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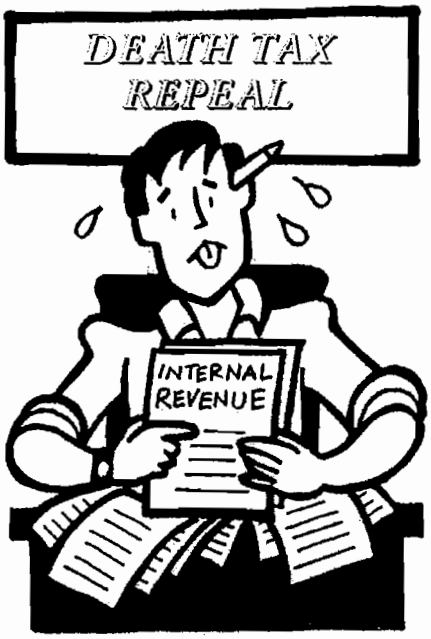

WHAT TO SAY IF YOUR CLIENTS ASK:
"SINCE THE DEATH TAX HAS BEEN REPEALED, WHY DO I NEED ESTATE PLANNING?

WHAT TO SAY IF YOUR CLIENTS ASK:

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by Robert J. Kolasa, Attorney, C.P.A., LL.M. Tax

I. INTRODUCTION

The sky is falling! The sky is falling! With one fell swoop of his pen, on June 7, 2001, President George W. Bush made good his campaign pledge and signed the Economic Growth and Tax Relief Reconciliation Act of 2001 ("2001 Tax Relief Act")[1] which in 2010 completely repeals the Federal estate and generation-skipping transfer taxes. Indeed, the enactment of such legislation is nothing short of revolutionary as dealing with the estate tax (or in adopting the lingo of the day, the "Death Tax"), has long been a central pillar in the estate planner's legal practice.

Undoubtedly, Death Tax repeal has caused more that a few practitioners to worry about their jobs and wear shocked expressions visualizing new careers in other well trodden legal disciplines less subject to legislative fiat. Or in other words, does Death Tax repeal effectively eliminate the trade of estate planners once the words "estate taxes" are taken out of their job description? The answer to this question is a resounding "NO!" Accordingly, the purpose of this article is to outline the new rules wrought by Death Tax repeal and discuss the practical ramifications of such changes to the practicing attorney.

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II. BASIC PROVISIONS OF THE NEW LAW

A. Increased Exclusion Amounts and Reduced Tax Rates

Prior to the 2001 Tax Relief Act, the estate and gift tax rates ranged from 18% on the first $10,000 of cumulative taxable transfers to 55% on transfers more than $3 million. For large estates with cumulative taxable transfers more than $10 million, an extra 5% tax (the "5% surtax") was imposed which had the practical effect of phasing out the benefit of the graduated rates.[2] However, under Section 2010 of the Internal Revenue Code ("Code"), an applicable credit referred to as the "unified credit" effectively exempted from lifetime and testamentary transfers "exclusion amounts" totaling $675,000 in 2001, $700,000 in 2002 and 2003, $850,000 in 2004, $950,000 in 2005, and $1 million in 2006 and thereafter. In 2001, the $675,000 exclusion amount ensured that taxable transfers exceeding such amount would generally be subject to estate and gift tax rates beginning at 37%.

Effective in 2002, the 2001 Tax Relief Act amends Internal Revenue Code Section 2001 to repeal the 5% surtax and impose the following exclusion amounts and tax rates:

Calendar Year	Estate Tax Exclusion Amount	Highest Estate, Gift, & GST Rates
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	Tax Repealed	35%*
*Gift-Tax rate equal to highest individual income-tax rate		

A striking point of the above table is the significant size of the estate tax exclusion amounts. If husband and wife who own joint tenancy assets in the amount of $1.35 million both die in 2001 without planning, the estate tax due upon the surviving spouse's death is $270,750. This is an *avoidable tax* as through proper estate tax planning (typically involving separate trusts with a "Credit Shelter Trust" or "A/B" trusts), estate taxes may be reduced to zero by utilizing the separate estate tax exclusion amounts of both husband and wife. Accordingly, for married couples, the 2001 Tax Relief Act permits the exemption from estate taxes of double estate tax exclusion amounts of $2 million in 2002 and 2003; $3 million in 2004 and 2005; $4 million in 2006, 2007 and 2008; $7 million in 2009 and unlimited amounts in 2010 and thereafter.

