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Review & Fix Estate Plans Before Law Changes Do

By Wayne Eig

In December of 2010, Congress and President Obama came to a compromise on a series of tax law changes affecting income, estate, gift and generation skipping taxes. (For a summary of the more salient changes, see the “Estate & Gift Tax Laws Provide Benefits For Now” blog post by Jeff Kolender, chair of the firm’s Estate Planning and Estate & Trust Administration practice groups.) These modifications generally had the effect of further extending, and in several important aspects, substantially expanding estate tax planning opportunities for many taxpayers. They adopted the now common and dreaded “sunset” provisions of recent tax law, which means that, without further legislative action, these favorable changes will by and large expire and be lost, in this case, at the end of 2012.

Every person should carefully review her or his planning in light of last year’s changes and the opportunities they may afford. Many of the specific tax savings opportunities are described in Kolender’s previously referenced blog post, but some of these same 2010 changes in the law may have unintended effects on existing plans which should also be carefully reviewed. The change in exemption amounts, while generally favorable, sometimes results in someone dispossessing a surviving spouse, a result which could lead to intra-family fighting and even litigation. Similarly, some plans which were intended to benefit both children and grandchildren may now operate to dispossess children in favor of grandchildren, another outcome probably not intended by the client. Ironically, the more “tax-driven” a particular 2010 or earlier plan may be, the more likely that it may have unintended results. There is simply no substitute for a careful review of how pre-2011 plans will operate in 2011 and 2012.

Even with these developments which are generally favorable to taxpayers, there remains considerable support in Congress for the elimination or serious reduction in several tax planning vehicles now available. As such, there is currently a window of opportunity to achieve meaningful tax savings for an undetermined period of time. Proposals have been made (i) to reduce the effectiveness of Grantor Retained Annuity Trusts, or “GRATs,” (ii) to limit the use of Crummey withdrawal powers often included in life insurance trusts, (iii) to significantly curtail the use of multi-generational or dynasty trusts (intended to provide descendants with strong creditor protection qualities) and (iv) to eliminate the use of valuation discounts in family-owned entities.

Finally, there is a series of “non-tax” reasons for reviewing planning, reasons that over time have taken on greater importance to all clients. These include (i) providing children, grandchildren and other beneficiaries with increased creditor protection in the business world and with respect to troubled marriages, (ii) retirement planning, (iii) planning for legal or physical incapacity, (iv) planning when assets are held in more than one state or more than one country, and (v) planning for non-citizens.

The uncertainties surrounding the present law are not causes to postpone or delay, but rather should be seen as invitations - and perhaps even mandates - to revisit your existing plan to make certain it continues to work as intended and to look to take advantage of the favorable provisions now being extended to taxpayers. It is important to be proactive, to act sooner rather than later, in order both to avoid unintended problems and to maximize the benefits available during this limited window of opportunity. Holding off on addressing these matters could very easily work counter to the intentions outlined in the original plan, and might result in you losing - possibly forever - some very favorable opportunities.