

private client services update

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WHAT'S THE LATEST ON ESTATE TAXATION?

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Taxpayers and tax planners alike are eager for news from the federal government on estate tax legislation. In earlier updates, the Kaufman & Canoles Private Client Services Group provided extensive background on the recent history of estate taxation, and the return of estate taxation in 2011. Congressional action has been expected, but not forthcoming.

The Economic Growth and Tax Relief Reconciliation Act passed in 2001 increased the estate tax exempt amount in a series of steps culminating with the \$3.5 million per person tax exempt amount applicable in 2009. The maximum federal estate tax rate likewise decreased under the 2001 legislation, and was set at 45% during 2009. The 2001 legislation went on to provide that federal estate tax would be eliminated in 2010. But the law provided that, absent action by Congress in the interim, estate taxation would return in 2011 with a lower \$1 million exemption and a higher 55% maximum tax rate.

Also, the step-up in basis rules which provided very favorable capital gains treatment for inherited assets were modified for 2010, increasing the capital gains taxes payable by many families.

Seeing government spending levels in 2008 and 2009, many estate planners and tax professionals predicted confidently that Congress would act before the end of 2009 in order to prevent elimination of the estate tax and loss of the revenue it generated. No legislation was enacted, however, and January 1, 2010 brought a year with no estate taxation at the federal level, modified step-up in basis rules and a great deal of uncertainty over the future of the federal estate tax.

Little concrete action has taken place in Congress on the topic. Before the end of 2009, the House of Representatives passed a bill which would have continued estate taxation under the laws in effect during 2009: a \$3.5 million per person exemption and a maximum federal estate tax rate of 45%. The Senate did not act on that bill.

Several bills have been advanced this year in both the House and the Senate. One proposal from Senators Lincoln (D-AR) and Kyl (R-AZ) followed the House bill (\$3.5 million/45%) and would have made the estate tax retroactive to January 1, 2010. Another recent bill, put forward in June by Senator Sanders (I-VT) proposes a \$3.5 million per person exemption and a 45% maximum tax rate, with the tax rate increasing on large estates above \$10 million. Senator Sanders' bill also includes a surtax on billionaires. An identical bill was introduced in the House in July. The debate seems to center on whether the exemption should be \$3.5 million per person or a greater \$5 million per person exemption and whether the maximum tax rate should be 35%, 45% or 55%. There does not appear to be much support in either chamber to eliminate the estate tax or to adopt an exemption below \$3.5 million.

Just as lawyers, accountants, and their clients are eager for a tax law around which to plan, significant citizen and lobby groups are clamoring for action by Congress. Farmers and small business persons, who are often identified as among the hardest hit if the estate tax returns with the lower \$1 million per person exemption, are organizing to push for relief legislation from Congress. The American Farm Bureau Federation, an organization representing the interests of farmers across the country, has joined with the United States Chamber of Commerce,

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the American General Contractors Association, the National Association of Manufacturers and other groups representing small businesses in advocating the return of an estate tax they once battled to eliminate. This quixotic position is driven, apparently, by realization that the elimination of estate tax on a permanent basis is quite unlikely.

The Obama administration has likewise been quiet on estate taxation, although the 2011 budget put forward by the President assumed a \$3.5 million per person exemption and a 45% maximum tax rate, consistent with his campaign platform.

Few estate tax planners are willing to predict the fate of estate taxation at this point. Key mid-term elections in November are likely to make both Democrats and Republicans shy away from enacting an estate tax law in coming weeks. Thus, the specter looms of a return of estate taxation with a lower \$1 million exemption, increasing dramatically the number of Americans who face estate tax and who therefore need careful estate tax planning by qualified tax professionals.

This means that individuals and couples with assets (including life insurance proceeds) valued at more than \$1 million, small business owners and farmers must keep a close eye on the evolution of estate tax legislation. A review of existing wills and trusts by a tax advisor is important. Because more Americans face capital gains and estate taxes in this legal climate, more careful, and frequent planning is in order.



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