

ESTATE PLANNING
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FEDERAL ESTATE TAXES

The current federal estate tax system is set to expire on December 31, 2009, and be replaced by a capital gain tax system (called carryover basis) the next day on January 1, 2010. The capital tax gain system is set to expire one year later on December 31, 2010, and be replaced by a new federal estate tax system identical to the system in place at the end of the year 2000. The exemption is scheduled to be \$1 million¹ in 2011, down from the current \$3.5 million.

Thus, the taxation of donative asset transfers is scheduled to be radically different in 2010 and 2011. It is fair to say there is a consensus that this uncertainty and complexity is unsatisfactory and legislation should be enacted clearing up the uncertainty.

Several weeks ago, the House of Representatives passed a bill (HR 4154) which permanently extends the current federal estate tax system and the \$3.5 million exemption. This was a partisan vote with most Democrats in favor and all Republicans against.

The Senate is deadlocked on the issue. Democrats want the \$3.5 million exemption. Republicans and several key Democrats want more, basically a \$5 million exemption and a lower rate. The Senate is currently tied up debating health care reform.

It is very possible the Senate will run out of time to pass an estate tax bill this year. If that happens, we will start 2010 with no federal estate tax and a new capital gain tax.

If the federal estate tax expires, it is possible that Congress will enact federal estate tax legislation in 2010. If it does, there may be a gap between January 1, 2010, and the date of the new legislation. Or, Congress may make any new legislation retroactive to January 1, 2010. But, the issue of retroactivity will surely end up in the United States Supreme Court. Making a new tax system retroactive would be very controversial.

¹The exemption was \$675,000 in 2000, but was scheduled to increase to \$1 million. That is why the exemption will be \$1 million.

WISCONSIN ESTATE TAX

Wisconsin has no estate tax at this time. It expired at the end of 2007. If Congress does nothing and the new system described above for 2011 comes into existence, Wisconsin will have a new estate tax identical to the tax at the end of 2000. The tax then was referred to as a “pickup tax.”

ROTH CONVERSIONS

In 2010, the income limit for converting taxable IRAs to Roth IRAs is lifted. There will be no limit for such conversions.

Roth IRAs have some advantages for estate planning.

Converting a taxable IRA to a Roth IRA incurs income taxes. Unfortunately, Wisconsin has not lifted the income limit for conversions. Thus, if a taxable IRA is converted in 2010, Wisconsin will charge a 2% penalty for an excess conversion in addition to the income tax. Attempts will be made to change the Wisconsin law so it conforms to the federal law.