However, as any estate planner quickly realizes, some clients for a variety of reasons do not want to engage in planning for estate taxes. They direct the attorney to draft simple wills (i.e., everything goes to the surviving spouse) or tax planning trusts are executed without assets transferred to such trusts, thereby negating the intended tax effects. Or worse, simple wills or unfunded trusts are implemented because attorneys are not aware of a client's exposure to estate taxes or do not possess the technical skills, time or desire to effect a tax avoidance plan. Given the myriad traps for the unwary under the current system of transfer taxation, the repeal of the Death Tax would substantially reduce legal malpractice concerns for many lawyers.

B. Gift Tax Remains with $1 Million Exemption

Significantly, the gift tax is not repealed and the gift tax exclusion amount under Code Section 2505(a) is set at $1 million in 2002 and thereafter for lifetime transfers. This is a fundamental departure from prior law whereby the unified credit could be applied with equal force to both lifetime and testamentary transfers. Thus, if taxable gifts were $1.4 million in 2006, the amount in excess of the $1 million gift tax exclusion amount ($400,000) is subject to gift tax even though the estate tax exclusion amount is then $2 million. Under the vagaries of the new law, the remaining $1 million estate tax exclusion amount ($2 million reduced by $1 million exempt taxable gift) would be applied to the donor's estate upon his or her death.

The good news is that the 2001 Tax Relief Act did not change the rules whereby donors of lifetime gifts are provided an annual exclusion of $10,000 (indexed for inflation, although there has been no inflation increase yet) for

transfers of present interests in property to any donee during the taxable year. If the non-donor spouse consents to split the gifts with the donor spouse, then the annual exclusion is $20,000. Unlimited transfers between citizen spouses are still permitted without imposition of a gift tax as are unlimited gifts for certain educational and medical expenses under Code Section 2503(e).

It is interesting that while the transfer tax on testamentary transfers will expire in 2010 (but see the discussion below related to the "sunset" provision which may reinstate the Death Tax in 2011), the gift tax will remain in full force and effect at a static $1 million exclusion amount. This is one result that the legal profession has only itself to blame. During the legislative period, several widely read articles[3] were published advocating the idea that with no gift tax, high-bracket taxpayers could freely transfer investments to lower income-tax donees. Better yet, without a gift tax why not transfer assets to donees in states with lower or no state income taxes, create trusts in jurisdictions without trust income taxes, or engage in creative transactions to avoid Federal and state income taxes altogether? Congress clearly felt compelled to retain the gift tax to avoid the tax shifting/avoidance planning opportunities a no gift tax environment would have presented.

C. The Insidious Return of Carryover Basis

In 2010, after repeal of the Death Tax, the prior-law rules under Code Section 1014 providing for a fair market value (i.e., "stepped-up") basis for property acquired from a decedent are repealed. Under the "carryover basis" regime of Code Section 1022, property transferred at the decedent's death will generally receive a basis equal to the lesser of:

(1) the decedent's adjusted basis in the assets; or

(2) the date-of-death fair market value of such assets.

However, there are three potential adjustments to basis (1) a $1.3 million basis adjustment (adjusted for inflation) to be added to the carryover basis of assets held at death; (2) a $3 million basis adjustment (adjusted for inflation) to be allocated among the assets passing to a surviving spouse; and (3) a basis adjustment for certain unused built-in losses and loss carryovers. The executor elects which assets will receive the basis increase. Certain assets not eligible for basis step-up are property acquired by gift during the three-year period before death, property constituting a right to receive "income in respect of a decedent" and various foreign investments. In order to soften the

carryover basis regime, after 2009 the pre-death appreciation of property used to satisfy pecuniary bequests no longer triggers income (Code Section 1040) and the $250,000 income tax exclusion for the gain on the sale of a principal residence can be utilized by an heir, the decedent's estate or living trust (Code Section 121(d)).

