

Tax Planning for 2010 Down to the Wire

As a changing power base in Washington wrangles over tax policy in the waning days of Congress' lame duck session, millions of families and investors are reluctantly awaiting the return of the estate tax and presumably much more stringent rules on gifting.

Already it's been a strange year for taxes. At this writing, the estate tax remained repealed in 2010, meaning that individuals dying during 2010 will be free to pass down their estates to heirs without any estate tax at all. However, as of Jan. 1, 2011, that picture will change drastically without any form of Congressional action – the estate tax will roar back with a vengeance with a low \$1 million exemption per individual, down from \$3.5 million in 2009, and a 55 percent top rate, up from 45 percent.

Also, the generation-skipping transfer (GST) tax – which also was repealed in 2010 – is also expected to return in 2011. It will carry a similar \$1 million exemption in 2011, down from \$3.5 million in 2009. While not as well known as the estate tax, the GST was written to prevent wealthy families from gifting assets to grandchildren as a strategy to cut their tax liability. In short, without any significant changes in tax policy, starting in 2011, individuals might see such gifts become subject to double taxation – the GST or either the estate or gift tax.

While there may be solutions even at this late date, the best choice is to seek out trained advice from both qualified tax, legal and financial planners, preferably in tandem. For wealthy taxpayers with a few years to go until retirement – or even until grandchildren arrive – it's also not a bad time to be thinking about your individual estate plans and how you'll manage assets as you get older.

In the meantime, consider the following strategies on gifting:

Start with the basics: Grandparents – and parents, for that matter – can avoid the gift tax by giving up to \$13,000 per recipient per year to each child or grandchild. Above that amount, remember that the gift tax stands at 35 percent in 2010 but is scheduled to rise to 55 percent in 2011.

You can go farther: You can gift an additional \$1 million all at once or over an extended period on top of each \$13,000 gift by borrowing from the amount you'll be able to shelter from the estate tax.

Opt to pay medical or tuition bills: If you pay a family member's school or hospital directly, you may give an unlimited amount. It's also important to know that you can do that on behalf of anyone, not just family members.

Don't forget charity: Charitable giving is not something that's done only in someone's will. You can donate assets to a charitable gift fund or community foundation where your investment grows tax-free and you can designate charities you plan to give to before and after you die.

And keep in mind some general last-minute tax planning advice:

Max out your retirement contributions: For 401(k)s, you have until Dec. 31 to make your 2010 contributions. The limit per employee is \$16,500 with an extra \$5,500 allowed to taxpayers 50 and older. IRAs have later deadlines.

Empty your flexible savings accounts: Flex accounts must be emptied out by yearend (or by the end of your company's standard grace period) or the money must be forfeited. Double-check the many items that qualify, because that list will get smaller last year – no over-the-counter medicines can qualify for Flex spending without a prescription.

Take advantage of energy credits: The Residential Energy Property Credit expires Dec. 31. Taxpayers spending for qualified improvements ranging from roofs to insulation and water heaters can qualify for a credit up to \$1,500.

December 2010 — This column is produced by the Financial Planning Association, the membership organization for the financial planning community, and is provided by Marnie Aznar, MBA, CFP®, a local member of FPA.