

# Estate, GST And Gift Tax Law In 2010

## Estate, GST And Gift Tax Law In 2010

**Insight — 1/12/2009 12:00:00 AM**

As you may be aware, current federal tax law repealed the federal estate tax and generation-skipping transfer ("GST") tax for one year beginning January 1, 2010. Although it was widely anticipated that Congress would take action in 2009 to prevent this repeal, it failed to act in time. As a result, significant changes in the tax law took effect on January 1, 2010. These changes impact the estates of decedents who die in 2010 and potentially create opportunities for lifetime tax planning in 2010.

Congress has indicated, however, that it will attempt to re-enact estate and GST taxes and repeal other changes in the new law in early 2010, with retroactive application. Whether retroactive taxation is constitutional is likely to be challenged in the courts. As a result, the practical impact of the current law, as well as the availability of potential planning opportunities, remain in question.

### Estate, GST and Gift Tax Changes

Under current law, beginning on January 1, 2010, there is a one-year repeal of the federal estate and GST taxes. The federal gift tax remains in effect with the same \$1.0 million lifetime gift tax exemption, but the highest gift tax rate drops to 35%. In 2011, the current tax law will "sunset," and the estate, GST and gift taxes will return with significantly higher tax rates and lower applicable exemptions than were in place in 2009. The following chart notes the tax rates and exemptions under current law:

	2009	2010	2011
Estate Tax Exemption Amount	\$3.5 million	Estate Tax Repealed	\$1.0 million
Gift Tax Exemption Amount	\$1.0 million	\$1.0 million	\$1.0 million
GST Exemption Amount	\$3.5 million	GST Tax Repealed	\$1,060,000 plus inflation adjustment
Highest Estate Tax Rate	45%	Estate Tax Repealed	55%
Highest Gift Tax Rate	45%	35%	55%
GST Tax Rate	45%	GST Tax	55%

		Repealed	
--	--	----------	--

These changes could impact certain estate plans that contain formulas to utilize the marital deduction and/or the estate and GST tax exemptions. For example, a common plan for a married couple avoids estate tax at the first spouse's death by funding, to the extent possible, a credit shelter or family trust for the decedent's children and leaving the balance of the estate to the spouse. Depending on the formula provisions and the beneficiaries of the trust(s), if there is no estate tax in 2010, these provisions could have unintended consequences with respect to the gifts to the spouse and children. In many cases, the spouse is a beneficiary of the credit shelter or family trust, and the practical impact of the estate tax repeal is diminished. However, in some plans, the impact could be significant. Any such scenario assumes that Congress fails to take action regarding the one-year estate and GST tax repeal and that the individual's death occurs in 2010.

### **Carryover Basis in 2010**

Another significant change is the adoption of the carryover basis system for inherited assets, which applies only for 2010. Under 2009 law, a decedent's assets generally received an income tax basis equal to their fair market value at the decedent's death. This basis "step-up" (or, in some cases, "step-down") had the effect of eliminating any built-in gain or loss in the assets at the decedent's death. Thus, a beneficiary could generally sell an inherited asset without income tax consequences.

In 2010, the basis of inherited assets will no longer be stepped-up to fair market value. Instead, a beneficiary's basis in inherited property will generally be equal to the decedent's basis in such property (or, if lower, the fair market value of the property at the decedent's death). As a result, a beneficiary inheriting an appreciated asset in 2010 could incur capital gains tax upon selling the asset.

There are certain exceptions to the new 2010 carryover basis rules. Under current law, the personal representative of a decedent's estate can increase the basis of a decedent's assets by up to \$1.3 million for assets passing to any beneficiaries, and by up to \$3.0 million for assets passing to a surviving spouse (outright or in certain qualifying trusts). Given the complexities of this new carryover basis regime, a review of your estate plan may be appropriate to determine whether updates are advisable to take advantage of the \$1.3 million and \$3.0 million basis adjustments. The carryover basis rules are only applicable for decedents who die in 2010 and potentially could be eliminated by Congress, possibly retroactively.

### **Planning Opportunities**

While Congress's failure to act in 2009 adds uncertainty to the estate planning landscape, the temporary repeal of the GST tax and the reduction in the gift tax rate may create planning opportunities. Due to the one-year repeal of the GST tax, for example, 2010 may be an advantageous time to establish dynasty trusts or transfer assets to grandchildren without being subject to GST tax. In addition, the reduction in the gift tax rate to 35%

could make 2010 an opportune time to make large gifts that are subject to gift tax.

### **Review of Estate Plans**

The tax law changes and uncertainty may warrant a review of your estate plan and updates to your estate planning documents. You may also wish to consider transactions that take advantage of the potential 2010 tax planning opportunities. If you have questions about the tax law changes and their impact on your estate plan, please contact a member of our Private Client Group.

**Circular 230 - This communication was not written and cannot be used for the purpose of avoiding Federal tax penalties that may be imposed on you, unless specifically stated.**

---

*Subscribe to get our Insights delivered to your inbox.*

*This publication is designed to provide general information on pertinent legal topics. The statements made are provided for educational purposes only. They do not constitute legal or financial advice nor do they necessarily reflect the views of Holland & Hart LLP or any of its attorneys other than the author(s). This publication is not intended to create an attorney-client relationship between you and Holland & Hart LLP. Substantive changes in the law subsequent to the date of this publication might affect the analysis or commentary. Similarly, the analysis may differ depending on the jurisdiction or circumstances. If you have specific questions as to the application of the law to your activities, you should seek the advice of your legal counsel.*