It is worthy to note that the aforesaid $1.3 million and $3 million basis adjustments result in additional basis to be allocated to assets. This is a liberalization of the Death Tax repeal bill that passed Congress last year and was vetoed by President Clinton (that bill would have only given a step-up for assets worth $1.3 million, or $3 million for spousal transfers).

EXAMPLE #1. The decedent dies in 2011 owning stock worth $7 million and having an adjusted basis of $3.7 million. Such stock passes to Decedent's son. The maximum basis adjustment is $1.3 million and the basis of such stock can be increased to $5 million. If such stock passes to Decedent's spouse, the maximum basis adjustment is $3 million and the stock basis can be increased to $6.7 million.

EXAMPLE #2. Decedent dies in 2011 owning stock worth $9.3 million and having an adjusted basis of $3.7 million. Such stock conceivably could have a cumulative $5.6 million basis adjustment: (i) the $1.3 million adjustment of the first spouse to die; (ii) the $3 million adjustment for assets transferred to a surviving spouse; and (iii) the $1.3 million adjustment of the surviving spouse.

The liability concerns of the executor (or trustee in possession of assets) adjusting basis can be problematic if total basis adjustments do not give non-cash assets a full basis "step up." It's logical to presume that basis increases should be added to those assets that are identified as likely to be sold (or subject to depreciation recapture) to avoid the payment of future income taxes. However, how can such allocation be rationally made if the assets are fragmented among multiple beneficiaries with competing interests? It would seem imperative that the underlying estate planning documents should either direct specific basis adjustments or contain broad exculpatory language to protect the executor from the criticism of unhappy beneficiaries not blessed with full basis step-up. Luckily, the $1.3 and $3 million limits will provide a complete basis step-up for most clients, leaving the prospects of litigation for fiduciaries of larger estates who can afford to fight recalcitrant beneficiaries in court. Further, for those of us who prepare estate tax returns (Form 706) and bemoan Death Tax repeal for the "loss" of future compliance

revenues, all is not lost as the Code Section 6018 carryover information reporting requirements are substantial (including value, basis, holding period and characterization), along with a $10,000 noncompliance penalty under Code Section 6716.

The $64,000 question is whether the modified carryover basis regime will actually be retained and not changed by future legislation. Many pundits are predicting that such rules will be repealed before 2010. In 1976 Congress enacted a carryover basis regime which was quickly repealed before it became effective. The perennial objections to carryover basis are complexity and that many clients just do not know the adjusted basis of their assets (and thus death, with its "step-up" regimen solves the problem). However, the soundness of this argument is somewhat flawed in that information technology has made basis tracking (at least for publicly traded investments) a much more attainable goal. IRS audits involving the determination of basis are quite rare and it would be hoped that if the carryover basis rules are retained, the IRS will be equally complacent. In any event, the tax practitioner should probably consider advising clients to retain all records of their bases in assets, including distinguishing between improvements that add to basis and repairs and other expenditures which do not.

D. The "Sunset Provisions" OR Is it Back to Traditional Estate Tax Planning in 2011?

Amazingly, news of the Death Tax repeal in 2010 may be greatly exaggerated since in order to meet arcane Congressional budget rules, the Senate and House conferees added "sunset provisions" officially causing the entire legislation enacted by the 2001 Tax Relief Act to expire in 2011 (with the pre-enactment laws to be reinstated in such year).[4] Seemingly, Congress is repealing Death Tax for 2010 and reinstating it for the year 2011. There are current legislative efforts underway to revoke this ridiculous takeaway [5], although given the current control of the Senate by the Democratic party, the repeal of the sunset provisions may be politically premature. Many commentators insist that given the history of the beast it will be impossible for Congress to avoid tinkering with the sunset provisions before 2010. There's been about three major tax acts per decade and it appears unrealistic to presume that Congress will "do nothing" and let the sunset provisions take effect. Since new laws can extend the sunset provisions an additional 10 years, it is even possible that in 2005 or 2006 a new tax act will delay the effective reinstatement of estate taxes to 2015 or 2016.

