ESTATE TAXES – IS 2010 THE BEST YEAR TO DIE?
By Jane M. McNamara, Attorney

Estate planning attorneys have joked that 2010 is the year to die. I personally have made terrible and inappropriate (yet funny) jokes about "pulling the plug" in 2010. Why? Because there is no estate tax in 2010. The federal estate tax disappeared this year, but is scheduled to return in 2011 in a big way. Next year, estates of more than $1 million are expected to be subject to federal estate tax – whereas in the past it was $3.5 million. And what's in an estate? Everything – real estate, life insurance, retirement, etc.

Last year (2009), an estate could have $3.5 million before the federal estate tax kicked in. We lawyers thought that Congress would get together in 2009 and extend the $3.5 million estate tax exemption for at least several more years. We really never thought Congress would allow a complete repeal of the estate tax in 2010 - surely Congress would get together well before 2010 and tinker with the law. And, when they tinkered, Congress would surely raise the $1 million estate tax exemption scheduled to be in effect in 2011. After all, most members of Congress have more than $1 million, they are all aging, and they don't want their estates to be taxed! But, our predictions were wrong...really wrong...and there has been no tinkering.

Congress has been unable to reach any agreement. True, they were very busy with the Health Care Reform laws, so it seemed no one really raised a fuss about the estate tax laws. 2010 crept in, and now there is no estate tax. And, 2011 will be here before we know it, with only a $1 million estate tax exemption. But, change may be in the air. There is a lot of talk about whether Congress has the legal ability to reinstate the estate tax now and make it retroactive to the first of the year. Will this happen? Who knows! We were predicting changes in 2009 that never happened, so nothing is clear.

Although it sounds like the wealthy can pass on millions tax-free in 2010 when they die, this actually isn't true. True, there is no estate tax in 2010. However, capital gains tax rules can be harsh for larger estates. As the rules now stand for the estate of someone dying in 2010, there is no estate tax, but accumulated capital gains can be taxable if and when heirs sell the property they inherit. How does this work? It is all centers on "carryover basis." Lets imagine you bought $1 million worth of stock in 2000, and it is now worth $4 million. You die in 2010. Your heirs receive the $4 million without estate tax. However, when they sell the stock, it's as if they paid $1 million for the stock (their carryover basis), and they have a taxable gain – and tax must be paid on any gain over $1.3 million. So, if they sold the stock for $4 million, they would get a $1.3 million exemption, and have to pay tax on the rest. So, even with no estate tax in 2010, heirs may still wind up paying quite a bit of capital gains tax.

The truth is, not very many Americans have that kind of net worth. But what if you are worth more than a million? The best answer for now might be to keep an eye on what Congress is doing, and consider having your estate plan reviewed. An update in your estate plan will depend on your net worth, the types of assets you own, your marital status, and your intended beneficiaries. But, it is important that we keep our eyes open, and see what's going on in Congress in the next several months.

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