



January 2010

Update on the Estate Tax Repeal Effective January 1, 2010

Despite some last minute attempts by the Senate, the estate tax has been repealed effective January 1, 2010. In the 2001 tax act known as EGTRRA, the estate tax exemption was increased and estate tax rates decreased over the span of 10 years, leading up to a full repeal of the estate tax in 2010. However, EGTRRA also included a “sunset” provision that causes the law to revert back to the pre-2001 rates and limits at the end of 2010. In other words, as the law stands now, the estate tax is repealed for 2010. The gift tax stays in place at a \$1,000,000 lifetime exemption and a 35 percent maximum marginal rate. Then, effective January 1, 2011, the estate and gift tax laws revert back to law as they were in effect before the passage of EGTRRA (see the chart below).

What will happen to the law?

There is quite a bit of speculation as to exactly what Congress will do with the estate tax. The House has already passed a bill that would permanently extend the law as it was in effect in 2009 (\$3,500,000 estate tax exemption, 45 percent maximum marginal tax rate). The Senate was unable to reach agreement on a bill before the current session adjourned for the holidays. So we technically start the 2010 year with no estate tax. There have been indications that as soon as Congress is back in session they will work on issuing a “letter of intent” alerting the public that they intend to extend or reinstitute some version of the estate tax retroactive to January 1, 2010. To add to the confusion, there are some legal analysts that question whether or not the retroactive imposition of an estate tax would be constitutional.

The Democrats have clearly indicated their intentions to reinstate the now repealed estate tax. Republican opposition, particularly in the Senate, is strong, which could spark a potentially lengthy debate. There has been no shortage of proposals ranging from making permanent the 2009 estate exemption and rates to increasing the exemption amount to as high as \$5,000,000 per person (indexed for inflation), with a maximum marginal rate of 35 percent and spousal rollover of the unused exemption of a deceased spouse. In addition, while it did not seem likely a few months back, it is possible that Congress will simply allow the law to revert back to 2001 law. This would allow Congress to agree to disagree by taking a “hands off” approach to the situation and allowing the pre-EGTRRA law to return and take effect in 2011.

What you need to do

There are several considerations in what, for now, is an estate tax free environment. However, the degree of urgency may vary depending on how your documents utilize formulas driven by either the estate tax exemption amount or the generation-skipping tax exemption amount to make distributions.

TAX ALERT

PROVIDED BY THE NATIONAL TAX OFFICE

Everyone should review their current estate plan to determine how the absence of a currently effective, federal estate tax will affect the operation of their plans. In many instances there may be little or no impact, but in some cases the impact will be dramatic. At the same time as existing plans are reviewed, consideration should be given as to whether this temporary repeal of the estate and GST taxes creates planning opportunities that should be pursued. Some common areas where modifications may be needed or where planning opportunities may exist include:

- The structure of asset distribution and allocation formulas in existing wills and trusts
- Gifting strategies that benefit from the reduced maximum gift tax rate and the absence of the GST tax
- Marital transfer formulas, particularly in cases involving second families
- Charitable transfer formulas that are based on the taxable value of an estate or trust
- The interaction of the repeal of the federal estate tax with state inheritance taxes
- The post-death use of disclaimers and spousal elections to redirect inherited assets
- The use of powers of attorney/appointment to increase flexibility for surviving spouses
- International estate planning implications, particularly non-U.S. citizen spouses or heirs
- Basis recordkeeping for tracking carryover basis of inherited assets

If Congress passes legislation with a retroactive effective date, these and other planning opportunities created by the temporary absence of a federal estate tax and GST tax and the reduction in the gift tax rate may not be available. Alternatively, if Congress does not act at all, this will be a one-year opportunity that will expire on December 31, 2010. Careful timely, planning, and coordination with legal counsel are essential to assure that proper safety valves are included in documents to protect against adverse results in the event of a retroactive reinstatement or change to the estate and GST tax laws.

We will continue to keep you informed as Congress makes decisions and takes action on this plan. Please feel free to contact Plante & Moran's tax team if you have questions:

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Year	Top Estate and Gift Tax Rate	Estate Tax Exemption	Gift Tax Exemption	Step Up or Carryover Basis
2009	45%	\$3,500,000	\$1,000,000	Step Up
2010	Estate tax and GST tax repealed; Gift tax rate 35%	N/A	\$1,000,000	Carryover
2011 and after	55% with a 5% additional tax for estates between \$10 and \$17.1 million	\$1,000,000	\$1,000,000	Step Up