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## CLIENT NEWSLETTER

On December 17, 2010 President Obama signed into law the "Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010" (TRUIRJCA). The new law:

- Extends for two years the current income tax rates and other income tax rates commonly called the "Bush Tax Cuts."
- Provides tax incentives to businesses
- Cuts federal estate and gift taxes for two years
- Extends unemployment benefits

In this newsletter, we will review some of the key points of the new law.

### ESTATE PLANNING

A temporary federal estate and gift tax law, in place since 2001, was set to expire on January 1, 2011. The new law extends and modifies the federal estate and gift tax for two years. Key provisions are:

- *\$5 Million Unified Estate and Gift Exemption.* For calendar years 2011 and 2012 individuals will be able to transfer, during life or at death, \$5 million to children and others tax-free. Transfers to a spouse or a charity remain tax-free.
- *Exemption Portability.* A spouse's unused \$5 million exemption can be used by a surviving spouse.

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- 35% Tax Rate. The maximum estate tax bracket is reduced to 35% on the value of taxable estates exceeding \$5 million.
- \$5 Million Generation Skipping Tax (GST) Exemption. For calendar years 2011 and 2012 individuals will be able to transfer, during life or at death, \$5 million to free from GST tax, either in trust or directly to younger heirs. Like the estate and gift tax, the maximum bracket on generation skipping transfers in excess of the exemption will be reduced to 35%.
- 2010 GST Tax "Holiday". For trusts known as "generation skipping trusts" that were created in 2010, the tax rate will be zero percent (e.g., not taxed) in perpetuity.
- 2010 Decedents. For decedents who passed away in 2010, estates are given a nine months extension of time from the date of enactment to file estate tax returns.

On January 1, 2013 the law is scheduled to revert to a \$1 million estate tax exemption and 55% maximum tax rate of pre-2001 law.

**What should you do?** For many, an estate that was well planned under prior law will remain the recommended route through 2012. The new law is temporary and existing plans should not be changed in haste. However, if you have not reviewed your estate plan for several years, the recent changes are a good reason to take a fresh look to make sure that the plan still does what you want it to do.

Married couples should continue the use of a trust, usually called the "family" or "bypass" or "credit shelter" trust, to minimize federal and New Jersey estate taxes for children and grandchildren. New Jersey continues to impose an estate tax which can be reduced or eliminated through the use of trusts. Also, trusts provide important benefits beyond tax planning, including asset preservation and protection.

"Portability" of the estate tax exemption allows a spouse to leave any unused available exemption to a surviving spouse, increasing the survivor's estate tax exemption. While a taxpayer friendly change, it is not automatic and does not eliminate the need for a well planned estate. Portability does not allow for inter-generational planning and it does not minimize a family's New Jersey estate taxes.

Spouses should continue to balance assets between them in order to limit estate tax consequences and they should use trusts to minimize the transfer tax cost as has been popular for the last half century. We also suggest that, at least for the short term, families continue to stay the course

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in existing estate plans through the use of trusts for the benefit of the surviving spouse. Again, there are many circumstances where trusts serve other benefits rather than just tax planning.

For larger estates there are also extremely important changes to the Generation Skipping Transfer Tax which previously prevented large transfers of wealth from generation to generation without estate taxation at each generational level. The new law offers to families with substantial wealth, a unique opportunity to plan lifetime multi-generational transfers during 2011 and 2012.

However, before families make large scale wealth transfers for gifting, they should consider the income tax ramifications of their gifting plan. While the \$5 million gift tax exemption allows large lifetime transfers, these can be negative income tax consequences to the recipients. The appreciated value of a gifted asset is subject to income tax, payable by the donee on the sale of a gifted asset. In contrast, the basis of an inherited asset is generally “stepped up”, avoiding income tax on the appreciated value of the inherited asset.

In a nutshell, the recent estate and gift tax revisions are temporary and the New Jersey estate tax remains unchanged. Your foundational estate plan can remain intact for the short term. However, if you have questions about how the new law impacts you and your family, if you have had changes in your life that may affect your estate or if your estate plan has not been reviewed in several years, you should consider reviewing your plan.

### INCOME TAX

- ***Individuals.*** The following have been extended through December 31, 2012:
  - ***Rates.*** All income tax rates for individuals (10, 15, 25, 28, 33, and 35%), as well as for estates and trusts stay the same. The maximum rate on long-term capital gains and qualified dividends will remain 15%.
  - ***Payroll Tax.*** The new law reduces the employee share of the OASDI portion of Social Security taxes from 6.2% to 4.2% for a maximum tax benefit of \$2,136.
  - ***Limitations and Phase outs.*** The itemized deduction (or “Pease”) limitation and the personal exemption phase-out stand repealed. The standard deduction and the size of the 15% bracket for married couples will stay double that of single filers.
  - ***Credits and Deductions.*** Most credits and deductions set to expire in 2010 have been extended, including: Child Tax Credit, Earned Income Tax Credit, American Opportunity Tax Credit, Adoption Credit, Dependent Care Credit, Employer-Provided

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Child Care Credit, Mortgage Insurance Premium Deduction, Student Loan Interest Deduction, etc.

- **Alternative Minimum Tax.** The AMT has been “patched.” In other words, the exemption amounts have been temporarily raised (\$47,450 for individuals, \$72,450 for joint filers).
- **Businesses.**
  - **Bonus Depreciation.** For qualified investments made after September 8, 2010 and before January 1, 2012, businesses may take 100% bonus depreciation in the first year property is put into service. For investments made in 2012, 50% bonus depreciation is allowed (100% for 10+ year and transportation property).
  - **Section 179 Expensing.** The Small Business Jobs Act increased the dollar limit to \$500,000 and the investment limit to \$2 million for 2010 and 2011. The new law provides for a \$125,000 dollar limit and \$500,000 investment limit for 2012. Off-the-shelf-computer software will continue to be treated as qualifying property until 2013.
  - **Small Business Stock.** The Small Business Jobs Act provided for an exclusion for non-corporate taxpayers of 100% of the gain from qualified small business stock acquired after September 27, 2010, before January 1, 2011, and held for at least five years. The new law extends 100% exclusion through 2011.
  - **Credits.** The Research Tax Credit and the Work Opportunity Tax Credit are extended until December 31, 2011.

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