

Proposed Changes to the New York Estate Tax

As part of his 2014-2015 budget, Governor Cuomo has proposed making significant changes to the New York State estate tax. This will describe the changes and point out some of the implications of those changes on estate planning, assuming the proposal is enacted in its current form. It is important to emphasize that the proposal is just that, a proposal. It is, of course, possible that the proposal will not be enacted or, if it is enacted, it will be amended. In short, stay tuned!

The proposal does not change the basic structure of the New York State estate tax. In a nutshell, the New York State estate tax continues to follow the federal estate tax to determine what is subject to tax, how assets are valued, and what deductions are available (with a possible exception that will be discussed below).

Proposed Changes

The first significant change is the increase in the amount exempt from New York tax. Over the course of four years, beginning April 1, 2014, the amount exempt from New York State estate tax increases on the following schedule: \$2,062,500 for decedents dying between April 1, 2014 to March 31, 2015; \$3,125,000 for decedents dying between April 1, 2015 to March 31, 2016; \$4,187,500 for decedents dying between April 1, 2016 to March 31, 2017; and \$5,250,000 for decedents dying between April 1, 2017 to December 31, 2019. See the chart at the end of the piece for the tax rates under the proposal.

After December 31, 2019, the New York exemption is to be indexed. Even as indexed, however, the New York exemption will be less than the federal exemption because it will not reflect the indexing in the federal exemption from 2013 on. Moreover, while the New York exemption is effectively a credit, there is an exception, which we will discuss below.

At the federal level, the exclusion against the federal estate tax not used at the death of a spouse may be inherited by the surviving spouse ("ported" is the technical word). In its current form, the proposal does not provide for portability of the New York exemption. If a decedent leaves all of his or her estate to a surviving spouse in a manner that qualifies for the marital deduction, the decedent's New York exemption will be lost.

The second significant change is that the New York State estate tax will take into account adjusted taxable gifts made by a donor after April 1, 2014 if he or she was a New York resident at the time of the gift.

The third significant change is a reduction in New York State estate tax rates. Eventually, that is, for decedents dying after March 31, 2017, the top rate will be 10% on estates in excess of \$3.6 million. The current top rate is 16%.

The fourth significant change is the introduction of a "New York-only" Qualified Terminable Interest Marital Deduction. Some explanation is in order.

The federal estate tax provides a deduction for certain transfers to a decedent's surviving spouse. The deduction is unlimited. Outright transfers qualify for the deduction; transfers to certain trusts that benefit the surviving spouse also qualify for the deduction.

One of the qualifying trusts is a "qualified terminable interest property trust" or "QTIP trust" for short. In order to qualify as a QTIP trust, the surviving spouse must be entitled to all of the income from the trust for his or her life and no other individual may have a beneficial interest in the trust while the spouse is alive. The QTIP deduction is elective.

PRACTICE LEADER
Martin W. O'Toole
motoole@hselaw.com

PARTNERS
David R. Ferris
dferris@hselaw.com

Anthony T. Lee
alee@hselaw.com

The New York provision, if enacted, would allow for a QTIP deduction for New York purposes where no federal estate tax return is filed. If a federal return is filed *and* the QTIP election is made, a New York QTIP election must also be made.

The provision effectively removes any question about the status of a QTIP election where the QTIP election was not needed at the federal level to avoid tax (there is a pronouncement from the Internal Revenue Service to the effect that such an election is void).

A fifth significant change is likely to prove controversial with respect to non-residents. In addition to taxing real property and tangible personal property that is located in New York for estate tax purposes, the provision would tax intangible personal property (e.g., a bank account) as though it were also located in New York if the property is used in a “trade, business or profession carried on” in New York.” Thus, an accountant in a partnership in New York who resided in Pennsylvania might have his or her partnership interest be subject to New York State estate tax.

The ability of a state to tax assets located in that state is unquestioned. Because intangible assets are deemed to reside where the decedent resides, the constitutionality of such an extension of New York’s taxing jurisdiction is likely to be tested. Moreover, it is not known if other states will be tempted to tax the intangible assets of New Yorkers who carry on a trade, business or profession in another state.

As part of the Report of the so-called “Green Island” Commission, there was discussion of a possible restoration of the New York gift tax. The budget proposal does *not* restore the New York gift tax.

Finally, with respect to changes, the proposal would eliminate New York’s generation-skipping transfer tax. As a practical matter, the tax had relatively little application in most estates.

Exceptions

As previously mentioned, some estates will not have the benefit of the increased New York exemption. Which estates? In a word, larger estates. The New York exemption is effectively a filing threshold *and* a credit. Where the taxable estate exceeds 105% of the exemption, however, “no credit shall be allowed to the estate.”

Even with the loss of the credit, the amount of New York tax is less than under current law. For example, assuming a taxable estate of \$10 million, under current law, the New York tax is \$1,067,600; under the proposal, the tax would be \$878,800, a reduction of nearly 18%.

