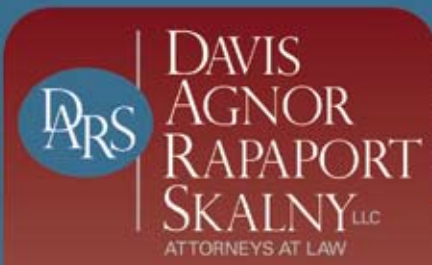


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Federal Estate Tax Reform: Missed Opportunity?

Way back in 2001, the U.S. Senate set into place a conundrum that turned estate tax planning into an oxymoron.

In an attempt to eliminate the Federal Estate Tax, what was then artfully called the “death tax,” the Senate constructed a resolution that would phase out the death tax by 2010. The problem was that there were not enough votes in the Senate to make this resolution a permanent change in law.

As background, in 2001 the Federal Estate Tax was a tax that was to be applied to an individual’s taxable estate that exceeded \$1 million once that law was fully implemented. The Senate, with full approval from the House of Representatives and the White House, was trying to find a way to eliminate the Federal Estate Tax altogether.

The problem was that in order to permanently eliminate a source of revenue such as a tax, Senate rules require a “super majority” of 60 votes. In 2001, the Republicans just did not have the votes. So, a compromise in the form of a resolution was brokered that could be passed by a simple majority of the Senators.

The Senate decided to phase out the death tax over a ten-year period. Starting in 2002, the first \$1 million of an estate could be protected. In 2004, this amount went up to \$1.5 million. Starting in 2006, this protection will apply to \$2 million, with \$3.5 million being protected in 2009.

In 2010, the fun starts; the Federal Estate Tax as we know it disappears. There will be no death tax at the federal level. But, in 2011, this compromise the Senate brokered in 2001 is sunsetted, with the result that the law as it was prior to the compromise comes back into effect. That means that only \$1 million can be protected after 2010.

Now you know how this compromise created a conundrum. How can one possibly do long-term tax planning in this environment of continually shifting sands and uncertainty?

In 2005, all of the questions raised by the 2001 Senate compromise were supposed to be answered. Again, the House of Representatives, with White House approval, passed a law permanently eliminating the Federal Estate Tax. And, again, the Republican Senators were looking for ways to get 60 votes to permanently eliminate the death tax.

New compromises were being discussed. One plan was to raise the size of the estate that could be protected to as high as \$8 million. Another plan was to keep the size of the estate at \$3 million or so, but reduce the rate of the tax from 45% to 15% for any amount over \$3 million. These and other plans were being discussed this past summer.

But then came Katrina. And then Rita. And then the “Scandalgates” of Karl Rove, Senator William Frist and Congressman Tom Delay. And the war Iraq keeps pressing on. And President George Bush’s popularity is heading for an all-time low. And the federal deficit keeps growing and growing. Etc., etc., etc.

You get the picture. Mother Nature, politics and economics are all joining together to put the permanent eradication of the Federal Estate Tax on hold. With the mid-term election coming in 2006, the Republicans are at risk for losing some of their votes in the Senate too, so that any window of opportunity for killing the death tax may have passed.

Of course, this does nothing to end the uncertainty of the original conundrum. History does have a habit of repeating itself.