

Estate Planning Update

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NORTH CAROLINA ESTATE AND GIFT TAX CHANGES SIGNED INTO LAW

On July 16, 2008, the Governor signed into law House Bill 2436 ("Act"). The Act includes (i) full repeal of the NC gift tax, and (ii) a change in the calculation of the NC estate tax.

Repeal of NC Gift Tax

The Act repealed Chapter 105, Article 6 ("Gift Taxes") effective for gifts made on or after January 1, 2009. Generally speaking, under NC's pre-2009 gift tax regime, a NC gift tax return is required for any gift of North Carolina real or personal property the fair market value (FMV) of which exceeds the annual exclusion amount (\$12,000 in 2008). The specific lifetime exemption for Class A donees (e.g., recipients who are children, grandchildren, stepchildren, parents) is \$100,000. The difference between this amount and the federal gift tax exemption amount (\$1,000,000) has frustrated lifetime gift planning for many families.

The benefits of repeal include:

- the ability to consume the entire federal gift tax exemption amount (\$1,000,000) without triggering NC gift tax;
- the elimination of the requirement to file a NC gift tax return (NCDOR Form G-600); and
- facilitated use of vehicles such as Qualified Personal Residence Trusts (QPRTs) by eliminating payment of NC gift tax due on taxable gift value and application of less favorable NC statutory present value tables.

Keep in mind that repeal does not affect, for example, the NCDOR's right to challenge NC gift tax returns filed for gifts made in 2008 and earlier years.

Also, generally speaking, (i) future interest gifts (e.g., a remainder interest in a life estate in property), and (ii) present interest gifts that are greater than \$12,000 and do not qualify for the marital or charitable deduction, to any one individual in a calendar year still MUST be reported on the federal gift tax return (IRS Form 709). Examples of common gift tax traps include:

- Gift of cash or property valued over \$12,000 to any one person in a calendar year;
- Sale of property to a relative or other person for less than fair market value;
- Below market interest loans to relatives; and
- Below market rent or rent-free use of property.

Change in NC Estate Tax Calculation

Under the old law, if any property in a NC resident decedent's gross estate was located outside NC, the amount of tax due was reduced by the lesser of (1) the amount of death tax paid in the other state, OR (2) the NC death tax credit amount \times (out-of-state property value / gross estate value).

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Application of the old law resulted in higher NC estate taxes if, for example, the other state did not have a death tax (i.e., if no out-of-state death tax paid, then no reduction in tax paid to NC). The Act eliminates (1) and restates the reduction of tax as the amount set forth in (2).

The restated provision became effective on July 16, 2008, and *it will apply retroactively to decedents' estates for which the statute of limitations for claiming a refund had not expired as of December 28, 2007*. Generally speaking, the statute of limitations for claiming a refund for overpayment is the later of 3 years after the return due date or 2 years after payment of tax. A personal representative of an estate for which the applicable statute of limitations had not expired as of that date may claim a refund under N.C.G.S. § 105-241.7. Executors of NC decedents' estates with out-of-state property (and for which NC Estate Tax Returns were filed as far back as late 2004) may want to take the following action:

- Review NC Estate Tax Returns (NCDOR A-101) with preparers to determine if an overpayment was made using the formula under the old law; and if so
- Weigh the costs and benefits of filing an amended return claiming a refund of the overpayment.

Stay tuned for federal estate and gift tax legislation -- but don't hold your breath!

Disclaimer: This update is intended only for informational purposes and does not create any attorney-client relationship or constitute legal advice with respect to any specific problem, issue, or set of facts. Nor do these materials contain an exhaustive discussion of the topics presented. Readers are advised not to rely or act on the information herein without first seeking professional counsel.

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