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GDB Legal Update

SPECIAL EDITION

TAX LAW CHANGES FOR 2011

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Tax Law Changes for 2011

By David N. Milner, Esq.

On December 17, 2010, President Obama signed the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (the "Act") into law. The Act impacts virtually all taxpayers.

The Act delays the expiration of the Bush Era Tax Cuts that would have otherwise occurred on December 31, 2010, for two years. This means that: income tax rates will remain the same in 2011 and 2012 as they were in 2009; long term capital gains and qualifying dividends will continue to be taxed at a 15% tax rate (a 0% rate in certain situations); the Child Tax Credit that would have been reduced to $500 after 2010 will continue at $1,000 and can be used against regular income tax and the alternative minium tax; and the Dependant Care Tax Credit will continue, as will various education and other incentives that were scheduled to expire. Many business and individual tax breaks that had expired at the end of 2009 have been retroactively reinstated and extended through 2011.

The Act provides new incentives for businesses permitting 100% bonus depreciation for certain property acquired and placed in service after September 8, 2010 and before January 1, 2012, and 50% bonus depreciation for property acquired and placed in service after December 31, 2011 and before January 1, 2013. The Act increases the available exemption from the alternative minimum tax.

For 2011 the Act reduces the Social Security tax paid by employees on wages received from their employer from 6.2% to 4.2%, and from 12.4% to 10.4% for those having self-employment income. Unchanged is the maximum amount subject to Social Security tax, which remains at $106,800 for 2011. It is important to note that the employer's contribution remains at 6.2%, and the obligation to pay the Medicare portion remains unchanged.

Perhaps the most significant changes made by the Act are to our system of Estate and Gift taxation. The Act reintroduces the Estate Tax for those decedents that die in 2011 and 2012. For those that died in 2010, their personal representative will have the ability to have the estate pay no federal estate tax at the expense of having a limited ability to increase the tax basis of the decedent's assets for income tax purposes. As an alternative, the personal representative can elect to have the new 2011/2012 rules apply, in which event there will be no limitation on the ability to increase the income tax basis of the decedent's assets to their value on the decedent's date of death.

The 2011/2012 rules provide for a "unified" $5 million exemption for lifetime transfers (i.e., gifts) or transfers upon death. Beginning in 2012 the exemption is indexed for inflation. The generation-skipping transfer tax exemption has also been increased for 2011 and 2012 to $5 million. The maximum tax rate for gifts, estates and generation skipping transfers is 35%. Of particular significance is the subtle change which permits a surviving spouse to utilize that portion of their deceased spouse's exemption that was not used by the deceased spouse. This provision effectively permits married couples to shield up to $10,000,000 of assets from gift and estate taxation, regardless of ownership.

The term "unified" effectively means that, beginning in 2011, individuals have the ability to transfer up to $5 million of assets, either while they are alive or upon their death, to someone other than their spouse without being required to write a check to the IRS. Unchanged is the ability of individuals to transfer as much of their assets as they would like to their spouse without incurring any gift or estate tax liability.

For example, if John made taxable gifts of $1,000,000 prior to 2011 (which was the most that could be made without incurring a gift tax liability), beginning in 2011, John can make additional gifts having a cumulative value of $4,000,000 without being required to write a check to the IRS. If John only makes additional gifts having a value of $500,000 while he is alive, and if John were to die in 2011 or 2012, the remainder of John's unified exemption will be available to shield assets having a value of $3,500,000 from estate taxation. If John dies leaving assets having a value of only $1,500,000, the balance of his $5,000,000 exemption ($2,000,000) will be available to his wife, effectively permitting her to shield up to $7,000,000 of assets from gift or estate taxes.

It is important to keep in mind that these changes only impact upon those who die in 2011 or 2012, or who died in 2010 if their personal representative elects to have the new rules apply. As the law presently stands, beginning in 2013, the exemption will revert to $1,000,000, and the maximum federal estate tax rate will be 55%.

These changes to our system of gift and estate taxation significantly impact upon the manner in which estates should be planned. We urge our clients to contact us to review their estate plans to determine whether any changes or modifications are warranted. Our tax and estate planning attorneys, David Milner, Esq., and Seymour Reich, Esq., can provide you with legal advice on these issues.

About the author: *David N. Milner is a partner at Gallet Dreyer & Berkey, LLP. Mr. Milner's practice focuses on tax law, estate planning, corporate law, and real estate. Mr. Milner, who is also a certified public accountant, helps clients to structure transactions in a manner calculated to reduce adverse tax consequences and helps families develop estate planning strategies.*