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A HAPPY  
NEW YEAR

# Client Update

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### **The Tax Law and Your Estate**

The 2001 Economic Growth and Tax Relief Reconciliation Act, was very complicated, and it unfortunately did not eliminate the need for estate planning. In fact, it made tax and estate planning more important.

The old law had a combined Gift and Estate Unified Credit and Tax Rate. It permitted each person to gift or bequeath a certain amount of money (the "exemption") without paying Gift or Estate Taxes. In general, this exemption was increasing yearly to \$1 Million in 2006. The top Estate Tax rate was 55%.

*The 2001 Act* – In general, increased the exemption; reduced the top tax rate; and separated the gift tax exemption and the estate tax exemption.

The main changes were as follows:

*Exemption for Estates* – This law increases the exemption from \$675,000 in 2001 to \$3,500,000 in 2009; eliminates Federal Estate Taxes in 2010; and then establishes the exemption at \$1,000,000 in 2011 and beyond, unless Congress provides otherwise. Note that whenever Federal Estate Taxes could apply (every year except 2010) the heirs/beneficiaries receive the assets at a stepped up basis (generally the Fair Market Value of the asset at the date of descendant's death) whether or not taxes are actually paid.

*Exemption for Gifts* – this remains at \$1,000,000 for 2002 and beyond and applies in 2010, too. Note that the donee acquires the donor's basis in the gifted asset; there is no stepped up basis. Note further that the yearly \$12,000 annual exclusion for gifts applies and does not reduce the allowable \$1 Million exemption.

*Estate Tax Rates* – The top Estate Tax Rate reduces over time from 55% in 2001 to 45% in 2009; in 2010 the tax is eliminated; and in 2011 and beyond the top tax rate is 55%, maximum, unless congress provides otherwise. Although this new law appears to give

tax relief, it is not as simple as that. The interrelation of Estate Taxes/Gift Taxes/ Basis rules have become more complicated and must be considered when planning your estate. For example, in 2010 there is no Federal Estate Tax; however, there is no step up in basis either. The heirs/beneficiaries will have to pay capital gains taxes when they sell the asset using the decedent's basis. There may be no actual Federal Estate tax Savings; but there will be potential capital gains taxes. Overall, the heirs may pay more taxes.

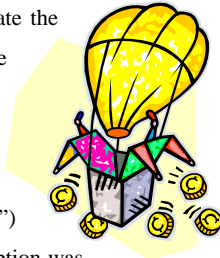
*What Should You do Now?* – Since it is uncertain when a person will die and the extent of his/her assets, it is important to continue to:

- Review your estate plan and prepare or revise your Wills, Living Wills and Power of Attorney. This is for family planning and potential capital gains.
- Include in husband and wife Wills, By-Pass Trusts to take advantage of both spouses' exemption amounts.
- Confirm that your assets are titled so that you affect your estate plan.
- When appropriate, establish and stick to a gifting program and make "annual exclusion gifts" to as many persons as makes sense.
- Take advantage of other Estate Planning Tools which can provide great tax savings opportunities and have virtually no effect on the person. For example, Life Insurance Trusts', Family LLC's; GRATS, Personal Residence Trusts, etc., are important tools.
- Keep accurate records to establish cost basis of assets. This will be especially important for beneficiaries of those persons who die in 2010.

<http://www.wellslaw.com/taxlaw.html>

### **What's New This Year?**

Like the weather, our tax laws are subject to frequent changes. Unfortunately, there continue to be many traps for the unwary and



uninformed tax payer. Here are some changes in effect for the 2007 tax filing season...and some others to consider for 2008.

A handful of tax benefits expired in 2007. Among them are the telephone excise tax refund, qualified electric vehicle credit, and a number of Hurricane Katrina-related tax provisions, including the special personal exemption for housing Katrina victims, special mileage reimbursements for Katrina-related charity work, tax-favored treatment of qualified hurricane distributions and loans from retirement plans, special limits for education tax credits, and exclusion from income of discharge of non-business debt. These provisions no longer apply.