Under the proposal, New York estate tax deductions track federal estate tax deductions with one likely exception. Although the proposed provision broadly states that the New York deductions are the federal deductions, the cross-reference to pertinent Internal Revenue Code provisions omits a cross-reference to the section providing for a federal deduction for estate tax payable to a state such as New York. In keeping with the current regime, in which the New York estate tax is *not* a deduction against the New York estate tax, it is likely that the non-deductibility of New York tax against the New York tax will continue.

Some Planning Implications

The eventual elimination of the New York State estate tax for estates under \$5 million (the figure does not reflect indexing) will be welcome for many estates.

Where the New York estate tax will apply, planning will not necessarily be simple under the proposal. First, without portability of the New York exemption, the question of whether to use the New York exemption at the first death of a married couple will still be present.

Second, for an individual near the federal exclusion, the combination of the “all or nothing” feature of the New York credit and the inclusion of adjusted taxable gifts in the New York gross estate may make planning to reduce an estate below the exemption difficult. Apart from the possibility of an estate having to pay tax, liquidity planning will be more difficult.

Third, the difference between the amount exempt from New York tax and the amount exempt from federal tax will complicate planning, particularly in drafting wills or living trusts.



Fourth, if post-April 1, 2014 gifts are subject to New York estate tax and the recipients are different from those who are beneficiaries under a decedent's testamentary documents, the estate beneficiaries effectively will be bearing tax on assets received by others.

On a near term basis, some will want to consider whether to make taxable gifts before April 1, 2014. Although there are many factors to be considered in making significant gifts, New York has provided a relatively limited time within which to do so.

One of the stated goals was to "address an incentive for wealthy New Yorkers to leave the State." It is uncertain whether the changes will cause any person who might otherwise move out of New York owing to the tax structure to reconsider his or her decision.

If you have any questions regarding this LEGALcurrents, please do not hesitate to contact any member of our firm's Trusts and Estates Practice Area at (585) 232-6500. □

	4/1/14 to 3/31/15	4/1/15 to 3/31/16	4/1/16 to 3/31/17	4/1/17 thereafter
to \$500,000	3.06%	3.06%	3.06%	3.06%
\$500,000 to \$1,000,000	\$15,300 plus 5% over \$500K	\$15,300 plus 5% over \$500K	\$15,300 plus 5% over \$500K	\$15,300 plus 5% over \$500K
\$1,000,000 to \$1,500,000	\$40,300 plus 5.5% over \$1M	\$40,300 plus 5.5% over \$1M	\$40,300 plus 5.5% over \$1M	\$40,300 plus 5.5% over \$1M
\$1,500,000 to \$2,100,000	\$67,800 plus 6.5% over \$1.5M	\$67,800 plus 6.5% over \$1.5M	\$67,800 plus 6.5% over \$1.5M	\$67,800 plus 6.5% over \$1.5M
\$2,100,000 to \$2,600,000	\$106,800 plus 8% over \$2.1M	\$106,800 plus 8% over \$2.1M	\$106,800 plus 8% over \$2.1M	\$106,800 plus 8% over \$2.1M
\$2,600,000 to \$3,100,000	\$146,800 plus 8.8% over \$2.6M	\$146,800 plus 8.8% over \$2.6M	\$146,800 plus 8.8% over \$2.6M	\$146,800 plus 8.8% over \$2.6M
\$3,100,000 to \$3,600,000	\$190,800 plus 9.6% over \$3.1M	\$190,800 plus 9.6% over \$3.1M	\$190,800 plus 9.6% over \$3.1M	\$190,800 plus 9.6% over \$3.1M
\$3,600,000 to \$4,100,000	\$238,800 plus 10.4% over \$3.6M	\$238,800 plus 10.4% over \$3.6M	\$238,800 plus 10.4% over \$3.6M	\$238,800 plus 10% over \$3.6M
\$4,100,000 to \$5,100,000	\$290,800 plus 11.2% over \$4.1M	\$290,800 plus 11.2% over \$4.1M	\$290,800 plus 11.2% over \$4.1M	
\$5,100,000 to \$6,100,000	\$402,800 plus 12% over \$5.1M	\$402,800 plus 12% over \$5.1M	\$402,800 plus 11.5% over \$5.1M	
\$6,100,000 to \$7,100,000	\$522,800 plus 12.8% over \$6.1M	\$522,800 plus 12.8% over \$6.1M		
\$7,100,000 to \$8,100,000	\$650,800 plus 13.6% over \$7.1M	\$650,800 plus 13% over \$7.1M		
\$8,100,000 to \$9,100,000	\$786,800 plus 14.4% over \$8.1M			
over \$9.1M	\$930,800 plus 14.5% over \$9.1M			



Harter Secret & Emery LLP

ATTORNEYS AND COUNSELORS

ROCHESTER

1600 Bausch & Lomb Place
Rochester, NY 14604-2711
585.232.6500

BUFFALO

Twelve Fountain Plaza, Suite 400
Buffalo, NY 14202-2293
716.853.1616

ALBANY

111 Washington Ave., Suite 303
Albany, NY 12210-2209
518.434.4377

CORNING

8 Denison Parkway East, Suite 403
Corning, NY 14830-2636
607.936.1042