After law school, Mr. Gerschick worked in the tax department of one of Atlanta's largest law firms, Powell, Goldstein. Later, Mr. Gerschick opened his own law firm. His practice focused on representing closely-held businesses and their owners. For many clients, he also acts as a business and financial advisor.

Mr. Gerschick is the President of VenCap Advisory Group, Inc. which is the sole general partner of VenCap Opportunities Fund, L.P., a venture capital fund. Mr. Gerschick's duties include finding companies in which to invest, reviewing and evaluating hundreds of business plans, as well as negotiating, structuring, documenting, and monitoring the fund's investments. He has also served on several boards of directors and audit committees.

Mr. Gerschick served on the American Institute of CPA's Business Valuation Subcommittee.

Mr. Gerschick also provides a variety of legal and consulting services. He provides tax, investment, financial and business advice to a variety of companies and investors. He consults with other CPAs and attorneys to help them better serve their clients, or he provides a second opinion. See www.Gerschick.com

Mr. Gerschick speaks frequently at seminars and conferences throughout the country regarding a variety of investment, legal, and tax topics. He has spoken about the purchase or sale of a business, real estate, corporate governance, financing businesses, financial statement analysis, and many other topics. See www.RegalSeminars.com

Mr. Gerschick has written many articles, relating to growing and financing businesses that have been published by the Technology Law Section of the Georgia Bar and the Michigan Association of CPAs. Mr. Gerschick has authored two monographs, [Raising Capital](#) and [Attracting Investors to Your Start-Up](#), both of which are offered by the Capital Formation Finance Institute in Washington DC. See www.cfi-institute.org. An interview with Mr. Gerschick was also published in [American Venture](#), a magazine targeted at entrepreneurs and accredited investors.