

No Quick Death For The Estate Tax

Janet Novack 06.07.06, 6:00 AM ET

WASHINGTON, D.C. - As Mark Twain might say, reports of the death of the death tax are greatly exaggerated.

U.S. Senate Majority leader Bill Frist (R-Tenn.) has promised a vote this week on the repeal of the estate tax approved by the House back in April 2005. (H.R. 8). Yet if this bill passes--considered unlikely even by repeal advocates, since it needs 60 votes to overcome a Democratic filibuster--the death tax wouldn't actually disappear until the start of 2010. That's one presidential and two congressional elections away.

What's more, President [George W. Bush](#)'s signature income tax cuts are all due to expire at the end of 2010, and the bills for Baby Boomers' retirement will start coming due about then--setting the stage for the possibility of major tax overhaul in 2009, under a different president, and before the estate tax actually expires.

"Given the budget issues and the competing tax cuts, it's hard to say it's over. The fat lady never really sings in tax policy," says Yale law professor Michael J. Graetz, co-author of the 2005 book *Death by a Thousand Cuts: The Fight Over Taxing Inherited Wealth*.

That's not to say that this week's action isn't important, as the outside money being poured into advertisements featuring tacky Paris Hilton impersonations (against repeal) and exaggerated claims of decimated family businesses (pro-repeal) attest. "If you do get 60 votes for repeal this year, it's going to be hard to bring the estate tax back in 2009. But if [repeal advocates] fail this time, then everything is on the table in 2009," says Graetz, a top Treasury tax policy official from 1990 to 1992.

Tellingly, opponents of repeal are against any repeal "compromise" that might pass both houses of Congress now; they figure they'll likely be in a stronger position later to retain more of the tax and the revenue it produces. Among those pushing compromise plans are Senate Finance Committee Chairman Charles Grassley (R-Iowa) and Sen. Max Baucus (D-Mont.), the ranking Democrat on the Finance Committee.

Here, it's useful to recap the existing law, as passed in 2001. The estate tax exemption rises through 2009--then, in 2010, the estate tax disappears entirely. But in 2011, it springs back to life in its pre-2001 incarnation.

A person who died last year could pass a total of \$1.5 million to non-spouse, non-charitable heirs free of federal estate tax. (Any amount can be left estate tax-free to a U.S. citizen spouse or to a charity.) This year, the exemption rose to \$2 million per estate, and in 2009 it rises again, to \$3.5 million.

In 2011, the exemption reverts to just \$1 million per estate, and the top rate shoots back up to 60% (including a surcharge), from 45% in 2009.

To add to the confusion, a popular provision in the current law that allows the tax basis of assets to be "stepped up" at death--meaning if heirs sell right away, they owe no capital gains tax--will be eliminated in 2010 along with the tax. It too comes back in 2011.

This cockamamie scheme was adopted as part of budgetary game designed to get President Bush's tax cuts through the Senate while minimizing their supposed costs. And the games continue.

H.R. 8, for example, makes repeal look cheaper (under the rules Congress uses for scoring bills) because it delays any change in the law and then makes the 2010 repeal permanent. So Congress' Joint Committee on Taxation figures the cost to the Treasury at less than \$1 billion for 2007 and \$56 billion in 2012, the first year when its full effects show up in revenues. (The 2012 cost would be even greater if the law didn't get rid of step-ups. But forcing heirs to prove the basis of inherited assets could prove so unpopular that step-ups might be restored, further raising the costs of full repeal.)

So what happens if repeal fails in the Senate this week? Even estate tax backers don't advocate a return to the 2001 law. For example, one of the leading proponents of the tax, William Gates Sr., father of the world's richest man, **Microsoft** (nasdaq: [MSFT](#) - [news](#) - [people](#)) founder **Bill Gates**, says he favors making the 2009 \$3.5 million exemption permanent, with an annual adjustment for inflation. At that level, advocates say, only 3 of every 1,000 estates would owe the tax. Maybe--but that compromise has no chance of clearing Congress while it's still under Republican control.