Now that the presidential election is over much of the national chatter has shifted to the "fiscal cliff" looming at the end of the calendar year when the terms of the Budget Control Act of 2011 are scheduled to go into effect. If Congress fails to reach a consensus on how to reconcile those provisions with the reality of the current fiscal situation in the United States, there will be far reaching consequences to taxing and spending across the board.

Under the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 Congress voted to extend the Bush-era tax cuts as they related to estate taxes. This avoided a sunset provision written into the Economic Growth and Tax Relief Reconciliation Act of 2001 which would have caused estate tax exemption amounts and tax rates to revert to the 2002 exemption level with a 2001 top rate. However, the law was only enacted to cover 2011 and 2012.

Year	**Exclusion Amount**	**Max/Top tax rate**
2001	$675,000	55%
2002	$1 million	50%
2003	$1 million	49%
2004	$1.5 million	48%
2005	$1.5 million	47%
2006	$2 million	46%
2007	$2 million	45%
2008	$2 million	45%
2009	$3.5 million	45%
2010	Repealed	
2011	$5 million	35%
2012	$5.12 million	35%
2013*	$1 million	55%
* under current law		

Under current law, in 2013 the estate tax will revert to the higher 2001-2002 levels, unless new legislation is passed altering that course. Estates valued at $1 million or more would again be subject to tax at progressive rates as high as 55% and portability (the ability of the surviving spouse to use up a deceased spouse's exemption) would disappear.

Only time will tell what the outcome will be, but based on President Obama's 2013 budget proposal, we can make a few educated guesses on what we may see:

Exemption Amount: Under President Obama's proposed plan, the exclusion amount would be set at $3.5 million per individual. $3.5 million was the exclusion amount in 2009, which looks to be the year which the president's plan would seek to mirror.

Tax Rate: The president's budget would call for a 35% tax rate on any amounts above the $3.5 million that passed as part of a decedent's estate. In theory, a lower tax rate reduces the tax owed for all taxable estates but saves the most money for the largest estates.

As an illustration, consider some numbers run by the independently operated Tax Policy Center if the exemption was raised from the default $1 million to the 2009 $3.5 million amount and the top rate was reduced from 55% to 45%. The exemption increase would reduce the number of taxable estates by more than 80 percent from about 53,000 to roughly 7,500 in 2013 and would save larger estates $1.38 million in tax (at a 55 percent rate). The rate cut would have a much larger effect for large estates: an estate with a taxable value of $5 million (after the exemption and any deductions) would save $500,000 while an estate worth $500 million would save $50 million in tax.

Portability: A key piece of the current legislation is called *portability*, which is the ability of a surviving spouse to use the exclusion amount of the deceased spouse when exempting an amount from estate tax liability.

For illustration purposes, let's assume the $3.5 million exemption is enacted beginning in 2013. Now, say Husband and Wife have $6 million in total assets and their individual wills transferred all assets to the surviving spouse. If Husband dies in 2013, Wife would inherit all of his assets without incurring any federal estate taxes (due to the ability of spouses to transfer unlimited assets to each other tax free). At this point all is well and good. However, without portability, Husband's estate tax exclusion has now been wasted. When Wife dies a year later, her $6 million estate will be subject to estate tax since she is only permitted to exempt the first $3.5 million of value from tax. This means that, without portability, Wife's estate would pay estate taxes at a rate of 45% on $2.5 million. Enter sad beneficiaries.

But, look at the same example with portability. When Husband dies in 2013, all of his assets pass to Wife tax free just like the first example. However, now, portability will allow Wife to carry over Husband's $3.5 exemption amount and preserve it. When Wife dies in 2014 not only can she use her $3.5 million exclusion but she can use Husband's unused $3.5 million exclusion as well (for a total exclusion amount of $7 million) enabling her to pass the entire estate to the chosen beneficiaries free of federal estate tax.

The benefit of portability to married couples is obvious, and given the current makeup of Congress, chances are good that portability will become a permanent part of any estate tax legislation.

There are a number of other areas in which the president is proposing modifications to current law, many of them centering around various valuation rules. From the Tax Policy Center, some of these include:

Requiring consistency in value for transfer and income tax purposes

The proposal would require recipients of substantial gifts or estates to limit their basis in any received gift or inheritance to that used by the donor. This would limit a recipient's ability to lower capital gains by claiming a higher basis.

Modify rules on valuation discounts

Valuation discounts have been commonly used in the past to reduce the tax payable on transfers of interests in family controlled entities. The administration would like to substantially limit their use as a tax-avoidance mechanism.

Require a minimum term for grantor-retained annuity trusts

Grantor Retained Annuity Trusts (GRATs) are a mechanism by which an interest in a trust is transferred to a family member whereby the creator of the trust receives an annuity off of the transferred assets for a specified period of time. The key, however, is that the creator of the trust who is receiving the annuity must outlive the chosen annuity period in order to see the tax savings. The president would like to set a minimum time frame on these trusts increasing the risk that the trust creator will die during its term, thereby subjecting the assets to estate tax.

Extend the Lien on Estate-Tax Deferrals Provided under Section 6166 of the Internal Revenue Code

Estates that are structured around closely held business interests have the ability to defer payment of any estate tax for up to 14 years under the theory that the significant tax payments could detrimentally affect the business. However, there is a risk that any business afforded that protection could fail within that 14 year period. Under the current laws, a tax lien can be placed on the estate to recover the amount owed, but those liens expire before the 14 year period expires (I'd venture to say you'd be hard pressed to find anyone that can give a legitimate reason this structure exists). The president's plan would modify the lien period to coincide with the deferral period giving the government possible recourse in the event of a default.