



**February 2010**

## **Federal Estate and Generation-Skipping Transfer Tax Repeal in 2010**

Congress failed to address pressing estate and generation-skipping transfer tax matters before it adjourned in December. Consequently, as of Jan. 1, 2010, the provisions of 2001 federal tax legislation (the “2001 Act”) will cause the federal estate and federal generation-skipping transfer (GST) taxes to be repealed for one year, starting on Jan. 1, 2010.

For 2009, there was a \$3.5 million exemption for each tax and a 45 percent top tax rate for each tax. Under the 2001 Act, the federal estate and GST taxes will come back into effect on Jan. 1, 2011, but with only a \$1 million exemption for estate tax, a \$1.1 million exemption for GST tax (indexed for inflation), and a top rate of (generally) 55 percent for each tax.

Although the U.S. House of Representatives passed a bill in December to extend the 2009 federal estate and GST tax rates and exemptions, the U.S. Senate did not act to provide any similar extension. A number of Senators have made statements regarding their intent to address this issue early in 2010.

There is no way to predict when, or if, the House and Senate will act in 2010. It is not clear whether any action by Congress during 2010 would or could be retroactive to Jan. 1, 2010. We will continue to monitor developments as the tax picture evolves.

### **Summary of exemptions and rates**

<b>Year</b>	<b>Federal Estate Tax Exemption</b>	<b>Top Federal Estate Tax Rate</b>
<b>2009</b>	<b>\$3.5 million</b>	<b>45%</b>
<b>2010</b>	<b>NA</b>	<b>0</b>
<b>2011 and thereafter</b>	<b>\$1 million</b>	<b>55% (+5%)</b>

### **Gift tax**

The repeal of the federal estate and GST taxes does not repeal the federal gift tax, which will continue in 2010 with a \$1 million exemption, but will have a top rate of 35 percent, rather than the 45 percent top rate that existed in 2009.

## **Current action**

**Meanwhile, depending on the action taken by Congress and whether such action is retroactive (and, if retroactive, whether it will be constitutional), there may be opportunities in early 2010 to make gifts at a lower gift tax rate, and to make GST tax-free transfers to grandchildren that would otherwise be subject to GST tax.**

**Moreover, it is important to be aware that the repeal (and assumed reinstatement in 2011) of the federal estate and GST taxes will affect many estate plans now in place. This is so because many wills (and living trusts) describe gifts in terms of estate and GST tax “exemption” amounts or other formulas tied to federal estate tax terms. Elimination of the taxes (and hence the exemptions) and the reinstatement of the taxes, but with smaller exemptions, could affect the operation of a will (or living trust) in ways that were not intended.**

**This would be a good time to review and adjust estate plans to be sure the one-year repeal of the taxes and its (assumed) reinstatement will not adversely impact the intended plan. There may also be non-tax related reasons to review your estate plan. Please call if you would like to schedule a meeting to review your plan.**

### **“Carryover basis” for income tax purposes**

**As part of the 2010 repeal of the federal estate and GST taxes pursuant to the 2001 Act, the income tax basis for property acquired from a decedent will be the lesser of the decedent’s adjusted basis or the fair market value of the property at the decedent’s death. This “carryover basis” is a significant change from the “step-up” in basis that has historically occurred at the decedent’s death.**

**There are two exceptions to the carryover basis provisions that allow an executor (i) to allocate up to \$1.3 million to increase the basis of assets and (ii) to allocate an additional \$3 million to increase the basis of assets passing to a surviving spouse or to a qualified trust for the benefit of the surviving spouse. The carryover basis law is scheduled to be in effect only for 2010.**

### **Further changes in January 2011**

**As noted above, under the 2001 Act, the federal estate and GST taxes come back into effect in 2011 with a \$1 million exemption for estate tax, a \$1.1 million exemption for GST tax (indexed for inflation), and a 55 percent top rate. (There is also an additional 5 percent surtax for certain large estates.) The federal gift tax exemption of \$1 million will continue in 2011, but with a 55 percent top rate. The carryover basis described above would not apply with regard to estates of decedents dying after Dec. 31, 2010.**