

Looking toward the future



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Jerald Kaiser, a director at financial advisory firm GHP Horwath, said it's not possible to just do away with estate taxes.

Changing political landscape may shift estate planning

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Think the presidential election will change the tax rules when it comes to estates? Maybe, but not yet, experts say.

"It is widely assumed that regardless of the election, we're likely to see some increase in taxes," said Bob Phelps, a Denver-based wealth adviser for JP Morgan's Private Bank. "We don't know for sure, obviously. There is a fairly broad consensus that there needs to be clarity."

There's uncertainty about what will happen to the estate tax in 2010, when it will vanish for a year, only to be reinstated in 2011 at a top rate of 55 percent. Since 2003, the top tax rate on estates has been lowered one percentage point a year from 49 percent.

The advice of tax experts: Don't bet that the estate tax will vanish in 2010.

"I think that, in general terms, there is no way to have no estate tax and then revert back," said Jerald Kaiser, a director at financial advisory firm GHP Horwath. "I don't think anybody thinks that. If you're planning on dying and were going to do so in 2010, just know that provision will be addressed."

"The consensus is that it's not going to happen."

Tax experts seem to agree that the current tax law isn't useful and that there's a much better middle ground.

But given the changing political landscape, it isn't clear what will happen to the current tax rate once the provision is addressed.

The presidential candidates offer different approaches to the estate tax.

Calling the current estate tax rules the "Paris Hilton Tax Break"—in reference to Hilton Hotels heir Paris Hilton — Sen.

Barack Obama, D-Ill., has said he would repeal the estate tax cut. Obama has proposed a \$3.5 million exclusion in 2009. Thereafter, the rate would top out at 45 percent.

Sen. John McCain, R-Ariz., voted to permanently cut the estate tax equal to the current long-term capital gain rate, which is 15 percent. Additionally, McCain has proposed raising the exclusion to \$5 million per person.

Both candidates support the current method for valuing mutual funds, stocks and other inherited property that have appreciated for several years.

Under the current method, the cost basis for an heir who receives inherited property is the value on the date of the death of the testator. This system is called the "step-up" basis because the value of the property gets "stepped up" to fair market value.

Either way, financial planners and their

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wealthy clients are looking for something simpler in the debate — clarity.

“The consensus is that we will have a more certain estate tax regime in '09 than in '08, Phelps said. “I think they are going to eliminate this patchwork of estate tax rules.”

In the meantime, estate and tax planners should move forward assuming that current tax rules will be in place.

“If people get concerned with this, we still have a month and a half after the election to do something,” Phelps said. “The uncertainty has made people reluctant to plan. For people who have been sitting on big appreciations of wealth, there is still time to do something this year.”

And if by some chance the estate tax is repealed in 2010, “then no harm, no foul,” Kaiser said.

Those planning techniques include a wide range of investment strategies.

One such strategy is to make a gift. While a gift giver is taxed for any amount over the first \$12,000 to a single recipient, the gift amount exceeding \$12,000 won't be subject to the gift tax unless this taxpayer has already given more than \$1 million in taxable gifts since 1976.

The gift tax ranges from 38 percent to 44 percent.

“We've been talking to people about making a taxable gift,” Phelps said. “In the gift-tax scenario, the effective tax is lower.”

Another approach is to pay someone else's tuition or medical expenses. The payments don't count toward the annual limit, but the payments must go directly to the medical or educational institution.

Estate planners also suggest that doing nothing might be an approach as well.

“Most of the Bush tax cuts end in 2010,”



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Jerald Kaiser, a director at financial advisory firm GHP Horwath, notes that most of the tax cuts initiated by President George W. Bush expire in 2010.

Kaiser said. “If nothing happens, the Bush tax cuts sunset and you have an automatic increase, the way the legislation was written.”

As far as ordinary income goes, financial planners say there are strategies that will allow people to accelerate income while there are lower tax rates.

“On the income tax side, we're planning for the possibility that there will be increases in the capital gains taxed,” Phelps said. “We are thinking about the strategies that people should pursue.”

Those strategies include investing in tax-exempt instruments and accelerating

payments from investments that have appreciated strongly, such as an IRA or general investment account.

Also, there could be other cash-rich distributions that would take place when there is some clarity in the tax picture. For instance, people that have closely held businesses with extraordinary cash should start to draw on that excess cash.

“We want to try to find assets, maybe some of which we can discount,” Phelps said. “It's a good time to be thinking about that.”

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