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As you may have heard or read, the Federal estate tax and generation-skipping transfer tax were repealed effective January 1, 2010, and they are scheduled to return on January 1, 2011. In addition, and less publicized, the maximum federal gift tax rate was reduced from 45% to 35%, and the stepped-up basis at death rules were replaced with a modified carryover basis regime effective January 1, 2010.

These changes to the transfer tax system have been in place since 2001, but very few practitioners expected them to become law. Most thought Congress would act to stop the repeal before December 31, 2009, but Congress was overwhelmed with health care reform and simply ran out of time. It is likely that Congress will enact new legislation in 2010 which will revoke the repeal of the taxes and reinstitute the maximum gift tax rate and stepped-up basis rules. However, it is unclear what the new rules will be and whether Congress will attempt to apply the new rules retroactively to January 1, 2010 (or whether such a retroactive application would survive a constitutional challenge).

In the past, many wills and trusts were drafted to minimize the payment of Federal estate tax with certain formula clauses using Federal estate tax terms. It is not entirely certain how these formula clauses will be construed if a person dies when there is no Federal estate tax in place. Wills and trusts need to be reviewed because each case is different and will depend upon the exact words used in each document.

Some clients may decide to have their current wills and trusts reviewed now in light of the repeal of the estate tax. Others may decide to wait and see what Congress does before reviewing such documents. If new wills and trusts, or amendments to existing wills and trusts, are signed now, such new documents may need to be reviewed again if (or some might say when) new legislation is enacted. If clients decide to wait, but then die prior to the enactment of new legislation, their testamentary intentions may not be achieved without incurring additional legal costs involving disclaimers or trust reformation proceedings in a probate court.

Aggressive clients may see this as a window of opportunity. The maximum gift tax rate is at an historical low. If clients believe that they will ultimately pay Federal estate tax, such clients might want to make a significant gift now and pay gift tax at the lower rates. Unfortunately, if new legislation is enacted retroactively, such clients may find themselves in a legal battle with the Internal Revenue Service to obtain the desired tax benefits.

We hope that you appreciate the complexity of the situation and understand there is no single solution for every client. Our goal is for you to understand your options, as well as the advantages and disadvantages of each option. We encourage you to contact us so we may assist you through this process. Please contact one of our estate planners listed to the left.

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