Tax Law Changes Create Planning Opportunities

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How can estate taxes affect your family? In 2008, the Dow was down 33.8%, the S&P 500 dropped 38.5% and the Nasdaq plummeted more than 40%. It was a bad year. Imagine feeling the effects of last year's losses in just one day. With federal estate tax rates ranging from 37% to 45%, your family could lose more in a single day than during the storm we weathered in all of 2008. Proper planning is essential, and the current economic environment and recent changes in the law offer some tremendous opportunities to minimize taxes.

Estate and GST Tax Applicable Exclusion Amounts Increased to $3.5 Million

On January 1, 2009, the applicable exclusion amount for federal estate tax and generation-skipping transfer tax was increased from $2 Million to $3.5 Million. The maximum federal estate tax rate remains at 45%.

With the economy showing little sign of improvement, the combination of lower asset values, reduced interest rates, and the prospect of estate and gift tax reform presents a unique opportunity for estate planning techniques that may yield significant tax savings. Many commentators predict that Congress will pass an estate tax reform package in 2009 that, while benefiting some, may place an onerous burden on others. Now is the time to capitalize on tax planning techniques that are still available and extraordinarily effective under current economic conditions.

Family Limited Partnership Discounts

New legislation has been introduced in Congress to eliminate the discounts that may be available for gifts of partnership assets. Plans involving such an entity should be implemented or reviewed as soon as possible to help ensure that gifts will be "grandfathered" under existing law.

Gift Tax Annual Exclusion Increased to $13,000

The gift tax annual exclusion, which is the amount donors can give to individuals and certain trusts each year, has increased from $12,000 to $13,000. The gift tax annual exclusion gives individuals an opportunity to transfer assets and reduce the size of their taxable estates without incurring tax liability. The increased amount, paired with lower asset values resulting from the current economy, offer a unique chance to maximize the benefit of tax-free gifts.

Contribution Limits for Retirement Plans Increased

Many retirement plan limitations were changed for 2009 due to cost-of-living index increases. Effective January 1, 2009, the limitation for elective deferrals to 401(k) plans increased from $15,500 to $16,500, and the limitation for total annual allocations to defined contribution plans for participants under 50 increased from $46,000 to $49,000. "Catch-up contributions" for individuals 50 or over increased from $5,000 to $5,500. There is no change to the limit on the amount an individual can contribute to an IRA, which remains $6,000 for individuals born before 1960 and $5,000 for those born after 1960.

Required Minimum Distributions Suspended for 2009

Ordinarily, retirement account owners and participants are required to begin taking annual minimum distributions no later than April 1 of the year following the year they attain age $70^1/_2$. However, the Worker, Retiree, and Employer Recovery Act of 2008 suspends required minimum distributions ("RMDs") for 2009 only. Anyone age $70^1/_2$ or older in 2009 need not take a 2009 RMD by April 1, 2010, but must still take a RMD for 2010.

The suspension allows taxpayers to forgo all or part of their required distribution for 2009 without penalty, creating an opportunity to lower 2009 taxable income.

Historically Low Rates and Depressed Real Estate Markets

Grantor retained annuity trusts or "GRATs" are trusts used to make future gifts of appreciating property to children and grandchildren on a virtually tax-free basis. The current historically low interest rates make it more likely that trust assets will appreciate at a rate faster than the current "applicable federal rate" or AFR, and the excess appreciation transfers to children and grandchildren tax-free. However, there is a possibility that changes to the Internal Revenue Code will eliminate gift tax-free GRAT planning. Again, unusual opportunities exist and should be seized quickly.

A Charitable Lead Trust or "CLT" is a trust that pays an amount to charities that you choose and then, after a period of time, the principal is paid to your family. These trusts can minimize any gift or estate tax while providing you (or your estate) with a current charitable deduction. The current low rate climate makes CLTs very attractive.

Low real estate values make this a good time to consider a qualified personal residence trust or "QPRT". A QPRT is a trust that holds a primary residence or vacation home for a set term of years. QRPTs may be used to reduce the size of a taxable estate, while keeping property in the family.

The current economic environment and recent legal developments offer rare opportunities for tax savings, but these opportunities won't last forever. It's important to review your plan now to take advantage of these benefits.

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