This author believes that Death Tax repeal will be allowed to stand and that effective in 2010 and subsequent years such tax will cease to exist. It seems that most estate planning attorneys wrongly proclaimed that Death Tax repeal would never occur by vastly underestimating the strong political will for repeal and the corresponding scant political opposition thereto. On the other hand, the permanency of the repeal is grounded on the presumption of government surpluses, economic growth and the will of future Congresses and Presidents to spend the very considerable sums necessary to reduce the estate tax to zero. Even if Congress feels compelled to retain the Death Tax, in such event it is predicted that the 2009 estate tax exclusion amount of $3.5 million will be allowed to stand and the Death Tax would then only apply to the very largest estates (i.e., $3.5 million for single persons; $7 million for married couples - or much, much more with aggressive planning).

E. Other Notable Changes

In the spirit of brevity, the other significant changes to transfer taxes wrought by the 2001 Tax Relief Act are as follows:

1. Generation Skipping Transfer Tax Repeal in 2010 and Transitional Relief. The 2001 Tax Relief Act repeals the 55% generation-skipping transfer tax ("GST") in 2010. This separate tax (in *addition* to the estate tax) is generally imposed for direct or indirect transfers to a "skip person" - such as a grandchild or unrelated person 37 ½ years younger than the donor, exceeding an inflation indexed $1 million exemption. Tentative repeal of the GST is welcomed as it is a technically complex, confiscatory tax which presents a significant trap for the uninformed. For 2002 and 2003, the GST exemption is $1,060,000 (plus inflation adjustment, if any) and in years 2004 through 2009, the GST exemption equals the increased estate tax exclusion amount. Various helpful technical amendments were also made to Code Sections 6632 and 6642 affecting the allocation of the GST exemption, severing of trusts and valuation rules.

2. The Rape of the States - Or How do you Spell Illinois Inheritance Tax Reenactment? The majority of states (including Illinois) have a "pick-up" estate tax whereby such states "share" in Federal revenues by receiving a State death credit (under Code Section 2011) in the computation of estate taxes payable. In an unfair sleight of hand to save Federal tax dollars, under the new law such credit is reduced in yearly 25% increments beginning in 2002 and completely repealed in 2005. That Washington's sharing of estate tax revenues with the states ends in 2005, well before the Federal Death Tax

repeal (2010, or later?) has angered many states legislators who now face a much earlier loss of tax revenues than their Federal counterparts. It is noted that Illinois' 1999 collection from estate taxes was $347 million, approximately 2% of its total state revenues.[6] Will Illinois reinstate its prior law inheritance tax (not based on the Federal calculation of estate taxes) to make up this lost revenue? Like the repeal of the Federal Death Tax, it's probably too early to tell. At the very least, its safe to say that the minority of states which maintain a separate inheritance tax system will continue to do so and the majority of states put out of the estate tax collection business will struggle to replace lost revenues. Attorneys should continue to give close attention to tax apportionment clauses in wills and trusts relating to state inheritance taxes

3. Repeal of the Qualified Family Owned Business Deduction ("QFOBI"). This deduction under Code Section 2057 for certain qualified family-owned businesses is repealed for decedents dying after 2003, although the recapture tax for disposition of QFOBI assets within the 10-year recapture period will still apply thereafter. As a practical matter, the repeal is not a big loss as planning to obtain QFOBI status never really became a popular objective for most practitioners and their clients

4. Liberalization of Code Section 6166 Estate Tax Deferral. Under Code Section 6166, the number of partners/shareholders in an entity eligible for 10-year estate tax installment payments is generally increased from 15 to 45.

III. PLANNING UNDER THE NEW LAW

A. Planning Partially Depends on the Planner's and Client's Views as to Whether Death Tax Repeal will be Permanent (Or, Will the Sunset Really Set?)

The truly unsettling aspect of Death Tax repeal is the "sunset" rule (discussed above) reinstating such tax in 2011 based on the law existing prior to enactment. This author believes that Death Tax repeal will actually happen (i.e., the sunset will not set), but admits that the estate tax exclusion amount could be frozen at some fairly high level (i.e., $2 million or $3.5 million), or the effective date of repeal delayed. Planning under such alternative scenarios for wealthy clients becomes problematic at best, if not downright nerve-racking. The estate planner is caught in a "Catch 22" regarding the nature of advice to clients. Why should one advise clients of the new law if such law is only an illusion which will someday disappear? One school of

thought is the "do nothing different" or "business as usual" approach which presumes that the law will revert back to its old form and all the present "tried and true" techniques will be equally available. Unfortunately, such a view is unrealistic and unbending to the probable realty that if not estate tax repeal, estate tax reform will substantially raise the bar and make planning unnecessary for all but the richest of our clients.

