

*The following is a brief summary of the new tax laws. It is important as advisors that we become familiar with these new changes*

## **WASHINGTON HOTLINE**

*-Economic Growth and Tax*

*Relief Reconciliation Act of 2001-*



On Saturday, May 26, 2001, the House and Senate passed the Economic Growth and Tax Relief Reconciliation Act of 2001. On Friday, Senators Charles Grassley (R-IA), Max Baucus (D-MT), John Breaux (D-LA) and Rep. Bill Thomas (R-CA) finalized the provisions of EGTRRA 2001. The largest tax reduction in two decades was welcomed by the President. He noted, "American taxpayers will have more money in their pockets to save and invest and the economy will receive a well-deserved shot in the arm."

The EGTRRA 2001 will reduce income tax brackets, repeal the estate tax by 2010, eliminate the marriage penalty, increase the child credit, increase IRA contribution limits and send rebates this summer of \$300, \$500 or \$600 to taxpayers. There was bipartisan support for the bill in Congress. The House passed the bill 240-154, with 28 Democrats joining the Republican supporters of tax reform. Interestingly, the Senate bill received approval from Sen. James Jeffords, who now is an Independent from Vermont, while Sen. John McCain of Arizona, who campaigned last year as a "Reagan Republican," voted against the tax bill.

*"Smoke and Mirrors" Estate Tax Repeal?*

*Will the estate tax actually be repealed in 2010?*

Inevitably, the tax process produces a compromise between the parties. The Democratic preference for estate tax reform was to expand the exemption equivalent to \$3.5 million. The tradeoff for this expanded exemption was less income tax rate reduction.

The Republican desire was for complete estate tax repeal, with a rapid reduction in the top estate tax rate. However, the funds available for estate tax reform or repeal were not sufficient to repeal the estate tax immediately or even to have a rapid phase-in of reduced rates.

The compromise result and the Joint Committee on Taxation budget cost estimates are described in the following chart. Since estate taxes are paid nine months after death, there is a delay of about one year in an estate tax change and the budget cost.

*Year Estate/GSTT Exemption Top Estate Rate Budget Cost*

2002	\$1 million	50%	\$0.1 Billion
2003	\$1 million	49%	\$7 Billion
2004	\$1.5 million	48%	\$6 Billion
2005	\$1.5 million	47%	\$8 Billion
2006	\$2 million	46%	\$5 Billion
2007	\$2 million	45%	\$10 Billion
2008	\$2 million	45%	\$12 Billion
2009	\$3.5 million	45%	\$13 Billion
2010	Estate/GSTT Tax repealed	35% (Gift tax)	\$24 Billion
2011	Estate/GSTT Tax repealed	35% (Gift tax)	\$54 Billion

EGTRRA 2001 clearly did change the estate tax picture. The increased exemptions will mean reduced tax rates for all except the very largest estates. Indeed, zero estate tax plans for 99.9% of all Americans are now possible.

*Will the tax actually be repealed in the year 2010? Or, to paraphrase Mark Twain, is the death of the "Death Tax" greatly exaggerated?*

*-The fundamental problem with the proposed repeal structure is twofold:*

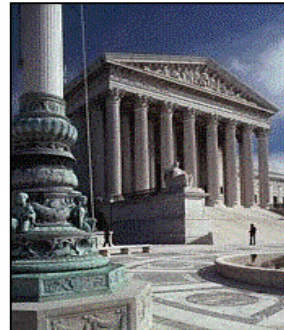
*First*, by 2009, with a \$3.5 million exemption per person, the estate tax will only apply to the very largest estates. This will be true even if there is substantial increase in the size of the estates of affluent Americans. Therefore, full estate tax repeal in 2010

would open the gates for political class warfare by those who prefer income tax reductions for the middle class.

[Second](#), repealing the estate tax at that time will involve a substantial tax cost. In addition, 2010 is the year when the first wave of the "baby boomer" generation reaches age 65 and starts to retire. This massive retirement group will require substantial expenditures for Social Security and Medicare programs. Thus, if the funding to repeal the estate tax cannot be located today, it seems unlikely that a large allocation of funds to repeal the estate tax will be available in the year 2010.

[Consider the political mathematics.](#) The income tax reductions in 2010 will cost about \$100 Billion per year and a Senator or Representative might note that all his or her taxpaying constituents benefit from those reductions. On the other hand, the estate tax repeal will cost \$50 Billion plus per year and will in 2010 benefit about one of every five hundred voters.

[If there are not sufficient funds to do both, will the Member of Congress choose income tax reductions or estate tax repeal?](#)



Politically, it will be difficult to freeze the estate tax repeal. However, it will be politically very easy to phase in the repeal again over the years 2010 to 2020. Considering the mathematics and political realities, there seems to be at least an even likelihood that estate tax repeal is still a very long distance in the future. The estate tax battle will continue for the next decade.

In the meantime, professional advisors will need to assist their clients in planning based on a two to five year timeframe. With the continued controversy over the entire transfer tax system, it seems imprudent to plan with a timeframe much longer than five years.

Editor's Note: Because of the importance to all professionals of the planning changes in EGTRRA 2001, GiftLaw is publishing this Special Report on the largest tax cut in the past two decades. Economic Growth and Tax Relief Reconciliation Act of 2001 The Joint Committee on Taxation (JCT) Summary Report on the proposed provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 has been released. House and Senate negotiators, led by Sen. Charles Grassley (R-IA), Sen. Max Baucus (D-MT), Sen. John Breaux (D-LA) and Rep. Bill Thomas (R-CA) have announced a compromise plan that reaches the Congressional Conference budget targets.

EGTRRA 2001 is scheduled to include \$1.25 trillion in tax relief over ten years plus \$100 billion in stimulus for 2001. EGTRRA 2001 includes seven major sections. These sections cover the [income tax brackets](#), the [child tax credit](#), [marriage penalty relief](#), [education incentives](#), [estate tax repeal](#), [pension and retirement enhancements](#), and the [alternative minimum tax](#).