

The Repeal of the Estate Tax and Other Fundamental Changes in 2010 and 2011

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Practice Area: Trusts and Estates & Estate Planning

As of January 1, 2010, the estate and generation skipping transfer ("GST") taxes are repealed, for one year, due to the unexpected failure of Congress to take any remedial action in 2009.

Changes Effective January 1, 2010

As the law now stands, the estate tax will not apply to individuals dying after December 31, 2009 and before January 1, 2011. In addition, the GST tax will not apply to generation skipping transfers made in 2010. The gift tax is retained as is the \$1 million gift tax exemption. The maximum gift tax rate for gifts in excess of \$1 million has been reduced from 45% to 35%.

Scheduled Changes on January 1, 2011

Beginning on January 1, 2011, unless Congress takes action this year, the maximum estate, GST and gift tax rates will equal 55% and the estate and gift tax exemptions will equal \$1 million. The GST exemption will be \$1 million, indexed for inflation. Estates between \$10 million and \$17.1 million in value will incur an additional tax of 5%.

Additional Complexity

Complicated new "carry-over basis" provisions have been in effect since January 1, 2010. Prior to 2010 the income tax basis of assets inherited from a decedent was adjusted or "stepped up" to the fair market value at the date of the decedent's death. Beginning January 1, 2010, each estate will be able to increase the decedent's cost basis in assets by \$1.3 million, plus an additional \$3 million basis increase for property passing to a surviving spouse. In Wisconsin these cost basis increases can also be applied to a surviving spouse's interest in marital property. The basis in property can not be increased beyond the fair market value at the decedent's death. Most estate planners believe that the 2010 carryover basis rules will be eliminated if the estate tax is reinstated.

Where We Go From Here

Congressional leaders vow that Congress will enact legislation reinstating the estate and GST tax with a \$3.5 million exemption to be retroactive to January 1, 2010. Others question whether such retroactive taxation would be constitutional or will ever take place. Whether and when Congress will take any action remains uncertain.

Impact on Current Estate Plans

Many estate plans include a formula based on the estate or GST tax to divide assets. For example, many plans include a Family Trust or other trust which is funded, by a formula clause, to the maximum extent possible that can pass free of estate or GST taxes. That formula clause may now control everything passing under the estate plan. This may or may not reflect your intent regarding the disposition of your assets. If necessary, this can be remedied by executing an amendment to your plan.

The tax law confusion creates some opportunities for high net worth people willing to make substantial transfers and willing to take the risk that there will be no effective retroactive enactment of estate or GST taxes in 2010.

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