

Speculating on the Future of the Federal Estate Tax

What's the future of the federal estate tax? All we know is that no one knows for sure; it's all speculation. So, let's take a look at what could happen. There are five possibilities: (1) Congress could extend current tax law (commonly referred to as the "Bush tax cuts"); (2) Congress could do nothing, essentially turning the calendar back to 2001; (3) Congress could compromise, agreeing on something between the 2001 tax rules and the rules that apply in 2012; (4) Congress could enact new estate tax reform; or (5) Congress could repeal the estate tax altogether.

Note: Only a few of the estate tax laws that are affected are discussed here.

CONGRESS COULD EXTEND CURRENT TAX LAW AGAIN, PROBABLY FOR TWO YEARS

That would mean the top gift and estate tax rate would remain at 35%. The generation-skipping transfer (GST) tax (this is an additional tax that's imposed on transfers to beneficiaries who are two or more generations below you) would also remain at a 35% tax rate. The gift and estate tax exemption (may also be referred to as an exclusion) would remain at \$5,120,000 (plus any adjustment due to inflation) plus any deceased spousal unused exclusion amount (DSUEA).

The DSUEA is the amount of the gift and estate tax exemption that the first spouse to die does not use. This amount can be transferred from the estate of the first spouse to die to the surviving spouse. This is referred to as portability. Portability would remain.

The GST tax exemption of \$5,120,000 plus any adjustment due to inflation would remain. There is no DSUEA for the GST tax (i.e., the GST tax exemption is not portable between spouses).

The smart money is on this possibility. It has been Congress's tendency of late.

CONGRESS COULD DO NOTHING

Congress could allow all or some of the provisions that sunset to expire, reverting to the 2001 tax rules. The top gift and estate tax rate would be 55% with a 5% surtax on estates that exceed \$10 million but do not exceed \$17,184,000. The GST tax rate would also be 55%. The gift and estate tax exemption would be \$1 million. And, the DSUEA would no longer apply. The GST tax exemption would be \$1 million indexed for inflation (estimated so far to be \$1,360,000).

Some analysts have proposed letting the Bush tax cuts expire as part of a plan to balance the budget over time.

CONGRESS COULD COMPROMISE

Congress could pass a compromise bill that would set the top tax rate to 45% and the exemption amount to \$3.5 million. Whether portability would expire or be extended is anyone's guess.

President Obama supports this option. His 2013 budget plan would return the gift and estate tax, and the GST tax, to 2009 levels; the top tax rate would be 45%, the exemptions would be \$3.5 million (but only \$1 million for gift tax purposes), and portability would be made permanent.

CONGRESS COULD ENACT ESTATE TAX REFORM

Many believe that permanent and comprehensive estate tax reform is needed. However, the political landscape is probably not currently amenable to this option. Besides, permanent tax reform does not really mean that it will be permanent (it could, of course, be modified or repealed by future legislation).

CONGRESS COULD REPEAL THE ESTATE TAX ALTOGETHER

The arguments for and against the repeal of the estate tax continue to wash in, like ocean waves. The tide was high for repeal a few years back, but the current economic and fiscal situation may have slowed its momentum, and the tide seems to be ebbing.



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