

# THE MASTERS

## WEALTH MANAGEMENT GROUP

### THE BIG ESTATE PLANNING QUESTION OF 2011

*Should you exploit the new \$5 million lifetime gift exemption?*

Provided by Gary C. Mastrodonato, CEA

In late 2010, Congress reunified the estate tax, gift tax and generation-skipping tax (GST), giving them all top rates of 35% with \$5 million lifetime individual exemptions.<sup>1</sup>

In addition, the estate and gift tax exemptions are now portable between married couples. Upon the death of one spouse, the executor of the estate can elect to transfer any unused portion of the \$5 million individual exemption to the surviving spouse.<sup>1</sup>

At the moment, these tax rates and generous exemptions apply through 2012. In 2013, things may change. So estate planning and tax planning professionals are alerting their clients of this window of opportunity.<sup>2</sup>

**The big news: the \$5 million lifetime gift tax exemption.** For married couples, the lifetime gift tax exemption is actually \$10 million thanks to the portability factor. In 2010, the lifetime gift tax exemption was down at \$1 million - and it wasn't portable.<sup>3,4</sup>

If you used up the prior \$1 million lifetime gift tax exemption before 2011, you now can gift up to \$4 million more before 2013 given the new \$5 million limit. (The lifetime gift tax exemption will be indexed for inflation beginning in 2012).<sup>2</sup>

So considering all this, the big question is: should you give away as much as you can to your children before 2013 with the intent of reducing inheritance taxes down the road?

After all, lifetime gifts reduce your taxable estate. Additionally, if you give your children appreciated securities, the long-term capital gains of those securities will be taxed at their capital gains rates rather than yours. If your children's income puts them in the 10% or 15% tax bracket, their capital gains tax rate is 0% through 2012.<sup>1,4,5</sup>

**Portability means great flexibility - provided you play by the rules.** Let's illustrate how this works. Dad doesn't gift up to \$5 million during his lifetime - he only ends up gifting \$3 million. Well, Mom can subsequently gift up to \$7 million after he passes thanks to the portability rules, as there would still be \$7 million to go toward the \$10 million lifetime gift tax exemption for a married couple.

There is an important rule you must follow to realize this portability: when the first spouse passes away, the executor of his or her estate must file an estate tax return even if no estate tax is owed. That estate tax return formally notifies the IRS that you are transferring the unused or partially used gift tax exemption.<sup>4,6</sup>

Incidentally, this estate tax return is due nine months after the death of said spouse, with a six-month extension permissible.<sup>6</sup>

**Do families need bypass trusts anymore?** We can't say goodbye to them, because 15 states still levy their own estate taxes with exemptions commonly at \$1 million or under. Moreover, who knows if portability will be permitted five or ten years from now?<sup>6</sup>

**The potential for savings could be great.** When you look at this remarkably generous lifetime gift tax exemption allowance in light of certain estate planning techniques that might leverage it - such as the grantor-retained annuity trust and the family limited partnership - the potential is intriguing.

**The problem: we don't yet know what 2013 will bring.** Yes, Congress could retain the \$5 million lifetime individual exemption and portability for 2013 and beyond. Yet if Congress lets this sunset, we're back to a \$1 million individual lifetime gift tax exemption with no portability. So, estate and tax planning professionals must again weigh the degrees of opportunity and ambiguity presented in our shifting estate tax laws.



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**Keeping Families & Generations Together**

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### **Citations.**

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