

ESTATE AND GIFT TAX ALERT

FEDERAL ESTATE AND GST TAX TEMPORARILY REPEALED

On January 1, 2010, significant temporary rules regarding the federal estate, gift and generation-skipping transfer (GST) tax laws became effective; they are scheduled to apply through December 31, 2010. Although it is widely anticipated that Congress will act this year to modify these rules, most likely retroactively to some degree, the temporary rules are currently the law. The principal changes embodied in the temporary rules are discussed below.

- The federal estate tax is repealed for death time transfers occurring in 2010. Accordingly, if an individual dies in 2010, his or her entire estate—regardless of its size or the identity of its beneficiaries—will pass free of federal estate tax. Under prior law, this result generally could be achieved only if the entire estate over and above the applicable estate tax exemption amount (\$3.5 million in 2009) passed to a surviving spouse and/or charity.
- The GST tax is repealed for both lifetime and death time transfers occurring in 2010. As a result, all testamentary or lifetime gifts made in 2010 to, or in trust for, or from certain trusts to, grandchildren or more remote descendants will pass free of GST tax. Under prior law, subject to certain exceptions, transfers to grandchildren or more remote descendants that exceeded the applicable GST exemption amount (\$3.5 million in 2009) and transfers from trusts not fully protected by the GST exemption incurred GST tax at the highest federal estate tax rate of 45 percent.
- The income tax basis of property inherited from an individual dying in 2010 will no longer receive a full “step-up” to date-of-death value. Under prior law, if an individual died owning assets with, for instance, a combined cost basis of \$1 million and date-of-death value of \$10 million, the basis in such assets ordinarily would be “stepped up” to \$10 million, and the \$9 million of built-in capital gains at death would not be recognized (and would escape income tax) on a subsequent sale of the stock. Under the temporary rules, inherited property receives, instead, a modified “carry-over” basis, which is generally the decedent’s cost basis plus an aggregate step-up of up to \$1.3 million. There is also an additional step-up of up to \$3 million for property passing outright to (or in an eligible trust for the benefit of) a surviving spouse.

- The top marginal gift tax rate applicable to taxable gifts made in 2010 to persons other than charity or a spouse and that exceed the donor's gift tax exemption is reduced to 35 percent. However, the temporary new rules do not repeal the federal gift tax, and the lifetime exemption from federal gift tax of \$1 million applicable to taxable gifts remains unaltered.

Absent congressional action this year, the federal estate and GST taxes are scheduled to be reinstated in 2011, at which time the exemption from federal estate, gift and GST taxes will be limited to \$1 million, and the highest estate, gift and GST tax rates will increase to 55 percent. In addition, the basis step-up rules will be restored. Although most commentators expect Congress to act this year to provide stability to the estate, gift and GST tax regime, our legislation trackers in Washington, D.C., have had no indication that any such legislative action will be taken in the near term.

Given the general uncertainty of the estate, gift and GST tax laws, we believe this is a critical time to review your estate planning and consider the effects both of the temporary rules as well as of possible future changes to those rules, both prospective and retroactive. Of course, Akin Gump Strauss Hauer & Feld LLP will monitor any proposed legislation and keep you informed of developments in this area on a real-time basis.

CONTACT INFORMATION

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