



Tax Planning - Part I: Estate Taxes



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I like to quote Ben Franklin to explain why my estate planning practice is recession-proof:

"In this world nothing can be said to be certain, except death and taxes."

The fundamental focus of any Elder Law practice is Estate Planning: Listening to clients and Preparing documents to provide what will happen when a client dies or becomes incapacitated. Believe it or not, I have to consider taxes with every estate plan I do. Taxes I consider include not only gift, estate, and inheritance taxes, but also income and capital gain taxes.

In this article, I'll talk about just the Federal and New Jersey Estate taxes.

During the last decade, the Federal and New Jersey Estate Tax systems have undergone substantial changes. In fact, because Congress failed to pass a tax law in 2009, anyone dying this year (2010) pays NO FEDERAL ESTATE TAX. This has been a boon for several multi-millionaires (such as George Steinbrenner) who

died in 2010. Congress is seemingly just becoming aware of the BILLIONS in lost revenue as a result of this law, and some lawmakers have recently introduced a bill to impose the federal estate tax on estates of people who die in 2010, which would be retroactive to January 1, 2010.

The Federal Estate tax is the "big one." Tax rates have reached and even exceeded 55%, so it is something people want to minimize or avoid altogether. Many people assume incorrectly that they don't have to worry about this tax because it traditionally has applied only to the wealthiest in the nation. Since the exemption amount (then known as the "Unified Credit") had not increased from \$600,000 in many years, in 2001, Congress set in motion a series of increases to the Federal Estate Tax Exemption, moving it from \$600,000 to \$3,500,000 in 2009. The purpose of these increases was to make sure that only the wealthiest would be subject to the FET.

• **The Federal Estate tax is fairly simple:** You can leave an unlimited amount to a spouse at death, free of tax (this is known as the "unlimited marital deduction"). Whatever is not left to

a spouse is taxed if the total amount exceeds the federal limit. As mentioned above, the Federal Estate Tax is effectively repealed in 2010: It is a "good year to die!" In January 2011, however, the federal estate tax exemption will drop down to only \$1,000,000. Thus, estates in excess of \$1,000,000 will be subject to a federal estate tax of up to 55%!

It has been quite a challenge trying to plan to minimize or avoid a tax which changes annually, and, at this point, possibly retroactively! We do have strategies, however, which allow maximum flexibility to set up trusts following the death of the first spouse to die. Most of my clients opt to put "disclaimer" provisions in their Wills, which provide that the surviving spouse can choose, within nine (9) months from the date of the spouse's death, to disclaim assets - so that they do not pass directly to the spouse and remain taxable in his/her estate. The Will provides that any "disclaimed assets" pass into a Trust which the spouse can access for



the rest of his or her life. The key to the trust is that, when the second spouse dies, the assets in the trust are not included in, or taxed in, the surviving spouse's estate.

The beauty of the disclaimer option is that it works to minimize both the Federal Estate Tax and the New Jersey Estate Tax.

Since 2002, New Jersey has imposed its own estate tax on estates valued over \$675,000, at a progressive rate ranging from 4.8 percent up to 16 percent for the largest estates. Prior to 2002, New Jersey received a portion of



the Federal Estate Tax, so there was little discussion of the NJET. In 2002, however, New Jersey "de-coupled" from the FET and we now need to plan to avoid or minimize the NJET as well as the FET.

In the next issue, we will talk about the Federal Gift Tax and the New Jersey Inheritance Tax. The following issue will cover Income Taxation of Retirement Assets, Annuities, and Savings Bonds and the Capital Gain Tax.

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