

NOVEMBER 2012 NEWSLETTER

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ESTATE PLANNING- THE SEASON OF TAX UNCERTAINTY: FEDERAL ESTATE TAXES FOR 2013 AND ONWARD

NEWS ALERT:

1. WEBSITE AND NEWSLETTERS

Pozzuolo Rodden, P.C. is pleased to announce that during the month of October 2012 our website was visited by more than 1,100 visitors and almost 7,900 pages of articles, newsletters, and attorney success stories were read. During October 2012, many of our past newsletters have been republished by many TV stations through the United States on their websites and by other national publications such as: KOTA ABC, Rapid City, South Dakota; KFVE 5-TV, Honolulu, Hawaii; Topix.com; hugohosting.com; pubmemo.com; uberi.com; and, estateplanningadministrationattorneys.com. All past Estate Planning and Corporate Law Newsletters are available at: http://www.pozzuolo.com/Pubs_Newsletters.shtml

2. QUESTION OF THE MONTH:

I have been living with my mother's home for 4 years and have been providing her day-to-day care and maintenance. Because she had a stroke and now is in need of more intensive care, I am admitting my mother to a nursing home. May my mother transfer her home to me and still be eligible for Medicaid? **Answer-See Page 4 of this Newsletter**

If there are any legal questions you would like this office to answer in the future, please email the question to us at info@pozzuolo.com. Each month, the question with the most relevance to our privately held business clients, advisors, and friends will be answered in our monthly newsletter. The questions can relate to any of the areas practiced by this office including business planning and transactions, corporate law, commercial litigation, employment law and litigation, commercial real estate and development, construction law and litigation, estate planning, estate administration, tax and pension law, family law litigation.

THE SEASON OF TAX UNCERTAINTY:

FEDERAL ESTATE TAXES FOR 2013 AND ONWARD

For Federal Estate Tax Planning, we are in an even more uncertain place than we were 2 years ago. Not only are we waiting and watching on what will be done with the Federal Gift and Estate Taxes (the "Transfer Taxes"), but now with the pending elections we are waiting on whose administration will be deciding these tax issues- another level of uncertainty. As of January 1, 2013, the Estate, Gift, and Generation Skipping Tax Exclusions would drop from the current \$5,120,000 to \$1,000,000, the spousal portability is lost, and the maximum marginal tax rate will increase from 35% to 60% (taking into account the 5% recuperation from \$10,000,000 to \$17,184,000) (See charts below). This would greatly increase the Federal Transfer Taxes payable by many estates, large and modest, that have not been taxed since prior to year 2001.

Please consider that most center city and suburban residents have estates in excess of \$1 million when you consider a home, a pension and a life insurance policy.

2013 Transfer Tax Rates			2012 Versus 2013		
Lifetime Transfers Exceed	To	Marginal Tax Rate		2012	2013
\$1,000,000	\$1,250,000	41%	Estate/GST Tax	Yes	Yes
\$1,250,000	\$1,500,000	43%	Estate/GST Exemption	\$5.12 M	\$1 M
\$1,500,000	\$2,000,000	45%	Gift Tax Exemption	\$5 M	\$1 M
\$2,000,000	\$2,500,000	49%	Exemption Spousal Portability	Yes	No
\$2,500,000	\$3,000,000	50%	Maximum Marginal Tax Rate	35%	60%
\$3,000,000	\$10,000,000	55%			
\$10,000,000	\$17,184,000	60%			
\$17,184,000+		55%			

2012 and 2013:

The 2012 TRUIRJCA rules postponed the sunset of the favorable EGTRRA rules. EGTRRA provided an Estate Exclusion of \$5,120,000, a Gift Tax Exclusion that matches the Estate Exclusion, a marital portability of the exclusions, and a maximum estate tax rate of 35%. This is scheduled to drastically change on January 1, 2013.

By way of background, first, the Estate and Gift Tax Exemptions at \$5,120,000 allow for a tax free wealth transfer opportunity for most estates. Second, there is presently a portability of the exemptions between spouses. A surviving spouse is permitted to use any unused exemption of a predeceased spouse if the predeceasing spouse's executor makes the proper election on the deceased spouse's federal estate tax return. This is important if one spouse owns the majority of the assets and the less wealthy spouse dies first; otherwise, the exemption is lost. Under portability, an asset owning surviving spouse may now use the unused exemption to receive a total exemption of \$10,240,000. Finally, while the pre-EGTRRA maximum tax rate was 60% (55% plus the 5% recuperation from \$10,000,000 to \$17, 184,000) the TRUIRJCA capped the federal tax rates at 35%. This provides substantial opportunities to gift or bequest assets out of an estate tax free or at tax preferred rates.

In 2013, this is to sunset. The exemption will drop back to \$1,000,000, there is no spousal portability, and a potential maximum marginal tax rate is 55% to 60%. The lower exemption rate would mean a potential additional \$8,000,000 of assets per married couple being taxed at a higher rate. That in itself could cause an increase tax bill as much as \$4,400,000 (55% * \$8,000,000) not including the effect of a higher tax rate on amounts above \$10,000,000. Further, no spousal portability means if a married couple owns \$2,000,000 of assets, but the wife is the sole owner of the assets, if she was the second to die, she could not use her husband's \$1,000,000 exemption amount. This would result in an extra \$43,000 of federal estate taxes not taking into account the effects of the lower exemption amount. Last, the higher marginal tax rate of 60% is almost double the marginal federal estate tax rate of year 2012.

Uncertainty in 2013:

There is much uncertainty and speculation as to what the final 2013 rules will be especially with the impending election. The two most likely options are: 1) allowing the rules to lapse into the 2013 default rules; 2) a continuation/modification of the 2012 rules; or, 3) an abolition of the Wealth Transfer Tax.

