

TAX, TRUSTS & ESTATES LAW MONITOR

UPDATES AND COMMENTARY ON BUSINESS AND INDIVIDUAL TAX AND ESTATE PLANNING

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Estate and GST Tax Repeal - Action May Be Required

The following letter was recently distributed to clients and friends of Cole Schotz:

Dear Clients and Friends:

Due to Congressional inaction in the final weeks of 2009, the Federal estate tax has been repealed for individuals dying in 2010 and the generation-skipping transfer (“GST”) tax has been repealed for generation-skipping transfers made in 2010. However, current law provides that the estate tax and GST tax will be restored as of January 1, 2011 with only a \$1 million applicable exclusion and a \$1 million GST exemption, indexed since 1998 for inflation, as compared to the \$3.5 million applicable exclusion and GST tax exemption that had been in effect in 2009. The Federal gift tax remains in place (though at a lower tax rate) with a \$1 million exemption and will not change except as to certain specialized trusts.

It was widely anticipated in the tax and estate planning community at large that Congress would take action before the end of 2009 to prevent this result. Therefore, virtually all tax professionals determined that it was unnecessary for clients to undertake a review of their estate planning documents prior to the end of 2009. Since Congress did not act, however, it is important for you to be aware of this situation which will likely be resolved in one of the following ways:

1. Congress could pass legislation which reinstates the estate tax and GST tax with specified exemption amounts that would be retroactive to January 1, 2010;
2. Congress could pass such legislation that would be effective as of a later date; or
3. Legislation will not be passed in 2010, in which case, there would be no estate or GST tax in effect until January 1, 2011, when those taxes would be reinstated with a top estate and GST tax rate of 55%, an applicable exclusion amount of \$1 million and a GST exemption of \$1 million, indexed since 1998 for inflation.

Of course, other scenarios are always possible as Congress’ action or inaction is impossible to predict. We will closely follow all discussions in Congress, review all proposed bills, and advise

you when legislation has been enacted. We also will post updates to our tax blog (www.taxtrustsandestateslawmonitor.com) on these matters as they break.

While the prevailing view is that Congress will address these issues and retroactively restore the estate and GST taxes effective as of January 1, 2010, there is no guarantee that this will occur. Therefore, it is important that you are aware that the current state of the law, with repeal in place, could create unintended results as to how your assets will pass at the time of your death and could result in adverse tax consequences. Whether your particular situation is impacted and, if so, in what manner, depends on the particular wording in your Wills, Trusts and other estate planning documents and on your family and financial circumstances.

Examples of only a few of the situations that could produce unintended results include (i) an allocation of assets between the children of a current or prior marriage and a surviving spouse and (ii) an allocation of assets between children and grandchildren, where such allocations are based on tax concepts that were in effect when your Wills were executed but are no longer in effect under current law. In both of these cases, assets may be distributed in a way that you did not intend. The potential tax consequences that could result if the repeal stays in effect are literally too numerous to mention here, and must be explored on an individual basis.

Another change that applies only in 2010 relates to the tax basis of inherited assets. Under the law in effect prior to 2010 and again in 2011, the tax basis of inherited assets generally changes to the value of those assets on the date of the decedent's death. Under the law now in effect, however, the basis in inherited assets remains the same with two limited exceptions: (i) up to a \$1.3 million increase in basis will apply to assets passing to beneficiaries on a decedent's death and (ii) up to an additional \$3 million increase in basis will apply to assets passing to a surviving spouse.

Given that the potential tax and distribution impact could be significant, we suggest that you contact a member of our Tax, Trusts and Estate Department to review the effect of this change in law on your estate plan, whether or not we drafted your estate planning documents.

Best wishes for a happy and healthy new year.

Very truly yours,

Cole, Schotz, Meisel, Forman & Leonard, P.A.

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