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Federal Estate Tax Repealed (For One Year Only, or Possibly Not at All)

As you may have learned from *The Wall Street Journal*, *The Washington Post*, *Los Angeles Times*, *Baltimore Sun* or other news media, Congress did not pass legislation in 2009 to extend the current Federal estate tax rate and exemption level. As a result, the Federal estate tax is repealed from January 1, 2010 through December 31, 2010.

The District of Columbia and Maryland still impose an estate tax on all taxable estates in excess of \$1,000,000. Virginia currently has no estate tax.

[New Tax Basis Regime](#)

With the repeal of the Federal estate tax comes a change to the income tax treatment of a decedent's property. For decedents dying in 2010, the basis of the assets in the estate will not be adjusted to the fair market value as of the date of death. Instead, the beneficiaries of the decedent's estate will receive "carryover" basis in the assets; meaning, the beneficiary's basis in the asset will be the same as the decedent's adjusted basis as of his or her date of death. There are exceptions to this rule. In general, assets passing to a surviving spouse that have up to \$3,000,000 of appreciation over the decedent's adjusted basis will receive a "step-up" in basis to the date of death value. In addition, assets passing to any other beneficiary or beneficiaries with up to \$1,300,000, in the aggregate, of appreciation over the decedent's adjusted basis may receive a step-up in basis to the date of death value. The amount available for this basis step-up could increase if the decedent had certain unrecognized losses at the time of death.

[Reinstatement of Estate Tax in 2011, or Retroactively to 2010](#)

Unless Congress passes estate tax reform legislation in 2010, the Federal estate tax will be reinstated in 2011, with an exemption of only \$1,000,000 and a maximum tax rate of 55% (with an additional 5% tax on the portion of the estate between \$10,000,000 and \$20,000,000).

It is possible that Congress will pass estate tax reform legislation in 2010 that will be effective retroactive to January 1, 2010. Any such retro-enactment of the Federal estate tax could be subject to constitutional challenge, leading to further delay and confusion. As a result, the uncertainty surrounding the Federal estate tax currently knows no bounds. We cannot offer any assurance that the estates of persons dying in 2010 will be exempt from Federal estate tax – we simply do not know if that will be the case.

[Generation-Skipping Transfer Tax Repealed](#)

The generation-skipping transfer ("GST") tax that applies to most transfers from a grandparent to a grandchild or more remote descendant is also repealed for one year, beginning January 1, 2010. As with the estate tax, Congress could retroactively reinstate the GST tax to the first of the year. Nevertheless, there may be planning opportunities for gifts to dynasty trusts (for the continuing benefit of your descendants) in 2010.

[Gift Tax Remains in Effect](#)

Unless otherwise changed by legislation, the Federal gift tax will remain in effect in 2010. The lifetime exemption from gift tax continues to be \$1,000,000 and is not indexed for inflation. Thus, a person may make up to \$1,000,000 of aggregate lifetime gifts – in excess of (i) gifts that qualify for the marital deduction, (ii) the gift tax annual exclusion amount and (iii) payments of certain medical and tuition expenses directly to the provider – without having to pay any gift tax. The gift tax annual exclusion amount also remains unchanged, at \$13,000 per donee (or, \$26,000 per donee for spouses electing to gift split) in 2010.

[Gift Tax Rate](#)

In 2010, the gift tax rate will be tied to the top marginal income tax rate, which means the gift tax rate drops from 45% to 35%. If, however, Congress passes retroactive estate tax legislation in 2010, there is a risk that it could also retroactively raise the gift tax rate. Although we cannot be certain, it may prove beneficial to make any gifts that could cause Federal gift tax to be incurred as early in 2010 as possible, just in case any 2010 legislation is made prospectively, and not retroactive to January 1, 2010. In that event, early planning would

enable donors to take advantage of the 35% gift tax rate.

Please note it has always been our practice at Venable to provide clients with flexible estate planning documents designed to accommodate changes in tax laws and family circumstances. However, in light of this new uncertainty created by Congress, you may wish to contact us in the new year to ensure your estate plan continues to meet your goals.

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