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AS UNCERTAIN AS THE DAY IS LONG: POSTPONING THE ESTATE TAX SUNSET

*By James P. Lamping, Esq.**

"Knowledge would be fatal. It is the uncertainty that charms one. A mist makes things wonderful." — Oscar Wilde (The Picture of Dorian Gray)

I. INTRODUCTION

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010[1] was passed by Congress on December 16, 2010 and signed into law by President Obama on December 17, 2010. The new law did not permanently address the uncertainty created by the sunset of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA).[2] Instead, it postponed the resolution of that uncertainty.

Many in the estate planning community now believe that an outright repeal of the estate tax, or at least a further extension of the new law, will be forthcoming. However, the conventional wisdom used to be that Congress would certainly act before 2010 to prevent the outright repeal of the estate tax, albeit for just one year. The conventional wisdom was wrong. Now the conventional wisdom is that Congress could not possibly allow the estate tax exemption to revert to $1 million in 2013. Perhaps this time the conventional wisdom will be correct, but then again, perhaps not.[3] The truth is that nobody knows what the law will be in two years. For now, we must be content with uncertainty. This article will examine the new law, as well as explore some of the challenges and opportunities presented by this uncertainty.

II. THE GIFT AND ESTATE TAX

A. The New Law

The new law provides for a $5 million applicable exclusion, with a flat 35 percent rate on the excess, for transfers at death occurring after December 31, 2010.[4] It also reunifies the gift and estate tax credit, which had been separated beginning in 2004, and rates so that the gift tax will have the same $5 million exclusion and 35% rate as the estate tax.[5] However, the higher exemption and lower rate only apply to gifts made after December 31, 2010, and not during 2010.

This would be very useful were it not for the fact that these provisions sunset on December 31, 2012.[6] By postponing the scheduled return of the $1 million exclusion and 55% marginal rates that applied under pre-EGTRRA law from January 1, 2011 to January 1, 2013, Congress arguably has created even more uncertainty in the estate planning arena than has existed over the past several years.

B. Choosing a Marital Deduction Funding Clause

One fundamental objective of marital deduction planning using a pecuniary formula with date of distribution funding is to use the formula that will produce a pecuniary subtrust that is smaller than the residuary subtrust.[7] That is the case because the distribution of appreciated assets in kind to satisfy a pecuniary bequest will result in the imposition of capital gains taxes.[8] Causing the pecuniary subtrust to be less than the residuary subtrust therefore minimizes exposure to capital gains taxes upon funding.[9]

For some estates, it will not matter whether the amount passing free of estate taxes is $1 million or $5 million. For example, a drafter would not alter his or her choice of funding formula for a $1 million estate or a $100 million estate under either scenario.[10] However, many estates in the midrange present a dilemma.[11] For those clients, the change from a $3.5 million exclusion amount in 2009 to the current $5 million exclusion amount may prompt a change in the funding formula. Whether or not that is the case, the prospect of a reversion to a $1 million exclusion amount in 2013 means that those plans should be monitored as the law develops.

One alternative that avoids this dilemma is a fractional share formula clause. Unlike a pecuniary bequest, funding under a fractional share formula generally will not trigger recognition of capital gains.[12] While a fractional share formula may be inconvenient to administer, it may also present the best solution to this conundrum. Of course, this begs the question whether it makes sense to use a bypass trust at all.

C. To Bypass or Not to Bypass?

If one is inclined to believe that the current law will be extended beyond the current sunset, it could be argued that the use of a bypass trust may be counterproductive. Many estates will no longer owe estate tax with the new, higher exclusion amount. However, assets that are transferred to a bypass trust and held in trust at the surviving spouse's death do not receive a new income tax basis at the survivor's death. The loss of the step up in basis will not be offset by a corresponding estate tax savings since an estate tax would not be imposed in any event.

However, there is no guarantee that Congress will act to prevent the sunset of the current provisions. If sunset occurs, a bypass trust makes sense in any estate over $1 million, since the current law provides that – beginning in 2013 – $1 million is the maximum amount that may pass free of estate taxes upon the death of the second spouse.

It should be emphasized that the relevant inquiry is the amount that can pass free of estate taxes upon the death of the second spouse. For example, if a married couple owns $4 million of community property, it may make perfect sense to provide for an outright gift of the deceased spouse's share to the surviving spouse if the unified credit is $5 million. However, if the unified credit has decreased to $1 million by the time of the death of the second spouse, such an outright gift would expose $3 million to estate tax.

A surviving spouse with a disclaimer trust may face an interesting dilemma if Congress has not acted to extend or repeal the sunset before the deadline to make a disclaimer. If the surviving spouse elects to receive assets outright, it is possible that those assets could be later subject to estate tax under a lower exemption amount. Conversely, causing assets to be funded into a bypass trust will cause the loss of the step up in basis. The uncertainty in the law likely means that there is no right answer.

Of course, there remain other reasons to use a bypass trust besides estate tax planning. An irrevocable bypass trust can shelter assets from the surviving spouse's creditors, provide management and protection for the surviving spouse by imposing professional management, and protect the ultimate remainder beneficiaries of the trust (often the first spouse's children from a prior marriage) from the survivor's spending or from diverting the decedent's assets to other beneficiaries.

