

THE REVISED NEW YORK STATE ESTATE TAX
(A Textbook Example of the Devil Truly Being in the Details).

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On March 31, 2014, Governor Andrew Cuomo signed legislation that dramatically revised New York State's Estate Tax regime. On its face, the new law appears to offer significant tax relief to Estates having a net worth ranging between \$2,062,500.00 and \$5,250,000.00. However, a detailed examination of the provisions in the new law make clear that without proper planning, an Estate valued between \$2,062,500 and \$5,250,000.00 can incur a large New York Estate Tax liability.

The "basic exclusion amount" is the key concept in the new law. As of April 1, 2014, the basic exclusion amount increased from \$1,000,000.00 to \$2,062,500.00. Subsequent increases to the basic exclusion amount are scheduled to go into effect at various intervals over the next several years. The basic exclusion amounts between now and December 31, 2018 are as follows:

- For Decedent's dying on or after 4/1/2014 and before 3/31/2015: \$2,062,500.00
- For Decedent's dying on or after 4/1/2015 and before 3/31/2016: \$3,125,000.00
- For Decedent's dying on or after 4/1/2016 and before 3/31/2017: \$4,187,500.00
- For Decedent's dying on or after 4/1/2017 and before 01/01/2019: \$5,250,000.00

For Decedent's dying on or after January 1, 2019, the basic exclusion amount will be subject to a cost of living adjustment. It is believed that by 2019, New York State's basic exclusion amount will equal the Federal Estate Tax exemption amount, thus ending the disparity between the Federal and State Estate and Gift taxes.

The benefits associated with the new law are considerable for anyone who dies with an estate valued at equal to or less than the basic exclusion amount. Given the increase in the exclusion amount, a considerable number of New York State residents will not be subject to Federal or New York State Estate Tax. However, the benefit of the new exclusion amount is phased out in a draconian manner for estates valued slightly above the basic exclusion amount. Estates that are valued between 100% and 105% of the basic exclusion amount receive a credit toward their tax liability, but will owe a considerable amount of New York State Estate Tax. Estates which are valued at more than 105% of the basic exclusion amount "fall off the cliff" and are subject to New York State Estate Tax from dollar one - thus losing the benefit of the exclusion amount entirely.

A few substantive examples will help illustrate the sweeping differences in New York State Estate Tax liability that occurs with just a small increase in the value of an estate:

Example 1: A dies on June 1, 2014. The value of A's estate is \$2,062,500.00. Because A's estate is equal to the value of the basic exclusion amount for Decedents dying between 4/1/2014 and 3/31/2015, the New York State Estate Tax Liability is \$0.00.

Example 2: A dies on June 1, 2014. The value of A's estate is \$2,124,275.00 - 103% of the value of the basic exclusion amount. Because the value of A's estate is between

100% and 105% of the basic exclusion amount, A's estate will receive a credit of \$31,550.00 toward the amount of New York State Estate Tax owed. However, this three percent increase in the value of A's estate leads to a New York State estate tax liability of \$77,200.00!

Example 3: A dies on June 1, 2014. The value of A's taxable estate is \$2,186,250.00 – 106% of the value of the basic exclusion amount. Because the value of A's estate is over 105% of the basic exclusion amount, the exclusion is completely phased out and the Estate is liable for New York Estate Tax from dollar one. According to the new statute, the New York State Estate Tax Liability on A's estate is \$113,700.00!!

The difference in the value of A's estate between examples 1 and 3 totals \$123,750.00 – but yields a difference in New York Estate Tax totaling \$113,700.00!! Future fiscal years will show an even greater disparity in New York State Estate Tax liability between estates of similar value.

Some other Highlights (and Lowlights) of the New York's State's New Transfer Tax Legislation:

The following is by no means an exhaustive summary of the provisions in the new law, but details some of the more prevalent provisions (and omissions) in the new law.

- The new law eliminates New York State's Generation Skipping Transfer (GST) Tax. The GST is an additional tax assessed against transfers made to people who are more than one generation removed from the Decedent (i.e. transfers from a grandparent to a grandchild). The elimination of an additional layer of taxation is definitely a highlight – however, please note the Federal GST still exists.
- The new law provides some relief for non-citizen spouses. New York resident spouses, who are not U.S. citizens, may inherit all property in an estate outright if a Federal Estate Tax Return is not required to be filed. Prior to this change, non-citizen spouses had to receive their inheritance through a special type of marital trust (Qualified Domestic Trust – QDOT) in order to qualify for the marital deduction. This is definitely a highlight of the new law as it allows a non-citizen spouse to inherit up to the Federal Estate Tax exemption amount outright and free of trust with no Federal or State Estate Tax liability.
- The new law provides that the value of all taxable gifts made by a Decedent in the three years prior to death will be included in the value of the Decedent's estate for purposes of calculating New York State Estate Tax. The three year look back period applies only to gifts made between 4/1/2014 and 12/31/2018. The following gifts are not included in the New York State Estate tax calculation:
 1. Gifts made while Decedent was not a resident of the State of New York;
 2. Gifts made by a resident Decedent before 4/1/2014;
 3. Gifts made by a resident Decedent on or after 1/1/2019;
 4. Gifts otherwise included in Decedent's estate under another provision of Federal Estate Tax Law (thus avoiding double taxation).

This provision is a definite lowlight as it seeks to artificially inflate the value of an estate solely for the purpose of calculating a higher New York State Estate Tax.

- The new law does not incorporate the concept of “portability” of the unused basic exemption amount. A recent revision to the Federal Estate and Gift Tax law allows a surviving spouse to use his or her predeceased spouse’s unused Federal Lifetime Exclusion Amount. If Husband dies and leaves everything to his Wife, Husband’s estate qualifies for the unlimited marital deduction and does not use the lifetime exclusion amount. Thus if Husband dies in 2014 and does not use his exemption of \$5,340,000.00, the surviving spouse can add that amount to her lifetime exemption amount. This allows Wife to pass a little less than \$11,000,000.00, to her children or other beneficiaries without incurring Federal Estate Tax. This superb tax planning device was not included in New York State’s revised Estate Tax law - a huge deficiency in (and lowlight of) the new law,

How do these changes impact you:

Estate, Tax and Financial Planning is an ongoing and continuous process. As events and circumstances in your life change, your documents need to be reviewed and, if necessary, revised. Sometimes change occurs personally, a new job, a death in the family, a change in financial circumstance. At other times, statutory changes require a review of your documents to ensure that they are drafted appropriately.

If your estate planning documents were prepared prior to January 1, 2013, and/or if your documents contain the mandatory establishment of “credit shelter” or “applicable exclusion amount” trusts, those documents will require review and potential revision in order to avoid unintended Federal and New York Estate Tax liabilities. Additionally, married couples who have an uneven division of assets should discuss with their financial advisors the benefits of dividing assets equally between each spouse. An equal split of their assets and careful drafting of their estate planning documents may lead to a potentially significant reduction in such married couple’s overall exposure to both Federal and New York State Estate Tax liability.