

Guide to the New Estate Tax Law

May 23, 2011 By Jeramie Fortenberry

I recently completed a series of articles on Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, P.L. 111-312 (TRA 2010), which was signed into law by President Obama on December 17, 2010. I have given a few presentations on this topic recently and decided to turn my materials into a series of articles. The four articles are:

1. [**Introduction to the New Estate Tax Law**](#) – This article contains some of the background information and legislative history preceding the enactment of the new law. I know you'll want to skip ahead to the substance, but be warned: you can't really understand the new Act unless you have a good grasp on what came before it and the situation we found ourselves in in 2010.
2. [**Estate Planning Under the New Estate Tax Law**](#) – This article discusses the substantive provisions of the act, including the new applicable exclusion amount (exemption) and tax rates, retroactive application of the Act, and a few planning pointers.
3. [**Portability Under the New Estate Tax Law**](#) – This article deals with a brand new feature of our estate tax laws—portability. Portability allows the unused exemption of one spouse to be passed on to the surviving spouse.
4. [**Why Tax Planning Still Matters Under the New Estate Tax Law**](#) - This article explains why estate tax planning—including credit shelter/bypass planning—is as necessary now as ever.

TRA 2010 provides welcome relief from the uncertainty that plagued estate planners at the end of 2010. But it is more of a patch than a fix. Since TRA 2010 sunsets in 2012, we can expect these same issues to pop up again, along with more of the usual political wrangling over a permanent solution. And if the past ten years are any indication, Congress will wait until the eleventh hour to provide any clarity.

If Congress fails to act by the end of 2012, the applicable exclusion will drop to \$1 million and the estate tax rate will go up to 55 percent. In my opinion, that is probably the least likely scenario. It is more likely that the law will remain at current levels or drop to the \$3.5 million exemption and 45 percent tax rate proposed by Senator Baucus and backed by many Democrats. Of course, the possibility of another temporary fix of a different nature should not be ruled out.

Over the next two years, the higher applicable exclusion amount and lower transfer tax rates will slash the revenue from transfer taxes. Outright repeal of the estate tax will be an easier sell in 2012, after revenue has dwindled enough to make it less of a hot-button issue. Estate tax repeal is a more likely scenario than it has ever been and is likely to be re-proposed by the end of 2012. Whether the modified carryover basis regime will also be reintroduced is anybody's guess.

Note: The higher exemption amounts will also mean much fewer tax returns will be filed. Check out our post on the [Estate Tax Stats for 2001-2009](#) to get a good idea of how drastic the decrease may be. This means the IRS estate tax division will have some time on its hands. Expect high audit rates.

Given the continuing uncertainty, estate plans should not place undue reliance on the new Act or predictions about what Congress may or may not do before the end of 2012. As we did in the years leading up to 2010, we must plan for the law as it is and try to build in as much flexibility as possible into the estate plan.

Tax planning still has an important role in most estate planning documents. And in many ways, it will be more of a challenge over the next two years. Estate plans must now be flexible enough to (1) adjust for fluctuations in the applicable exclusion amount, (2) plan for the possibility of estate tax repeal at the end of 2012 and reintroduction of modified carry-over basis regime, (3) plan for special elections, such as portability and basis adjustments; and (4) do all of this while meeting the client's non-tax goals.