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Estate Tax Reform Update

It is only 21 months until the federal estate tax is repealed – for one year – and 33 months from reduction of the estate tax exemption and a 22-33% increase in the estate tax rate. Unless Congress takes action soon, planning for most families with assets exceeding \$2 million will continue to be challenging. Below is a brief summary of the current law and a recent update on possible congressional action.¹

Current Law. Currently, every individual may give away up to \$2 million at death (reduced by any taxable gifts made during each person's lifetime) free of federal estate tax (the "**exemption amount**"). For 2009, the exemption amount will increase to \$3.5 million per person (\$7 million per married couple), and the estate tax rate will remain at 45%. In 2010, the estate tax is repealed (suspended) for one year. But, beginning January 1, 2011, the exemption amount is reduced to \$1 million per person (\$2 million per married couple), and the top estate tax rate increases to 55% (with a 10% surtax on estates between \$10 million and \$50 million, bringing the top rate on those estates to 60%).

Congressional Action. On March 12, the Senate Finance Committee (the "**Committee**") heard testimony about alternatives to the estate tax and expressed concern about returning to excessive estate tax rates and imposing estate taxes on family farms and small businesses. The Committee Chairman, Senator Max Baucus (D-Montana), and ranking member, Senator Charles Grassley (R-Iowa), have pledged to pursue estate tax reform as 2010 approaches.

The Senate is also considering the estate tax in debates over the fiscal year 2009 budget. On March 26, an amendment offered by Senator Baucus to the budget resolution passed 99-1; this amendment would make the 2009 estate exemption amount (\$3.5 million per person and \$7 million per married couple) and the top estate tax rate (45%) permanent. Five other amendments offered to revise or repeal the estate tax failed to garner 51 votes. Although Senator Baucus supports a full repeal of the estate tax, he has stated that this amendment reflects the "minimum" estate tax reform acceptable to him, and he is expected to offer a second amendment to increase the exemption amount to \$5 million per person (\$10 million per married couple) and reduce the top estate tax rate to 35%. Senator Grassley specifically noted he also supports a "fiscally appropriate compromise" of higher exemption amounts and lower estate tax rates. The Committee plans another hearing in April, which will focus on the deferral of estate tax for small businesses, farms, and ranches; special use valuations for farms and ranches; reunification of the gift, estate, and GST exemptions; and portability of the exemption amount between spouses (which would allow a surviving spouse to use a deceased spouse's exemption amount).

What will happen? Our crystal ball tells us that Congress will address the estate tax before 2010, and pass some form of compromise legislation involving higher exemption amounts and lower estate tax rates. It appears likely that the exemption amount will be between \$3 million and \$5 million per person (\$6 million and \$10 million per married couple), with a top estate tax rate between 35% and 45%. We will provide further updates if Congress adopts legislation on any of these proposed changes.

¹ This information only applies for estate tax purposes. The lifetime gift tax exemption remains at \$1 million per person and its use during life also counts against the estate tax exemption available at death.

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