The solution may be to plot a middle course and presume that the new rules will be with us for an intermediate horizon such as 5 years. This approach would assume the permanence of the $2 million [2006] exclusion amount and probably dictate "business as usual" for most clients with greater assets or short life expectancies. Disclosing and explaining this time frame would enable clients to accept or reject your assumptions and implicitly determine the degree of sophistication, cost and planning to be taken into account. After all, the estate planner's job is to articulately communicate the current state of the law (however imperfect) and outline relevant choices, with the ultimate decisions to be made by the client.

B. "Brass Tacks" or How the New Law Will Affect Your Practice

Getting away from the philosophical debate of whether Death Tax repeal is illusory, the following are some non-exhaustive practical suggestions and observations on how the 2001 Tax Relief Act will affect your estate planning practice:

1. Inform Clients of the Change in Law. It makes good sense to educate clients and prospects as to the new law by mailing out information handouts, writing articles, conducting seminars and updating information on your web page. Nothing beats a client by client analysis reviewing old plans and determining whether updates should be recommended for simplification, or to reach client objectives. All these techniques and others could be coordinated for maximum effect. The point is that Death Tax repeal presents an unique marketing opportunity to mine your client base.

2. Review Plans to Avoid the "Wrong Tape Measure Trap." The "wrong tape measure trap" generally refers to the fact that the gradually increasing estate tax exclusion amounts (from $675,000 to $3.5 million) may change the distribution of assets in ways not intended by clients. For example, presume husband dies holding a $2 million estate with a trust adopting the typical "A/B" marital bequest formula designed to eliminate or minimize estate tax. If husband dies in 2001, the marital bequest to wife would be $1,325,000 ($2

million less the 2001 exclusion amount of $675,000). If husband dies in 2005, the marital bequest would be $500,000 ($2 million less the 2005 exclusion amount of $1.5 million). If husband dies in 2007, the marital bequest would be zero ($2 million less the 2007 exclusion amount of $2 million). Thus the possible "swing" in marital assets to the surviving wife is from $1,325,000 to zero, depending on when the husband dies. The swing is exacerbated if the wife is not a beneficiary of the residuary trust. It's an understatement to say that such results should be communicated to clients in order to avoid unintended results. Some ways to address this issue at the drafting end would be to: (i) use a "single-fund QTIP" marital trust leaving all trust property solely to the benefit of the surviving spouse; (ii) use a "Clayton QTIP" marital trust which gives the executor or trustee the authority to allocate the portion of the trust for which the marital deduction is not elected to the nonmarital trust; or (iii) leave a set percentage (such as 50%) to the surviving spouse.

3. Consider "Leaving Alone" Many Existing Estate Tax Plans for Now. Couples who have already split their assets between two revocable trusts with the relevant marital bequest formula designed to eliminate or minimize estate taxes can probably be advised not to do anything for a while. Some exceptions to this conclusion which may require immediate corrective actions are where (i) the spouse is not a beneficiary of the residuary trust holding the estate tax exclusion amount (see the above discussion of the "wrong tape measure trap"); (ii) the trust contains a residuary marital formula whereby funding of the estate tax exclusion amount triggers substantial capital gains realization; and (iii) the combined assets of husband and wife do not exceed the current estate tax exclusion amount and in the interest of "simplicity" there is no need to engage in bypass trust planning (with possibly a disclaimer trust inserted [discussed below] as a hedge against estate tax reenactment).

4. Consider Drafting More Disclaimer Trusts. This technique gifts to the surviving spouse the residuary estate, but provides that any property disclaimed by the surviving spouse passes to a "Disclaimer Trust" in which the spouse is a primary beneficiary. Such trust can be a standard bypass or QTIP Trust. Effectively, the disclaimer diverts assets to a separate trust in order to utilize the decedent's estate tax exclusion amount. If the clients are not hung up about the surviving spouse's "control" of trust assets, this technique presents maximum flexibility to the surviving spouse. The downsides are that the surviving spouse may not disclaim in desirable situations, the unavailability of granting the surviving spouse a power of appointment over trust assets and greater creditor exposure for assets not held

in a bypass trust.

