



Estate Planning: Living Beyond 2010 May Be Taxing!

We are all familiar with the two famous sayings, “The only thing that is constant is change,” and, “Confusion is an enemy of planning.” In 2010, when it comes to estate planning, both of these are true.

When you first examine the fact that Congress did not reinstate an estate tax for 2010, it appears to be positive for the heirs of wealthy parents and of little consequence to anyone else. However, when you analyze the details a little further, you might conclude that Congress has increased the chances that many Americans will owe estate taxes on an inheritance from those who pass on after 2010. Sadly, many current wills and trusts are written with the assumption that there is an estate tax and this could therefore become problematic for a surviving spouse or beneficiary.

Congress has looked at several different proposals to finalize estate tax rules and rates starting immediately (or even retroactively to January 2010).

Here are some things that those of you who have accumulated wealth need to know about the estate tax as well as some suggestions to protect you and your heirs, at least until Congress takes further action.

- The estate tax and generation skipping transfer tax (a tax on assets given to grandchildren) were both repealed under current law at the end of 2009.
- Both the estate tax and the generation skipping tax are scheduled to return in 2011 at the same unfavorable rate that applied 10 years ago. That is, currently for 2011 there will be a \$1,000,000 exemption with up to a 55% tax on the remainder of the estate.

- Currently, there is still a gift tax if you give away more than \$1,000,000 in your lifetime, but the current tax rate has been reduced from 45% to 35%.
- Your heirs may now have to use the original price paid for an asset when computing the tax liability instead of the value at the time of the owner’s death. This drastic change of “cost basis” could become very expensive and difficult for your heirs to manage. For example, if you inherit shares of a security that your parent accumulated many years ago, you now need to find the original price purchased, adjusted if at all, for reinvested dividends (the taxes you already paid). When you sell these shares, you may owe a capital gains tax on the appreciation of these securities. Currently, each estate can exempt \$1.3 million in gains from this “carry-over basis rule” while another \$3,000,000 exemption applies to assets inherited from a spouse.

These are just some of the confusing facts that financial professionals and estate planners have to work with in this year of change. As for the future, as we said earlier, “The only thing that is constant is change.” Congress has recently looked at several proposals that restore estate taxes (some of them even retroactively to the beginning of this year). In fact, one proposal that has continuously been bantered about is restoring the \$3,500,000 exemption for estate tax and generation skipping transfer taxes and leaving a 45% tax rate for the remainder. Unfortunately, this does not make the job of estate planning easier.



Year	Lifetime Gift Tax Exemption	Total Gift and Estate Tax Exemption*	Generation Skipping Tax (GST) Exemption	Gift, Estate and GST Taxes/Top Rates**
2009	\$1 million	\$3.5 million	\$3.5 million	45%
2010	\$1 million	Unlimited	Unlimited	35%
2011	\$1 million	\$1 million	\$1 million	55%

* The estate tax exemption amount is reduced for lifetime taxable gifts.
** Does not include surcharges.
Source: www.irs.gov

The table above offers the current rates and exemptions that existed in 2009 and are in place today for 2010 and 2011. If you think the table is confusing, consider the fact that there has been discussion that if Congress passes any retroactive legislation, people with enough money at stake will bring potential lawsuits arguing that a retroactive tax is unconstitutional. Regardless of whether or not this happens, if Congress is to make a change for this year, the sooner they act, the fewer number of people will bring potential lawsuits and the quicker the government can start collecting taxes on large estates again. Congress must act quickly in order to reduce the number of potential lawsuits and continue collecting taxes on large estates.

So what can you do to prepare in these confusing and changing times?

Here are some steps to consider:

How organized are your records?



Everyone involved will benefit if you organize all of your records now to show the assets and the cost basis of those assets on anything that your heirs will inherit. In fact, if you are helping a sick parent or family member, it is probably worth your time to see if they kept records in order to avoid possible bookkeeping nightmares should you be affected by the carry-over basis rule.

Review your Will and Living Trust.

If you have these documents, please make sure they include language that protects you against the change in estate tax exemption amounts. Instead of naming a specific sum that will fund a trust, many investors refer to a percentage. Phrases such as “that amount,” or “that fraction,” or “that portion” are many times standard practice. Although this year there is no estate tax, your documents will reflect your current intent.

Consider a Bypass Trust.

A Bypass Trust often includes a formula clause that allocates the maximum tax-free amount to the trust if you die before your spouse. This trust can then distribute your assets as you specify in the trust document. For example, it can leave money to your spouse and family members while your spouse is still alive and eventually pay what is left to the family members upon the death of your spouse. By using a trust rather than leaving your funds to your spouse outright you can be sure that neither the assets nor their appreciation will be considered a part of your spouse’s estate and therefore will not be subject to tax when he or she dies. Although there is currently no estate tax if you die, depending on how your formula clause is worded, it is possible that all of your assets can go into a Bypass Trust. Please proceed with caution because this strategy could lead to some potentially painful scenarios. For example, if the trust is not set up to

make payments for your spouse, your spouse may get nothing. Another possibility is that if your trust is not set up to benefit your spouse, all of your money could be locked up into the trust and your spouse may wind up in a very awkward situation. Once again, it is time to review your Bypass Trust (sometimes called a "Family Trust"). See if there is a formula or clause that was specifically put in place to satisfy the inheritance tax that now potentially becomes a problem because of current tax laws. This is an area you should definitely review with a knowledgeable attorney.

Review all your beneficiary designation forms.

Some of your assets will not pass through a Will or Living Trust. For example, if you have life insurance or retirement accounts you need to make sure that your beneficiary designation forms are current with the beneficiary designations that you want. Remember, a beneficiary form will always override any trust or will directive.

Confirm that you have a current and updated Durable Power of Attorney.

Many investors do not have this essential document. Even if you have one, it is imperative that you make sure it is current and includes language that applies to today's rules.

It is time to give your estate plan a check-up.

As of right now, the estate tax repeal covers many issues or concerns people have about the payment of estate taxes. In 2009, primarily those with over \$3,500,000 were concerned about estate taxes. Please keep in mind that regardless of your net worth you still should have an estate plan.



Estate planning goes far beyond taxes and is essential to all investors. Whether estate taxes are a concern for you in 2011 or not, it is always helpful to give your estate plan a check-up.

For example, you should:

Review what state taxes, if any, exist.

Although the federal tax is currently in a state of flux and doesn't exist for 2010, the state in which you officially reside can have estate taxes which may affect you. Please keep in mind that most states honor a Will that was signed within that state. You should check with a local lawyer to make sure the state you live in honors your Will if you have moved states recently.

Use trusts as needed.

Trusts still continue to be an important part of estate planning and can sometimes protect against financially irresponsible family members, former spouses and creditors. They are still a helpful piece of estate planning but may need to be reviewed and updated.

Think about not just 2010, but the future as well.

This is a good time to revisit your current arrangements and make sure you understand the tax consequences that will go into effect next year on funds going to your spouse and your grandchildren. You may have to amend your current trust either now or shortly after any new laws are passed.

Last but not least, take care of yourself and make sure that what you have spent your lifetime accumulating moves in the direction that you'd like!

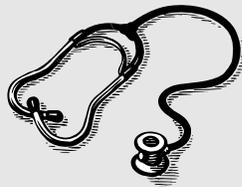
In conclusion, estate planning is a way to take care of yourself, the people you love and the funds you spent a lifetime accumulating. Whatever happens in Congress should not postpone seeking out the advice of a qualified financial professional and attorney to make sure that your estate is properly planned on your specific terms. **As a financial planner, we help and direct clients with their estate plans. If you have any questions about yours, please give us a call.**

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