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A DISTRACTED CONGRESS ALLOWS ESTATE TAX TO EXPIRE

LEGISLATIVE INACTION CREATES CONSIDERABLE UNCERTAINTY

In an act of neglect considered unthinkable only weeks ago, Congress ended its 2009 session without extending the federal estate and generation-skipping transfer (GST) tax systems, forcing both to “sunset” as of December 31.

Rescission was scheduled in a 2001 law that steadily increased the exemption from these taxes to \$3.5M, while reducing the top tax rate to 45 percent through 2009. As of January 1, the estate and GST taxes have disappeared altogether, and the top gift tax rate has dropped to 35 percent with the lifetime exemption remaining at \$1M.

All this looks more like a product of Congressional diversion than an intentional effort to abolish the 93-year-old estate tax. Throughout the year multiple bills were proposed in the House and the Senate, the most recent simply extending 2009 law, but none were ultimately debated and passed. Although the political winds may have shifted during the recess, **HRO believes that the most likely scenario now is for a retroactive extension of 2009 law soon after Congress reconvenes.** But even assuming that Congress enacts legislation retroactive to January 1, the gap period poses several concerns and perhaps some opportunities:

- *The Retroactive Effect May Not Stand* – The IRS has a long and successful track record defending retroactive tax rate changes in the courts, but enacting a “new” tax to be effective before its passage may not be deemed constitutional. Estates of decedents dying in the gap period will inevitably make that argument, triggering protracted litigation. Short of dying to exploit this confusion, there may be opportunities for generation-skipping transfers during the gap that could ultimately prove to be tax-advantageous.
- *Taxable Gifts* – While the gift tax remains, a reduction in the maximum tax rate from 45 percent to 35 percent could alter the analysis in determining whether to make a taxable gift. Similarly, a transfer that could later be treated as a gift, such as an intra-family loan, might be best timed for the lower rate period.
- *Estate Plan Review* – Given these uncertainties, and the recent gyrations in asset values and estate tax exemptions, **HRO recommends a review of your estate plan to ensure that it still accomplishes your family and charitable goals.** While most tax-sensitive plans are written with formulaic allocations that adjust to changing exemption amounts, applying current law could distort your non-tax objectives, resulting in an unintended division of your assets. An evaluation of how you hold your assets and how they would now be distributed under your plan has become critical in light of these developments. A straightforward codicil to your will (or amendment to your trust) could ensure that your plan still reflects your intentions.

Please contact us if we can answer any questions or assist in a review of your plan.

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