Another credit, the residential property energy credit, is only available through 2007. This allows you to take a tax credit for 10% of the costs of having qualified energy saving items installed in your primary residence. The maximum credit is \$500, but only \$200 can be used on energy saving windows. In addition, there is another credit available for installing special solar or fuel-cell equipment. Also, just for 2007, the alternative minimum tax has special exemption rates that shield some additional 20 million tax payers from falling victim to this special taxing scheme. This issue is revisited annually by Congress.

All the usual tax bracket, exemption and deduction amounts have been adjusted for inflation, allowing you to shield more money from taxation, lowering your bill:

- Personal exemption - \$3,400 for 2007, \$3,500 for 2008.
- Standard deductions – singles and married filing separately, \$5,350 in 2007 and \$5,450 in 2008; heads of households, \$7,850 in 2007 and \$8,000 in 2008; married filing jointly, \$10,700 in 2007 and \$10,900 in 2008.
  - Standard mileage rate – business use, 48.5 cents per mile in 2007 and 50.5 cents in 2008; charitable use, 14 cents per mile in 2007 and 2008; deductible medical or moving travel, 20 cents per mile in 2007 and 19 cents in 2008.
  - Equipment expensing election – business expensing limit of \$125,000 in 2007 and \$128,000 in 2008.
  - IRA deductions - \$4,000 in 2007 and \$5,000 in 2008; additional catch-up contributions of \$1,000 for those ages 50 or over.

The amounts you can set-aside in a qualified retirement plan will remain constant for 2007 and 2008. The maximum salary deferral to a 401(k), 403(k), 457 or simplified employee pension plan is \$15,500, with additional catch-up contributions of up to \$5,000 for

those age 50 or older. Deferrals to a SIMPLE plan are limited to \$10,500 with a catch-up of 2,500.



<http://www.completetax.com/TaxTips.asp>

## A Look Ahead to Changes in 2008

Just before adjournment, Congress has handed out some Christmas presents for taxpayers affected by the alternative minimum tax (AMT) and forgiveness on their mortgage debt. Congress left a number of tax issues, including extension of expiring provisions, for another day.

Congress ended up doing the minimum that was expected, but what they did will spare many taxpayers some grief.

The AMT can apply to almost anyone, but tends to affect mainly middle-class tax payers with substantial itemized deductions, such as those who live in high-tax states. Like the standard deduction for regular taxes, there is an “exemption” based on filing status used in calculating possible AMT liability. But unlike the standard deduction, exemption amounts for the AMT were never indexed for inflation and each year threatens to revert to levels that will ensnare millions of additional taxpayers in the alternative tax system. The Tax Increase Prevention Act of 2007 offers relief in the form of a one-year “patch” that will help taxpayers in 2007 but leaves the future of the AMT in doubt.

The law sets 2007 AMT exemption amounts at \$44,350 for single taxpayers, \$66,250 for married couples filing jointly and \$33,125 for married filing separately. These amounts are \$2,000 higher than 2006 for single filers and married taxpayers filing separately; \$4,000 higher for joint filers. More important, they are about \$11,000 higher for single and married filing separately and about \$22,000 higher for joint filers than the 2007 exemptions they would have had to use if no “patch” had been enacted.

The new law also extends for the 2007 tax year the ability of tax payers to use most nonrefundable personal credits to offset their AMT liability. These include the dependent care credit, credit for interest on certain home mortgages, credit for the elderly and disabled, the Hope credit for certain college expenses, the Lifetime Learning credit and the credit for certain non-business energy property.

Altogether, the “patches” for 2007 will keep about 20 million taxpayers out of the clutches of the AMT. But only for 2007. What happens in 2008 is anyone’s guess.

<http://www.completetax.com/taxguide/news/07-003lookahead.asp>

