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CLIENT MEMORANDUM
June, 2001
New Tax Law

Congress has passed a new tax bill called the "Economic Growth and Tax Relief Reconciliation Act of 2001" (EGTRRA) which has been signed into law by President Bush.

A. INCOME TAX PROVISIONS

1. The 15% Income Tax rate is reduced to 10% on the first \$6,000 of income for each single taxpayer, on the first \$12,000 for married taxpayers, effective for 2001. Accordingly, the tax reduction is 5% of \$6,000, or \$300, for single taxpayers (\$600 for married couples), and this amount is expected to be "rebated" to taxpayers before October 1, 2001.

2. The maximum Income Tax rate, currently 39.6%, is reduced to 38.6% for 2001; 37.6% in 2004; and 35% in 2006. The 28% bracket becomes 27% in 2001; 26% in 2004; and 25% in 2006. Other brackets are similarly reduced.

3. The disallowance of itemized deductions and of personal exemptions for high income taxpayers will be phased out; but this phaseout does not start until 2006.

B. ESTATE AND GIFT TAX PROVISIONS

1. Under current law, the Estate Tax exemption is \$675,000, and the maximum Estate Tax rate is 55%. Following is how the exemption will be increased, and the maximum rate decreased, over the next 9 years.

YEAR	ESTATE TAX EXEMPTION	MAXIMUM RATE
2001	\$ 675,000	55%
2002	\$1,000,000	50%
2003	\$1,000,000	49%
2004	\$1,500,000	48%
2005	\$1,500,000	47%
2006	\$2,000,000	46%
2007	\$2,000,000	45%
2008	\$2,000,000	45%
2009	\$3,500,000	45%
2010	Estate Tax is repealed	
2011	The Repeal Provisions will expire; and the old law (as in 2001) regarding Estate Tax will be reinstated, except that the exemption will then be \$1,000,000.	

2. The Gift Tax is not repealed. The gift tax exclusion will increase to \$1M in 2002, and stay there. The apparent reasoning is that Congress wanted to prevent income tax avoidance which might have been accomplished by transfers of income-producing assets from a high bracket taxpayer to another family member who may be in a low income tax bracket.

3. Currently, heirs are given a "step-up in cost basis" to the date-of-death value, which allows heirs to avoid income tax on the decedent's

lifetime capital gains. In 2010, when the Estate Tax has ended, property acquired from a decedent will no longer receive a step-up in basis, except on the first \$1,300,000 plus an additional \$3,000,000 for assets passing to the spouse. This is, in essence, a complicated provision, which means that in 2010, heirs will ultimately pay income taxes on capital gains which occurred before the decedent's death. This provision also "sunset" (that is, expires) in 2011.

SUMMARY

Regarding the new law on Estate and Gift Taxes, there appears to still be much uncertainty at least in the long term. The exemption increases from \$675,000 to \$1,000,000 next year and gradually to \$3,500,000 in 2009. And, the rate drops gradually from the current maximum of 55% to 45% by 2009. The Estate Tax is repealed during the year 2010, but only for that 1 year(!). In that same year, inherited assets will be deemed to have the same "purchase price" in the hands of the heirs as in the decedent, meaning that the heirs would essentially inherit capital gains tax liabilities. The Repeal will then expire (that is, "sunset") at the end of 2010; and the old law (that is, the law now in effect in 2001) will be reinstated in 2011. Will Congress and the President act between now and 2011, to make any of the changes permanent? No one has an answer to that question.

For the most part, the Will/Trust that you may have prepared under current law is still appropriate, at least for the balance of 2001. If your estate is in the range of \$675,000-\$1,000,000, the By-Pass Trust in your Will will become less necessary (in 2002) from the standpoint of Estate Taxes, but Trust planning is still appropriate for other asset protection reasons. We will be following-up with another Client Memorandum in a few months, to review what changes, if any, to your Will might be appropriate in light of the new law.