

## *Q Do I still need my life insurance policy now that estate taxes have been repealed?*

Life insurance serves many purposes besides creating liquidity to pay estate taxes. The policy may be used to create a cash fund for emergencies, maintain the survivor's standard of living, or fulfill other family goals, such as college for your grandchildren. Keep in mind that after one year of full repeal, the estate and gift tax system is scheduled to return on 1/1/2011 in the form that existed prior to the Act of 2001. Also, as States lose estate tax revenue they may very well choose to adopt new laws taxing transfers at death, either as State estate taxes or State inheritance taxes.

## *Q Do I need to have my estate plan reviewed?*

Every estate plan should be reviewed on a regular basis. Certainly, with the sweeping changes made by the Act of 2001, it would be wise to assemble your financial advisor, your attorney and your accountant to review your situation and how you are affected by the Act of 2001. For example, changes in the Act of 2001 can create situations where current estate plans that fund the credit shelter trust and use a tax formula tied to the pre-Act law may now largely "disinherit" the surviving spouse from your estate. You want to plan now so you don't inadvertently "disinherit" your spouse or pay more taxes, either estate, income or capital gains, than you have to.

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*Under the Economic Growth and Tax Relief Reconciliation Act of 2001, numerous changes to the federal estate and gift taxes are scheduled to take effect between 2002 and 2010. These include repeal of the estate tax for the year 2010, although gift taxes on lifetime transfers would continue in effect. Current (meaning year 2001) estate and gift tax law would be reinstated for year 2011 and thereafter. Therefore, the Act provides several years of lower rates and higher exemptions followed by one year of repeal for 2010. The Equitable Life Assurance Society of the United States does not provide legal or tax advice. You should consult your tax advisor regarding the possible application of this recent legislation to your situation before implementing any estate and gift tax planning techniques.*

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# Estate Planning and the Tax Act of 2001

**T**he Economic Growth and Tax Relief Reconciliation Act of 2001 (Act of 2001) was signed into law on June 7, 2001 by President Bush. The Act touched many different areas of taxation and raises as many questions as it has answers. The following are some questions that you may have on how the Act of 2001 affects your individual estate plan.

## **Q** *What changes does the Act of 2001 make to the estate tax area?*

The Tax Act of 2001 increases the unified credit that is available to reduce the estate tax liability at death during the years 2002 through 2009. In 2010, the estate and generation skipping transfer taxes are completely repealed, but on January 1, 2011, both systems will revert back to the law prior to the Act of 2001 under the “sunset” provisions. During 2010, property will pass under a modified carry-over basis system. A married individual’s estate may be able to increase basis on property included in the estate by as much as \$4.3 million if assets are properly arranged. This means that, unlike current law which passes most property with a full step-up in basis equal to the value at death, the heir may now receive the property with the decedent’s basis or the fair market value, **whichever is lower**. This means that the heir may recognize capital gains when they sell the property in the future if there was any appreciation in value. Consequently, although the estate will not need to pay estate taxes, the heirs may need to pay capital gain taxes at the time they dispose of the property. Again, this provision is scheduled to “sunset” on 1/1/2011. The income tax treatment of estate assets such as pensions and the gain in annuity contracts remains unchanged.

## **Q** *Will my estate still get a credit for any inheritance or estate taxes paid to the State?*

Under the Act of 2001 the credit for State death taxes reduces gradually over the period 2002–2004. In 2005, the credit is replaced with a deduction for any death taxes actually paid to the State. This would have the effect of increasing payments for federal transfer taxes because of the different value of deductions and credits in our tax system. Also, many States impose an estate or inheritance tax equal to the federal credit. These States could lose substantial revenue when this credit is repealed in 2005. States

may very well choose to impose their own death tax in addition to the payment of federal estate taxes. This may also have the effect of increasing the total amount of death taxes that would be paid.

## **Q** *Am I still subject to estate and gift taxes during the phase-in?*

Yes, those systems will continue to exist during the phase-in between years 2002 and 2009, but the highest tax rates will be reduced and you will be able to pass larger amounts of property at death without taxation. For example:

Estate Tax			
Year	Unified Credit	Applicable Exclusion Amount	Maximum Tax Rate
2002	\$345,800	\$1,000,000	50%
2003	\$345,800	\$1,000,000	49%
2004	\$555,800	\$1,500,000	48%
2005	\$555,800	\$1,500,000	47%
2006	\$780,800	\$2,000,000	46%
2007	\$780,800	\$2,000,000	45%
2008	\$780,800	\$2,000,000	45%
2009	\$1,455,800	\$3,500,000	45%
2010	Estate Tax Repeal		
2011	\$345,800	\$1,000,000	55%

On January 1, 2010, the estate and generation skipping transfer tax systems will be repealed for one year until December 31, 2010. The gift tax system will remain for lifetime transfers, and on January 1, 2010, the maximum gift tax rate will equal the high-

est income tax rate which is projected to be 35% at that time. On January 1, 2011, under the “sunset” provision all three systems will revert back to the law prior to the Act of 2001.

## **Q** *I keep reading about “sunset” provisions. Exactly what does “sunset” mean?*

The “sunset” provision contained in the Act of 2001 has the effect that on January 1, 2011, the tax system, including the gift, estate and generation skipping transfer tax provisions, will revert to the system we had prior to enactment. Back to a system that was most likely in place when you chose your planning strategy. So, a full repeal of the estate and generation skipping transfer taxes is short lived in the current law. For one year only, to be precise. The “sunset” provision builds in a certain amount of uncertainty and speculation as to what may occur when or if the “sunset” provisions go into effect on January 1, 2011.

## **Q** *Should I continue to do estate planning?*

Yes, estate tax planning is only one aspect of estate planning. The most important aspect of estate planning is outlining your wishes prior to your death. Estate planning allows you to arrange the distribution of your assets so the property that you would like goes to whom you would like when you would like. Estate planning is not only about taxes and expenses, it can provide sound judgment while you are alive to ease the burden on those who survive you; so it is for everyone who will be survived by a loved one. Now more than ever your estate planning strategy must not only be developed, but must be reviewed on a consistent basis. The changes built into the Act of 2001 and its possible repeal when the “sunset” provision goes into effect on 1/1/2011 create an environment where continuing review is a necessity.