

Part 1. Congress is Brilliant: Why 99% of "Poor" Taxpayers Now Hold the Short End of the Stick

2-7-14 by James M. Kane, Attorney

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There are estimates that only about 0.14% of estates (14 out of 1000) will now face the threat of paying federal estate tax. This is the result of Congress in early 2013 enacting the inflation-adjusted \$5.0 million federal estate exemption. This is an inflation-adjusted \$10 million combined exemption for married couples. [The state death tax exposure, if any, varies based on each state's laws.]

But, this generous estate tax exemption is a mirage with Congress essentially having now converted our federal death tax into an income tax system. The result is the 99% of "poor" estates that will pay no estate tax now face substantially increased income tax exposure.

With this new income tax system's multi-faceted application, there is no single income tax element that readily spotlights this increased exposure. A brilliant, stealth design.

Instead, this exposure consists collectively of several income tax elements: (i) the compressed trust ordinary income tax rates, the additional 5% capital gains rate, and the 3.8% Medicare investment tax at these compressed trust thresholds and (ii) a

failure to leverage the stepped-up basis as fully as possible at each spouse's death.

Estate planning must now center on income tax planning in order to mitigate this new income tax estate system. My following three comments touch on this new income tax paradigm.

One. We trust & estate lawyers and other estate planning practitioners will, no doubt, continue to assist the top 1% crowd with gift, estate, generation skipping transfer tax ("GST"), and income tax savings opportunities.

There remains a continuing demand within this 1% group for excellent tax planning, in many ways not much different than this group's tax planning needs prior to the recent 2013 tax legislation.

But, our assistance for the other 99% crowd is no less important. Experienced lawyers and practitioners can add tremendous estate planning value for this group by helping reduce this new income tax exposure.

Two. There is presently a disconnect between this need for planning and the awareness of this need by the 99% crowd.

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The focus by both Congress and the media on the generous \$5.0 million estate tax exemption has (temporarily) overshadowed this new income tax system. Also, few within the 99% group have yet felt the financial pinch of these increased income taxes.

Three. Flexibility built into the estate plans for this 99% group is the premium feature that separates excellent planning from mediocre planning.

For example, this requires including sufficient provisions within the estate planning documents so as to enable the opt-in or opt-out of various elective income and estate tax features at each spouse's death (e.g., defective trust status, QTIP elections, stepped-up basis options, powers of substitution, withdrawal rights, disclaimers).

I will continue from time to time with more email alerts that are helpful in raising awareness for income tax savings and other estate planning options for this 99% group.

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