Judith A. Jarashow
Attorney at Law
60 Walnut Street
Third Floor
Wellesley, Massachusetts 02181

Memo to clients
January, 2010

As you may already be aware, Congress failed to pass tax legislation in 2009 to keep the estate and gift tax law as we have known it in effect. As a result, the federal estate tax is repealed for 2010, and the following rules now apply:

• The gift tax remains in effect, but the tax rate on taxable gifts (those in excess of the $13,000 annual exclusion) is reduced from 45% to 35%.

• The gift tax credit continues to shelter up to $1,000,000 in taxable gifts.

• The generation-skipping transfer tax is repealed for both lifetime transfers and those at death.

• The universal step-up in income tax basis at death no longer applies. Instead, estates will have the ability to allocate $1,300,000 of additional basis to appreciated property generally and $3,000,000 of additional basis to property passing to a surviving spouse. Beneficiaries who inherit appreciated property with appreciation in excess of the available basis allocation amounts will pay capital gains tax when they later sell the property.

Massachusetts is not affected by the failure to address federal estate taxation. There is still currently a $1,000,000 exemption from Massachusetts estate taxes as well as the unlimited marital deduction. Estates in excess of $1,000,000 will be subject to Massachusetts estate tax (if there is no surviving spouse).

Most Congressional watchers expect new (and hopefully permanent) federal estate and gift tax legislation in 2010, possibly with retroactive application, the constitutionality of which is almost certain to be challenged in the courts. Failure to pass legislation this year will result in a return to pre-2001 law, with estate tax imposed on estates over $1,000,000 in value and a top tax rate of 55%.

There may be uncertainty about how the provisions of your estate planning documents will be interpreted if there is no federal estate tax. This is because several provisions of your documents are phrased in terms of tax concepts, such as the estate tax exemption amount (also known as the unified credit) and the marital deduction (if applicable). Because those tax concepts are not in the law at present, there may be some question as to what your documents

mean and how your property will be disposed of. It is essential that you have your documents checked to make sure that they say what you want them to. There may be very unpleasant and unintended consequences depending on when you die, that bear no relationship to how you had hoped to dispose of your assets.

For example, you may have given the “maximum amount that can pass tax-free to my children after taking into account all applicable federal credits and deductions”. If you die in 2010 and if there is no retroactive legislation to correct the current impasse, then all your assets will pass to your children and nothing to your surviving spouse, because the maximum amount that you can give tax free is unlimited in 2010. If you are married this is undoubtedly not what your intended.

If you are interested in making substantial gifts, there may be opportunities available now that will not exist if new legislation passes. As noted, there is currently no federal estate tax or generation skipping tax in 2010. The exemption for gift tax purposes remains at $1 million throughout 2010. Gifts in excess of $1 million are taxed at 35% (instead of 45%). There is some chance that taxable gifts made before the enactment of new legislations will be taxed at 35% and not 45%. In addition, transfers to generation skipping trusts may be "grandfathered". Depending on your risk tolerance, you may want to evaluate whether to make taxable gifts before the law changes.

If you have questions about the existing law and how it may affect you, please feel free to contact me.

Yours truly,

Judith A. Jarashow