

## The Estate Planning Advisor

# Federal Estate Tax Is Repealed – But For One Year Only!

By Richard J. Shapiro, J.D.

From the moment in June 2001 that President Bush signed into law the legislation that provided for the repeal of the federal estate tax in 2010, estate planners have been convinced that Congress would by now have acted to “fix” what is widely acknowledged to be preposterous tax policy. Not only does the repeal exist for this year only, but the federal estate will return with a vengeance in 2011, as the exemption returns to its 2000 level of \$1 million per person. Compared with the 2009 exemption of \$3.5 million, 2011 will see many more “middle class” estates subject to the imposition of federal estate tax.

But just because there is no federal estate tax in 2010 doesn't mean that Congress has necessarily done taxpayers a huge favor. That's because 2010 also brings the elimination of the unlimited “step-up” in basis for inherited assets. In 2010, only the first \$1.3 million in assets (\$4.3 million if there is a surviving spouse) will be valued at their “date of death” value for capital gains tax purposes. All other assets will be passed to the heirs at a “carryover” tax basis, and will result in the imposition of a capital gains tax if appreciated assets are later sold by the heirs. Trying to determine the original tax basis of many assets – especially stocks that may have been owned by a decedent for many years – will be a record-keeping nightmare.

We're already seeing the impact of this irrational tax policy. A recent article in the *New York Post* described how 87 year-old Fritz Lohman died at 11:00 a.m. on New Years' Eve. Since Lohman died in 2009, his \$10 million estate will be subject to a total federal and New York State estate tax in excess of \$3.5 million. Had Lohman survived thirteen hours, his estate would have been subject to a New York estate tax of about \$1 million.

Why this tax roller coaster? When the current estate tax legislation was passed in 2001, the Senate's budget rules required that the legislation “sunset” in 2011. The Republicans were then able to claim that they had lived up to their 2000 election promise to repeal the estate tax, leaving it to future Congresses and Presidential administrations to come up with a more permanent resolution. The Republicans came close to passing a permanent repeal of the estate tax during the latter years of the Bush administration, but fell a few votes short. Today, with the nation fighting wars on multiple fronts, facing the need to fund an ambitious health care plan, and trying to keep Social Security afloat -- all during a period of economic stagnation -- it seems unlikely that Congress will be willing to forego the revenue that would be generated by the estate tax beginning in 2011. At best, we may see legislation enacted that will return the tax to the 2009 per person exemption of \$3.5 million.

What's the average person to do? Married couples with total assets (including the value of the death benefit of their life insurance) in excess of \$2 million need to review their wills or living trusts to ensure that the estate tax planning language takes into account the possibility of a death in a year without a federal estate tax. The absence of such a "savings clause" might lead to the unintended result where all of the deceased spouse's assets pass into a "credit shelter trust" for the benefit of the deceased spouse's children – with nothing passing to the surviving spouse!

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