5. Consider More Flexibility in Trust Drafting. To hedge against future tax law changes, independent trustees can be granted broad special powers of appointments, trust protectors can be empowered to distribute assets to trust beneficiaries, and independent persons (through the trust instrument or power of attorney) can be given the power to rewrite the trust instrument. All these techniques bear varying risks of litigation if a beneficiary is disenfranchised from trust assets. Further, the new law begets changes of attitude in trust drafting such as: (i) making substantial gifts to children (or transferring all assets to the surviving spouse) upon the death of the first spouse to die; (ii) redrafting marital trusts to sprinkle distributions to non-spouse beneficiaries or distribute income and principal to spouses for limited durations (such as 10 years, or until remarriage); (iii) redrafting residuary and irrevocable trusts to include spouses as beneficiaries; (iv) creating hybrid charitable trusts naming family members and charities as beneficiaries; (v) creating multiple trusts for different asset classes to optimize basis adjustments under the modified carryover basis rules; (vi) drafting alternative distribution provisions utilizing traditional estate planning clauses if death occurs before Death Tax repeal, but leaving all property outright to the surviving spouse if death occurs after Death Tax repeal.

6. Accept the Rise of Joint Tenancy and Joint Trusts. Accept that holding assets in joint tenancy may increase as the need to fund "credit shelter" trusts to utilize the first spouse to die's estate tax exclusion amount will not be present. Some prospects will use estate tax reform as an excuse to further procrastinate their estate plans. This is satisfactory as the increased use of joint tenancy and assets held in the clients' own names (versus trusts) will only add to legal fees for probate and guardianship administration. Further, joint trusts for married couples will become increasingly popular as many of the perceived technical problems relating to such trusts evaporate once Death Tax is repealed, or combined assets are less than the then applicable estate tax exclusion amount.

7. Accept the Demise of Advanced Estate Planning Transactions Effectuated Only to Reduce Estate Taxes. The family limited partnership, grantor retained annuity trusts, private annuities, sales to defective grantor trusts, sale of remainder interests, self-cancelling installment notes and many other irrevocable transfers may be less popular now because of Death Tax repeal. All these transactions generally involve irrevocable transfers and if clients survive to the date of Death Tax repeal, they may resent the disadvantages of

the "unnecessary gifting of assets." This is where client education becomes important - let the client knowingly decide whether to adopt advanced planning techniques in the face of estate tax reform. For middle market clients who most likely will outlive Death Tax repeal (or have assets less than the current estate tax exclusion amounts), such transactions should probably not be done if they do not have true economic motivation apart from estate tax reduction objectives. For instance, a family limited partnership enacted to have senior family members retain control of assets and make current gifts to younger members may be advisable if the senior members truly wish to retain control of the assets. However, for very wealthy clients (more than $10 million) there may be "too much to lose" if Death Tax repeal is reversed and such techniques will probably continue whether or not they are propelled solely for tax avoidance reasons.

8. Don't Pay Gift Taxes. Generally, it doesn't make sense to pay gift taxes by making taxable gifts exceeding the $1 million gift tax exclusion amount. This result is the reverse of the prior system, where paying gift taxes (although rarely done) was arguably preferable to paying estate taxes because of the "tax exclusive" nature of gift taxes. Beware overly aggressive planning techniques which may get zapped on IRS audit and impute taxable gifts to the client.

9. Accept the Demise of Irrevocable Insurance Trusts. Some planners are suggesting that clients who have estate tax problems now (but possibly not in the future if the new law stays in effect) should rush to execute irrevocable life insurance trusts utilizing term insurance as a hedge against the revival of the Death Tax. However, under estate tax reform it seems that the usage of irrevocable insurance trusts to hold life insurance free of estate taxes will decline and trustees will seek various "exit strategies" such as (i) allowing policies to lapse if there are no estate tax liquidity needs; (ii) having "trust protectors" distribute the insurance policy to beneficiaries in order to end trust administration; and (iii) the creation of "new" trusts to purchase insurance policies (for cash value consideration) from "old" insurance trusts in order to effectively change the terms of how the death proceeds should be administered.

