

IRS issues notice on 2010 estates

By: [Correy Stephenson](#)

Staff writer

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After months of speculation and anticipation on the part of estate planning attorneys and tax practitioners, the Internal Revenue Service has issued a Notice and Revenue Procedure for 2010 estates seeking to exempt out of the estate tax.

[Notice 2011-66](#) offers guidance and examples on how to handle an estate tax exemption and [Revenue Procedure 2011-41](#) explains the applicable tax rules when opting out.

Both the estate tax and the generation-skipping tax (GST) were repealed on Jan. 1, 2010 but were retroactively reinstated on Dec. 17, 2010 when [President Barack Obama signed](#) the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.

Under the law, the estate tax exemption was set at \$5 million (or \$10 million per couple), with a maximum estate tax rate of 35 percent.

Pursuant to the notice, executors of 2010 estates may opt out of the estate tax by filing Form 8939, Allocation of Increase in Basis for Property Acquired from a Decedent.

If they choose to do so, the estate will be subject to carryover basis rules, explained Robert Keebler, a CPA with Keebler & Associates in Green Bay, Wis.

If they elect instead to pay estate tax, they will receive a complete step-up in basis.

"The choice is largely about balancing the income tax against the estate tax," he said. "And the wrong choice can be devastating."

But get ready to work fast.

Form 8939 was expected mid-September, with a strict deadline for filing of Nov. 15, 2011 – and no extensions are allowed.

That essentially gives practitioners a two-month window in which to make the election and file forms, Keebler explained. "We are going to have a fairly interesting October and early November," he said.

The time period is "certainly putting a lot of people on edge," agreed Bernard A. Krooks, an estate planning attorney at Littman Krooks in New York City.

Run the numbers

Some estates may actually benefit from paying the estate tax, Krooks said.

"You really have to run the numbers to see where the client will be better off," he said.

As a general rule, Keebler said that estates valued at less than \$5 million (or \$10 million for married couples) are likely to elect to pay the estate tax, while estates greater than \$30 million will most likely elect out of the tax to avoid a greater tax penalty. Gross estates between \$5 and \$30 million (\$10 and \$30 million for married couples) are most in need of analysis, he said.

While the Notice and Revenue Procedure are extremely detailed and complex – and offer many valuable examples, Keebler noted – the following are some issues for practitioners to be aware of when considering an election out of the federal estate tax:

- **Basis increase.**

The Revenue Procedure explains how to allocate basis increases and the types of property that are not eligible for such an increase, Keebler said, including property the decedent held with a general power of appointment and QTIP trusts. The basis increase is \$1.3 million for individuals other than the decedent's spouse and \$3 million for property that passes to a spouse.

- **Conditional or protective elections.**

In some valuation situations, a taxpayer may choose to file a conditional or protective election where the asset is difficult to value – an interest in a family business or a tenancy in common property interest, for example. But the IRS said that it will not allow conditional or protective elections for the estate tax election.

Michael J. Jones, a CPA and estate planner at Thompson Jones in Monterey, Calif., noted that courts have permitted protective elections where the IRS has not and practitioners could consider “putting in a protective election even though the Service might not recognize it.” That way, the election could help in a later decision to litigate, he suggested.

- **GST issues.**

The IRS “is attempting to do a really nice thing” by not requiring taxpayers to file a GST return in order to elect out of automatic allocation of GST transfer tax on future trust distributions in inter-vivos direct skip transfers, said Jones, the author of the *Guide to Electing Out of the 2010 Estate Tax (And Into Modified Carryover Basis)*.

“This is a really, really great thing for taxpayers, because it will eliminate filings only to get rid of the unwanted automatic allocation of GST transfers,” he said.

The election is available for direct skip gifts – those made from a grandparent to a grandchild, for example – made between Jan. 1, 2010 and Dec. 17, 2010.

- **Executors.**

The IRS is requiring that executors file Form 8939. But it appears the agency “is expecting some turf battles between heirs and co-executors on whether to elect out of the estate tax,” Keebler said.

If the parties cannot agree or more than one executor files a form, then the Notice provides that the IRS will instruct the parties to re-file within 90 days “and get their act together,” Keebler said. “The IRS is trying to set this up so that there is a resolution procedure within the Notice.”

If the parties cannot get on the same page, then the IRS will decide whether to elect in or out of the estate tax for the decedent.

- **Limited amendments.**

While the Notice provides that no extensions will be allowed for filing Form 8939, Jones noted that if the form is filed early, the IRS will allow amendments for limited purposes.

Timely filings can be amended using Form 90100 until May 15, 2012. And an amendment is also allowed in situations where a filer needs to make a spousal basis increase, Keebler said, which the IRS will allow within 90 days of the date of distribution of qualified spousal property.

'Heightened' malpractice concerns

The IRS has described the Revenue Procedure as a safe harbor, Jones said, which gives lawyers good reason to follow its mandates.

But given the short time period and the unknown forms, attorneys should "tread carefully," Krooks cautioned. "We are dealing with something new, with no history, no course of professional conduct and no authority other than this one announcement."

To avoid malpractice concerns, Krooks encouraged attorneys to explain everything to clients in writing.

Keebler agreed.

"There is always malpractice exposure every time you file a tax return, but it is heightened on a filing people are going to have to do just once," he said.

Questions or comments can be directed to the writer at: correy.stephenson@lawyersusaonline.com