

KEY CHANGES IN FEDERAL ESTATE AND GIFT TAX (AND CALIFORNIA NO CONTEST) LAW

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As you probably have heard, there have been significant changes to the federal estate and gift tax laws effective January 1, 2010. Plus, California law was modified in important ways that can affect estate plans. These changes will likely affect you and the structure of your current estate plan.

Repeal of Federal Estate Tax (2010)

The most notable change in the law is the repeal of the federal estate tax. As the law is now written, individuals that die in 2010 will not have federal estate tax levied against the value of their estates. That said, there is much talk by Congress indicating that a new law may be signed by the President sometime this year which reinstates the federal estate tax. It is unclear whether any new law will attempt to be retroactive to January 1, 2010.

The federal generation-skipping transfer tax ("GST") was also repealed. The GST applies to transfers of assets on death or by gift during life. Generally, this was a 45% tax imposed on the transfer of assets to individuals in a lower generation than your children, such as to grandchildren and great-grandchildren.

What this means to you:

You may choose to wait and see if Congress modifies the estate tax law. If no law is enacted, the estate tax will come back into force on January 1, 2011. We recommend you consider scheduling an appointment to meet with your attorney at Procopio if any of the following apply to you or your current estate plan:

- You have any immediate health concerns;
- Your estate plan includes gifts to grandchildren in an amount based on the federal generation-skipping transfer tax exemption;
- Your estate plan provides for the creation of a sub-trust upon your death for the benefit of beneficiaries other than your spouse, potentially resulting in your spouse being unwittingly disinherited; or
- Your estate plan makes gifts tied to the federal estate tax exemption amount, such as gifts utilizing the marital or charitable deduction to reduce federal estate tax.

Limited Increase in Tax Basis at Death

The new law also limits the amount by which the tax basis of estate assets is increased at death. Prior law allowed the tax basis to increase to the full fair market value. Tax basis is the means by which taxable gain is measured upon the sale of an asset when it is sold or disposed of. Prior law provided that the assets generally received a new tax basis in those assets equal to the fair market value on the date of death. This eliminated, or at least reduced the future gain to the heirs that was subject to income tax. The new law, however, limits the amount of basis increase on death to \$1.3 million (plus an additional \$3.0 million for certain assets left to a spouse). All other beneficiaries will generally receive the decedent's basis in the asset; hence will be subject to income tax on the gain from a subsequent sale of the asset to the extent the sale's price exceeds the decedent's carryover tax basis.

What this means to you:

It is more important than ever to keep accurate records that indicate the tax basis of your assets. For instance, if real property was purchased in 1962, those purchase and home improvement documents should be kept for safekeeping.

Decrease in Federal Gift Tax

Effective January 1, 2010, the federal gift tax rate was decreased from 45% to 35%. If Congress acts this year to reinstate that federal estate tax, they may also increase the federal gift tax back to the 45% rate and may be retroactive to January 1, 2010.

What this means to you:

Gifts of assets at this lower rate may save you and your heirs a substantial amount in gift and/or estate taxes. You should discuss whether gifting assets is appropriate for you.

California State Law Now Limits the Enforcement of "No Contest" Clauses

California recently revised its law related to provisions found in some Trusts and Wills commonly referred to as "no contest clauses." Generally, a no contest clause disinherits a beneficiary for contesting a decedent's estate plan or specific testamentary instrument such as a Trust or a Will. Under the new law effective January 1, 2010, no contest clauses will be upheld in only limited circumstances.

What this means to you:

If your estate planning documents contain no contest clauses, you should consider meeting with your attorney at Procopio to discuss whether it continues to work in the fashion it was intended.

Summary

This Client Alert does not provide specific legal advice to your personal circumstances or your estate plan. Please do not hesitate to contact your attorney at Procopio, to make an appointment to discuss whether these changes require further action on your part.

Feel free to contact an attorney from the Trust, Estate and

Probate Practice Group at Procopio, Cory, Hargreaves & Savitch LLP (“Procopio”).
[Procopio Trust, Estate and Probate Practice Group.](#)

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