CHANGE IN FEDERAL ESTATE TAX MAY INCREASE STATE DEATH TAXES

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SEPTEMBER 26, 2003

As a result of recent changes in Federal law not adopted by New York and many other states, some changes may be necessary in your will or other estate planning documents if your estate plan was designed to defer all estate tax at your death by providing for all of your assets other than an applicable exclusion amount to pass to (or in trust for) your spouse.

An applicable exclusion is available with respect to an aggregate amount of taxable transfers made by every individual during life or at death. Under Section 2010 of the Internal Revenue Code of 1986, as amended, in 2003 the applicable exclusion exempts from Federal gift and estate tax transfers totaling $1 million ($2 million per married couple). On January 1, 2004, the applicable exclusion will rise to $1.5 million ($3 million per married couple). However, current New York estate tax law specifically limits the applicable exclusion to $1 million. Thus, for most New York residents dying in 2004, it will result in a New York estate tax of $64,400. [1]

If you are married and you predecease your spouse, your estate planning documents may direct that an Applicable Exclusion or Family Trust be funded at your death with an amount equal to the Federal applicable exclusion you have remaining at death. The remainder of your

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[1] Under current Federal law, the applicable exclusion is increasing gradually to $3.5 million in 2009. As the applicable exclusion increases, so will the New York estate tax bill. The chart below shows the New York estate tax payable for a New York resident dying with a taxable estate equal to the Federal applicable exclusion amount in the years subsequent to 2004 assuming there is no change in the law.

Calendar Year	Federal Applicable Exclusion	New York Estate Tax
2005	$1,500,000	$ 64,400
2006	$2,000,000	$ 99,600
2007	$2,000,000	$ 99,600
2008	$2,000,000	$ 99,600
2009	$3,500,000	$229,200

assets may pass to your spouse, outright or in trust. The purpose of this structure is to utilize fully the applicable exclusion amount so that you can pass that amount to your children estate tax-free, and have the remainder of your assets qualify for the estate tax marital deduction, thereby deferring estate tax on those assets until your spouse's death.

Under this structure, if you die in 2003, the Applicable Exclusion or Family Trust will be funded with $1 million (assuming you have not made any taxable gifts during your life); no Federal or New York estate tax will be due at your death because the applicable exclusion amount for both Federal and New York estate tax purposes is $1 million. If you die in 2004, however, the Applicable Exclusion or Family Trust will be funded with $1.5 million; no Federal estate tax will be due at your death, but New York estate tax in the amount of $64,400 will be payable because for New York estate tax purposes the applicable exclusion will remain at $1 million. In subsequent years, the New York estate tax bill will grow as the applicable exclusion amount is scheduled to rise for purposes of Federal estate tax law.

If it were clear that the Federal estate tax would be imposed at the death of your spouse, it may make sense to pay the New York estate tax at your death to receive the benefit of the full Federal estate tax applicable exclusion amount. Given the possibility of Federal estate tax repeal, however, if you are a New York resident, you may prefer to amend your estate planning documents to limit the amount passing to your Applicable Exclusion or Family Trust, so that such amount will pass free of Federal estate tax as well as New York estate tax at your death. If you adopt this approach you may consider making lifetime gifts to make full use of the Federal applicable exclusion amount.

A similar issue may exist for non-New York residents, depending upon the state of residence.

If you have any questions or would like us to review your current estate plan, please call Mildred Kalik (212-455-2778), Pamela L. Rollins (212-455-3468), David J. Stoll (212-455-2766) or any other member of our Personal Planning Department.

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