If Congress does not act by January 1, 2013, the above 2013 default rules will apply. This means the exemptions drop to \$1,000,000, the maximum marginal tax rate increases back to 60%, and the loss of the spousal portability. This would cause a tremendous increase in the Federal Wealth Transfer Taxes for almost all of our clients, especially the privately held business owners.

The second option is a modification of the current rules with a higher maximum tax rate, a lower exemption amount, and retention of the spousal portability. For instance, the most recent proposals have been a permanent \$3,500,000 exemption and a maximum rate of 45% with portability.

Another act proposes a \$1,000,000 exemption indexed for inflation from 2000, a maximum tax rate of 55%, and portability. Neither of these proposals is as favorable as the 2012 estate tax rules.

If President Obama is elected, he appears to favor a maximum tax rate of 45%, an exemption amount of \$3,500,000, and spousal portability. On the other hand, Governor Romney purports for an abolition of the Federal Wealth Transfer Taxes all together. A complete abolition appears unlikely unless Congress maintains a Republican majority.

However, one major issue, even if each candidate would like to amend the Federal Wealth Transfer Tax rules, is whether Congress will have the time to focus on amending the Wealth Transfer Taxes by January 1st. With the hot topics of the elections being the economy and unemployment figures, foreign affairs, and health care, Wealth Transfer Taxes may take a back seat especially with much of Congress and potentially the President serving his/their last two months in office. There is a possibility that the taxes are not amended causing a sunset back to \$1,000,000 exemption and the 55% marginal tax rate becomes permanent. Regardless of what the exact rule will be, it is apparent that the exemption amounts will likely decrease and the marginal tax rates will increase.

Conclusion:

There is much uncertainty about the future state of the Federal Wealth Transfer Tax system for 2013 and going forward.. While politicians seem eager to have an exemption amount higher than \$1,000,000 and a marginal tax rate lower than 55%, politics may lead to the pre-EGTRRA tax rules. Regardless of what the actual tax rules will be, it is apparent that the exemption amount will shrink and the highest marginal tax rates will increase. Therefore, the best way to prepare for this is to take advantage of the window of opportunity and use the favorable 2012 treatment during the last 2 months of year 2012, if possible, by using the \$5,120,000 exemption amounts by gifting before it is possibly lost forever.

Lastly, we strongly recommend writing, emailing, faxing or calling your U.S. Senators and Congressperson to express your opinion about this Federal Estate Tax uncertainty.

QUESTION OF THE MONTH:

I have been living with my mother's home for 4 years and have been providing her day-to-day care and maintenance. Because she had a stroke and now is in need of more intensive care, I am admitting my mother to a nursing home. May my mother transfer her home to me and still be eligible for Medicaid?

The answer is yes, if you meet the "Caregiver Child Exception." Generally, Medicaid will contribute to the long-term care of an individual if that person meets three eligibility tests based on (1) medical eligibility, (2) income eligibility, and (3) resource eligibility. Basically, to be eligible for Medicaid, you must be in a position of medical and financial need. An asset like a home may be counted in a person's resource eligibility, negatively affecting that person's eligibility based on financial need. A child's first instinct may be to simply transfer her mother's house to herself in order to remove that asset from her mother's estate. Doing so would make it

appear that her mother is in greater financial need of Medicaid. Unfortunately, the Medicaid officials are aware of this tactic and have imposed restrictions on Medicaid eligibility to prevent it.

Regarding transfers, the general rule is that a transfer of assets without compensation within five years of an application for Medicaid will cause a penalty period to be assessed. Within that penalty period, Medicaid will not be granted. Fortunately, for the daughter in the hypothetical above, there is an exception to the general rule, called the “Caregiver Child Exception.” The Caregiver Child Exception says that if the child has (1) resided in the parent’s home for at least two years prior to the parent’s entrance into a nursing facility, and (2) provided a level of care to the parent that allows the parent to stay at home and not have to enter into a nursing home, then the transfer of the home to that caregiver child does not create a penalty for Medicaid purposes.

In order to meet the exception, the daughter would have to show that she lived with her mother for two years leading up to her admittance to the nursing home and that she provided the required level of care. In a recent case in New Jersey, a son was able to prove, via his family members’ testimony, that he lived with his mother for the required time and helped her bathe, walk, and cook, among other things.¹ Assuming the daughter in the question above lived in her mother’s home for two years and provided the required level of care, then her mother may transfer her home to her without incurring the Medicaid penalty. The daughter would be well advised to seek a doctor’s letter which outlines her mother’s health issues justifying the need for her care by her daughter and that because of the daughter’s care, the mother was able to stay at home rather than having to live at a nursing facility. It will also help if the daughter can secure statements from other family members attesting to the same thing.

¹ V.P. v. Dept. of Human Services, (N.J. Sup. Ct., App. Div., No. A-2362-09TI, Sept. 2, 2011)

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Publications

All of the following professional publications and past newsletters written by attorneys of this office are available by clicking here: [http://pozzuolo.com/Pubs Articles.shtml](http://pozzuolo.com/Pubs%20Articles.shtml)

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Money Purchase Pension Plan Falls Out Of Favor

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Adapt Estate Planning Strategies to Fit the Needs of Same-Sex Couples

Actual resolution of legal issues depends upon many factors, including variations of facts and state laws. This newsletter is not intended to provide legal advice on specific subjects. It is to provide insight into legal developments and issues. You should always consult with legal counsel before taking any action on matters covered in our updates.

This newsletter is courtesy of Pozzuolo Rodden, P.C.

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