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FINANCIAL FOCUS



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Your Accounting for a New Economy

Will the Estate Tax Stay Repealed for 2010?

In 2001, a law was passed that gradually phased out the federal estate tax through 2009, and repealed it altogether in 2010. That law, however, “sunset” or expires in 2011 and reinstates pre-2001 tax law levels (with an exemption of \$1 million and a top tax rate of 55%). Since 2001, the economic and political climate in the United States has hanged significantly. The federal budget deficit has ballooned, the financial markets have been in turmoil, and most importantly, power has shifted to the Democrats. So, the question is: just how likely is it that 2010 will be an estate tax-free year?

Chance of repeal?...virtually zero

Of course, anything can happen, but President Obama has made it clear that he believes the estate tax should continue in some form or other. And in the Senate, Finance Committee Chairman Max Baucus has firmly stated “...repeal isn’t going to happen.” With increased Democratic majorities in both chambers of Congress, it seems highly likely that some action will be taken soon to head off the one-year sabbatical scheduled for 2010.

Future of the estate tax

Several bills have been introduced in Congress in the intervening years since 2001, some calling for full repeal, others for reform. Reforms that have been proposed include:

- Raising the exemption and/or lowering the tax rates
- Making the exemption “portable” between spouses (allowing surviving spouses to use any unused portion of the deceased spouse’s exemption)
- Replacing the estate tax with an inheritance tax (transferring the transfer tax burden to heirs)

- Replacing the step-up in basis rule with a carryover basis rule (also transferring the tax burden to heirs in the form of capital gains tax)

President Obama has endorsed the following reforms:

- Freezing the estate tax at 2009 levels (\$3.5 million exemption and 45% top rate)
- Indexing the exemption for inflation
- Disallowing or limiting valuation discounts

Planning for continued uncertainty

All indications point to the estate tax remaining for the foreseeable future. While the uncertainty that continues to surround the exact components of the estate tax may tempt some individuals to do nothing or wait and see, it may be wiser to review your plans now to ensure that they can withstand the winds of change.

Creating a flexible estate plan is the key to avoiding the pitfalls of future tax law changes, as well as changes that may occur in your personal life. A flexible estate plan uses language and provisions in wills and trusts that maximize the ability to pass estate assets free of estate taxes. And other tools, such as disclaimers and powers of appointment, can allow heirs or trustees to respond to circumstances existing at the time of your death.

Beyond tax

Remember that dealing with estate taxes, no matter what the future may hold, is just a piece of your estate plan. An experienced financial professional can help you identify strategies that may help you achieve your overall estate planning goals.