

Now What? Repeal of The Federal Estate Tax And Implications For Estates in 2010  
*By John F. McDermott, Attorney at Law*

Despite all indications to the contrary, Congress failed to act in 2009 to prevent the repeal of the Federal Estate Tax. Therefore, for the one calendar year 2010, there is no estate tax or generation-skipping transfer (“GST”) tax on any estate regardless of size. This article makes general observations applicable for the 2010 calendar year, or for a shorter period of time should Congress act to reinstate the estate tax - perhaps retroactively to January 1, 2010.

Although the estate tax has been repealed, the Federal Gift Tax remains in effect. The annual gift tax exclusion amount remains at \$13,000 per gift, and the lifetime exemption from gift tax remains at \$1 million.

Importantly, many people have wills that use formulas referring to provisions in the estate tax laws to determine amounts passing to a spouse, children, grandchildren, other family members or charities. Estate tax repeal could make the interpretation and application of these formula provisions unclear or cause the amounts passing under the formula to be different from what was expected when the will was prepared. For example, a will might contain a formula allocating the maximum amount that can pass free of estate tax to a family trust and leaving the remainder of the estate to the spouse. Because the estate tax has been repealed, such a formula might now direct more of the estate to the family trust than was intended. Similarly, a will might leave grandchildren an amount equal to the testator’s remaining exemption from GST tax. If no GST tax exists, the amount intended could be difficult to interpret from such language.

The changes in the law during 2010 also affect income tax planning. New rules apply for 2010 concerning the income tax basis of property acquired from a decedent. Income tax basis is the value from which gain or loss on assets sold is measured. Before 2010, the income tax basis of an asset changed to its current value on the date that its owner died. For 2010, this automatic “step up” in basis will not incur. Instead, the deceased owner’s income tax basis will “carry over” to the persons who inherit the assets (unless the value at the owner’s death is lower). This change will affect far more people than were affected by the estate tax, particularly since the estate tax exemption had risen to \$3.5 million in 2009.

During the period of repeal, the basis of property acquired from a decedent will be the lower of (i) the decedent’s income tax basis (“carryover basis”) or (ii) the value of the property on the decedent’s date of death. Therefore, while no step-up in basis is allowed, the basis of property might be stepped down. The law further provides that up to \$1.3 million in additional basis may be allocated to property left to any heir, and that up to \$3 million in additional basis may be allocated to property left to the decedent’s spouse, either outright or in a qualifying trust for the spouse. Clearly, this allocation process will be complicated, and the IRS has not yet issued guidance or forms.

The 2010 hiatus from estate tax lasts for only one year under current law. As of January 1, 2011 the estate tax will return at higher tax rates and lower exemption amounts than applied in 2009. There is speculation that Congress will act to terminate the estate tax relief earlier and that a reinstatement of the estate tax may be made retroactive to January 1, 2010. Therefore, there remains considerable uncertainty regarding what, if any, estate tax will be imposed on estates of persons who die in 2010.

To more fully understand how these changes may affect your individual estate plan, you should contact your estate planning attorney or advisors.

John F. McDermott is an attorney with the Baton Rouge, Louisiana law firm of Taylor, Porter, Brooks & Phillips, L.L.P. [www.taylorporter.com](http://www.taylorporter.com)