10. The Rise or Fall of Lifetime Gifts to Family Members? Why make gifts to family members if gifting to reduce estate taxes is no longer necessary and gifts may preclude some assets from obtaining a "stepped-up" basis? There's no real answer to these queries other than the observation that under estate tax reform clients are more free to retain or gift assets based on their preferences,

rather than on tax law considerations. Income tax considerations will be a more important factor to encourage gifts to donees in lower brackets. Gifts in trust with various "strings" attached (i.e., reversion or forfeiture provisions causing inclusion in the donor's estate) should become more popular as will sale and loan transactions permitting donors to receive economic benefits from transferred assets. Further, gifts in trust to children (rather than outright gifts) may sometimes be preferable if the terms of the trust would enable the child to direct subsequent transfers to his or her beneficiaries without the imposition of gift, estate or GST taxes.

11. The Rise or Fall of Charitable Gifts? Some commentators predict that the new law will not hurt charities in the long run as Death Tax repeal will leave people with more property they can dispose of for charitable purposes. However, it's hard to see how charitable giving will not suffer as estate tax avoidance has constituted the primary motivation for many wealthy clients in making large charitable transfers. Charitable remainder trusts may become more popular, especially since the carryover basis rules will increase the need to dispose of low-basis assets at minimal tax cost. Charitable lead trusts will probably lose some of their appeal in a regimen with no estate taxes to minimize. Further, without the constraint of the estate tax limitations, new types of hybrid foundations and charitable trusts may be designed subject to a less rigorous standard of supervision.

12. The Demise of Generation-Skipping Transfer Tax (GST) Planning? The mathematical sizzle behind GST planning is that an entire level of estate taxes is avoided by the single taxable transfer from grandparent to grandchild (versus the double taxable transfer from grandparent to child and then, upon the child's death, from child to grandchild). As in charitable giving, if the estate tax avoidance motivation is not present, it's questionable whether these transactions will flourish. Of course, dynasty trust creation will continue for the independent economic purpose of preserving family fortunes for many generations, rather than for estate tax reasons.

IV. CONCLUSION

Estate planning will survive the spectacle of Death Tax repeal. Prior to the 2001 Tax Relief Act, the greatest service estate planners achieved was the formulation of a plan directing assets to beneficiaries consistent with client objectives. The avoidance of estate taxes was *not* the primary motivation of planning, and in many cases the existence of such tax had no real significance as it could easily be avoided or minimized. The 2001Tax Relief Act repeals

he Death Tax in 2010, but due to a sunset provision such tax magically eappears in 2011. The uncertainty of whether Death Tax repeal will become ermanent creates many transitional problems for the estate planner in ormulating current strategies for effective tax planning. It is suggested that Death Tax repeal will become a reality in 2010, yet, if this does not happen, state tax reform should still mean a $2 million or $3.5 million estate tax exclusion amount. Whatever the effect of future laws modifying the provisions of the 2001 Tax Relief Act, it is clear that the estate planner is left with more work in sorting out endless possibilities to optimally meet client objectives.

FOOTNOTES:

1. Public Law No. 107-16.

2. Under former Code Section 2001(c)(2), estates from $10,000,000 to $17,184,000 were taxed at 60%, with estates over $17,184,000 effectively subject to a flat 55% rate on all amounts exceeding the exclusion amount, as the benefit of the graduated rates were phased out.

3. For example, see "Wealth Transfer Tax Repeal: Some Thoughts on Policy and Planning", Trusts and Estates, February 2001, Blattmachr and Gains.

4. Section 901 of Public Law No. 107-16 entitled "Sunset Of Provisions of Act." Critics have charged that this provision is accounting chicanery which hides hundreds of billions of dollars from the 10-year Congressional Budget that will actually be lost in 2011, but not taken into account in such budget.

5. H.R. 2143 proposes to make the repeal of the estate tax in 2010 permanent.

6. "States Expecting to Lose Billions From Repeal of U.S. Estate Tax", The New York Times, June 21, 2001, Sack (pages A1 and A20).

Changes in Estate Tax Could Bring About a Bad Heir Day

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