Wealth & Succession Planning

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BURKE, WARREN, MACKAY & SERRITELLA, P.C.

TAX ALERT

On December 17, 2010, President Obama signed the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010, making significant changes to Federal tax laws. The Act received wide publicity because it extended current income tax rates for all taxpayers through 2012. The Act also made significant changes to estate, gift, and generation-skipping transfer (GST) tax laws. These changes provide you with new estate planning opportunities, which may only be available for a limited amount of time.

Changes to Estate, Gift, and GST Taxes

Estate Tax Exemption and Rate. The Federal estate tax exemption amount (the amount that may be transferred at death free of Federal estate tax) has been increased to $5 million for each taxpayer (or $10 million for a married couple) with a maximum estate tax rate of 35%.

Gift Tax Exemption and Rate. The Federal gift tax exemption amount (the amount that may be transferred during life free of gift tax) has been increased from $1 million to $5 million for each taxpayer. This means that a married couple may transfer up to $10 million in assets, gift tax free, for the benefit of children, grandchildren, or other beneficiaries. Gifts over this amount are taxable at a top rate of 35%.

Generation Skipping-Transfer Tax Exemption and Rate. The GST tax exemption amount (the amount that may be transferred over multiple generations free of transfer tax) has also been increased to $5 million for each taxpayer (or $10 million for a married couple). The GST tax rate has been reduced to 35%.

Window of Opportunity

If Congress does not enact new legislation by December 31, 2012, then the pre-2001 rules (*e.g.*, only a $1 million estate and gift tax exemption with a top 55% rate) will return effective January 1, 2013. This means that you may only have a two year window of opportunity. Following are steps to take advantage of the increased gift and GST tax exemption amounts during this timeframe:

- **Outright Gifts:** Make outright gifts to children and more remote descendants.
- **Gifts in Trust:** Make gifts to GST tax exempt trusts for the benefit of children and more remote descendants. Utilizing assets you expect to appreciate significantly in the future increases the tax savings of such a gift.

- **Forgive Loans:** If you have made loans to children or others, consider forgiving such loans thereby using a portion of the increased gift tax exemption.

- **GRATs:** Use a grantor retained annuity trust (GRAT) when making a gift. A GRAT is a trust to which you gift assets, retaining the right to receive an annuity from the trust for a certain period of time. Upon the termination of such period, the GRAT assets pass in trust for children free of estate and gift tax. Although there were fears that the Act might include provisions that would curtail the use of GRATs, such provisions were not included. GRATs remain an excellent wealth transfer tool, particularly in light of continuing historically low interest rates.

- **Irrevocable Grantor Trusts:** Use an irrevocable "grantor" trust to make a large gift to a trust. Under the grantor trust, the assets of the trust are not subject to estate, gift, or GST taxes, but you pay the income tax on trust income, thus maximizing the amount being transferred from your taxable estate to the beneficiaries. You can also consider selling additional assets to the trust, without triggering capital gains tax.

Illinois Estate Tax

Although the Federal estate tax exemption was raised to $5 million per taxpayer, in January, 2011, Illinois enacted legislation setting the Illinois estate tax exemption at only $2 million per taxpayer. Consequently, it is very important to review your estate plan to be certain that it is structured to avoid not only Federal estate tax at the death of the first spouse to die, but also Illinois estate tax. It is also important that the asset holdings of spouses are structured to take advantage of each spouse's $2 million Illinois exemption amount. While spouses with assets of $5 million may escape Federal estate tax, if their plans are not properly structured, an Illinois estate tax of approximately $352,000 will be payable upon the survivor's death.

If you would like to discuss these opportunities, please contact me at 312-840-7009.

Karen K. MacKay

BURKE, WARREN, MACKAY & SERRITELLA, P.C.

330 North Wabash Avenue, 22nd Floor
Chicago, Illinois 60611-3607
312/840-7009 PHONE • 312/840-7900 FAX
kmackay@burkelaw.com • www.burkelaw.com