



## **ESTATE PLANNING IMPLICATIONS OF THE AMERICAN TAXPAYER RELIEF ACT OF 2012**

Happy New Year to you. On January 2, 2013, President Obama signed into law the American Taxpayer Relief Act of 2012 (the "Act"). With respect to estate planning, the Act made permanent the law which had been in effect for 2011 and 2012 (and was due to expire if Congress had not acted) except that the gift, estate and generation skipping transfer (GST) tax rate on transfers above the exemption amount has increased from 35% to 40%. The gift tax, estate and GST tax exemption amount adjusts annually for inflation and increased from \$5,120,000 for 2012 to \$5,250,000 for 2013. Portability of unused federal estate tax exemptions between a deceased spouse and the surviving spouse has now been made permanent as well (i.e., any federal estate tax exemption not utilized when one spouse dies may be used by the surviving spouse or his or her estate, subject to rules governing remarriage and subject to the first deceased spouse's executor making the election on a timely filed federal estate tax return).

As we reported in earlier newsletters (available on our website), the gift, estate and GST exemption was set to be reduced to \$1,000,000 if Congress had not acted. In addition, instead of the 35% flat tax rate in effect for 2011 and 2012, there would have been graduated tax rates up to 55%. Portability of the federal estate tax exemption would have expired.

Faced with the potential for reduced exemptions and increased rates, many of you made significant gifts prior to the end of 2012. Those gifts continue to be good planning. Future appreciation in the value of the gifted assets is removed from the donor's taxable estate. In addition, for our clients who gifted property located outside of Connecticut (or for our clients who are not Connecticut residents), those gifts will reduce the state death taxes to be paid at the donor's death. Finally, for those of you who set up "grantor trusts," the donor's retention of the obligation to pay income tax on the taxable income of the gifted assets can further increase the benefit to the recipient.



The Act also extended until the end of 2013 the opportunity for individuals 70½ years of age or older to make tax-free IRA distributions (up to \$100,000) directly to public charities. This can result in significant tax savings since the distribution is not included in the donor's adjusted gross income (AGI) or subject to phase-out of deductions. In addition, the donor can save on Connecticut income taxes since those are based on the federal AGI. The distribution may be used to meet the taxpayer's required minimum distribution.

While not part of the Act, the gift tax annual exclusion amount will be \$14,000 in 2013, an inflation-adjusted increase from \$13,000 in 2012. This is the maximum amount that an individual can gift to a beneficiary in a calendar year without using gift tax exemption or paying gift tax (subject to exceptions for unlimited gifts to a U.S. citizen spouse or to charity, or the direct payment of tuition or medical expenses). There is no limit to the number of beneficiaries to whom a donor may make annual exclusion gifts. The annual exclusion amount for gifts to a spouse who is not a U.S. citizen increased from \$136,000 to \$143,000.

Although the changes in the estate, gift and GST tax are "permanent," it is always possible that the law could be changed in the future. In addition, President Obama in the past has proposed changes to certain estate planning techniques which could be addressed in the future (such as grantor retained annuity trusts, grantor trusts and family limited liability companies and partnerships). We will of course advise you if there are future changes in the law which may affect your estate planning.

Each of you may wish to consider how the Act affects your planning. If you made gifts in 2012 which used all of your then \$5,120,000 gift tax exemption, you may wish to consider gifting the additional \$130,000 exemption available this year (or twice that amount for a married couple). If you were waiting to make significant changes to your estate plan until there was more certainty in the tax law, now would be a great time to update your plan. If you were inclined to make gifts late in 2012 but did not have enough time, you now have the time to complete those gifts. Lastly, now that portability is permanent, some of you may wish to simplify your plans and leave a greater portion of your estate to your spouse outright (but keep in mind that there are many

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benefits of trusts which cannot be attained with outright gifts, such as taking advantage of the Connecticut \$2 million estate tax exemption, sheltering post-death appreciation from future taxation, managing assets, and protecting assets from future creditors, future spouses and others).

We would be happy to assist you if you wish to make changes to your estate plan or if you wish us to review your plan to see if it makes sense for you in light of the new Act.



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