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LITIGATION AND VALUATION ADVISER

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What is the Fate of the Estate Tax?

There has been much speculation about permanent estate tax legislation – but no hard news as to what will happen. If no permanent estate tax legislation occurs this year, a bill will be passed to extend 2009 rules into 2010; thereby capping the estate tax rate at 45% and keeping the exemption at the current $3.5 million per person.

The fear is that if no legislation passes in 2010, the existing estate tax law will sunset and in 2011 the estate tax will be set at a brutal 55% rate with a paltry $1 million exemption.

Recently-released 2010 budget proposals by the Obama Administration addressed GRATS and valuation discounts.

GRATS

Grantor Retain Annuity Trusts, (GRATS) are a common means of wealth transfer, especially in this environment of low interest rates. The Treasury proposed to restrict the use of GRATS by imposing a 10-year minimum term.

Valuation Discounts

Congress attempted to restrict valuation discounts and "estate freeze" planning in the early 1990s, but the tax courts allowed discounts for a variety of reasons. There is significant case law that supports discounts, especially for minority interests in privately held (non-marketable) companies.

While pundits believe that the ultra-restrictive Pomeroy bill (H.R. 4242) is dead, another bill (H.R. 436) has been introduced in Congress that would incorporate some of the Congressional Joint Committee of Taxation's recommendations. Among other things, H.R. 436 also would impose two significant limitations on the availability of valuation discounts for transfer tax purposes:

- ***Nonbusiness assets.*** The act generally would disallow valuation discounts for transfers of family limited partnership interests and other non-actively-traded interests to the extent the entity owns "nonbusiness assets," such as marketable securities. Nonbusiness assets held by the entity would be valued as if the transferor transferred those assets directly to the transferee. In addition, no discounts would be allowed in valuing a non-business asset that consists of a 10%-or-more interest in another entity.

- ***Aggregation***. The act would prohibit minority interest valuation discounts for transfers of family limited partnership interests and other non-actively-traded interests if the transferee and certain family members control the entity.

Discount Restriction Issues

We foresee a string of court cases in order to properly address the grey areas related to these restrictions:

- Will marketable securities be considered nonbusiness assets if they are actively traded?
- How will the terms of a highly restrictive partnership agreement affect marketability in this new environment?

For more information about this and other issues related to estate tax legislation, contact Senior Manager Christina Yaccarino at (631) 719-3456 or CYaccarino@hrrllp.com.

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