D. Using the Gift Tax Structure under the New Law

The gift tax regime may present similar challenges. At first blush, a $5 million gift tax credit and a flat 35 percent gift tax rate might seem advantageous; however, "advantageous" is a relative term. If one is inclined to believe that the applicable exclusion amount and rates will remain at least where they are currently, it may make sense to hold assets until death in order to receive the full step up in basis.[13] Conversely, if one is inclined to believe that Congress will allow the current law to sunset at the end of 2012, it may make sense to use the additional $4 million of applicable exclusion amount while it is available. The stakes are even higher if one is deciding whether to pay gift taxes. It is axiomatic that the tax exclusive nature of the gift tax makes it less expensive than the tax inclusive estate tax.[14] That is particularly true when the gift tax rate is relatively low, and estate tax rates may increase if the current law sunsets. By contrast, if the estate tax is repealed outright, any money spent on gift taxes would be wasted.

E. A $5 Million Gift Tax Exclusion Now Means a $5 Million Gift Tax Exclusion

Under the law in effect during 2010, the amount that a person could give without incurring a gift tax may have been something less than $1 million. The gift tax credit under prior law was calculated based upon the tentative gift tax that would otherwise be owed in the absence of the credit.[15] During 2010, the tentative gift tax was lower than in prior years because the gift tax rate was lower. As a result, the available gift tax credit was lower. However, if a person used a portion of his or her gift tax credit in a prior year, when rates were higher, a greater amount of the credit would have been consumed. The net result was that the amount a person could give during his or her lifetime without paying a gift tax may have been something less than $1 million.[16]

The new law makes it clear that the total amount that may be transferred during a person's lifetime is $5 million.[17] In other words, if a person previously made gifts of $1 million, he or she may now give an additional $4 million, regardless of the rates in effect at the time of any previous transfers.

F. Portability and the Inflation Adjustment

The new law includes two provisions that are interesting on paper, but have little practical application in the absence of permanent legislation. First, the new law provides for portability of the estate tax exclusion between spouses.[18] In other words, a surviving spouse may use his or her deceased spouse's unused exclusion amount without creating a bypass trust. This is not the first time that this has been proposed.[19] While portability would fundamentally alter the estate planning landscape, this provision in the new law is only effective until December 31, 2012.[20] Thus portability only exists to the extent that both spouses die during the next two calendar years. Suffice it to say that most estate planners will not take that bet.

Second, the new law contains inflation adjustments for the gift, estate, and GST exemptions.[21] Since the new exemption amounts take effect in 2011 and are scheduled to sunset at the end of 2012, any inflation adjustment could only apply in 2012.

In light of the fact that the portability and inflation adjustment provisions have almost no practical value, it appears that they were designed for the sole purpose of presenting a fait accompli to lawmakers dealing with the next sunset at the end of 2012. For now, they remain an interesting footnote to the new law.

G. Meet the New Law, Same as the Old Law

The new law extends the application of a variety of provisions that had been scheduled to expire at the end of 2010.[22] In particular, the loosening of geographic limitations relating to conservation easements[23] and the expanded availability of provisions relating to the extension of time to pay the estate tax[24] will remain in place until the new law sunsets at the end of 2012. Unfortunately for the State of California, and many other cash strapped states that only have a pick up tax, the replacement of the state death tax credit with a deduction will also continue to apply.[25] As a result, no estate taxes will be paid to the State of California.[26]

A number of generation skipping transfer tax provisions that had been scheduled to sunset also received a reprieve under the new law. Perhaps most significantly, the qualified severance rules will continue to apply.[27] In addition, the application of authority relating to the automatic allocation of GST exemption,[28] retroactive allocation of GST exemption,[29] and substantial compliance rules[30] have also been extended.

H. The Estate Tax in 2010

1. *2010 or 2011 law?*

The new law provides that the new estate tax regime – $5 million exemption and 35% rate – applies to the estates of decedents dying in 2010,[31] unless the executor[32] elects to apply the carryover basis regime instead.[33] In that case, the estate will not be subject to estate tax but also will not receive any basis increase for the decedent's appreciated property, except for the limited $1.3 million basis increase and possible additional $3 million basis increase that is allowed to a surviving spouse.[34]

This may present the executor with an interesting dilemma. Many estate planning documents have been drafted to express the decedent's intent should death occur while no estate tax is in effect. If properly drafted, these provisions would have dealt with a retroactive application of the estate tax. However, these provisions typically do not provide guidance in the event that the executor is required to choose between the carryover basis rules or the imposition of the estate tax. Consequently, there may be an ambiguity in even the best drafted estate planning document.

To compound the problem, beneficiaries with disparate interests may benefit disproportionately from one alternative or the other. For example, suppose that a beneficiary of a large estate is entitled to a specific bequest of a low basis asset, and the document provides that any estate taxes are paid from the residue. The beneficiary of the specific bequest would likely prefer to receive a step up in basis, while the residuary beneficiaries would likely prefer to avoid estate taxes. It is possible that the only viable solution is for the executor to file a petition for instructions and let the beneficiaries fight it out.

Regardless of whether the executor intends to file a petition for instructions, it often will be useful to determine the impact of selecting between the estate tax and carryover basis regimes. The executor may need to prepare both the carryover basis return and the estate tax return, then compare the tax impact under each alternative.[35] This is not a purely quantitative analysis.

A capital gains tax will not be imposed until an asset is sold, whereas the estate tax is imposed almost immediately. In addition, it is possible that a capital gains tax may never be imposed. An asset held until the death of the beneficiary will receive a step up in basis at that point, and may be protected by the beneficiary's estate tax exemption.[36] Conversely, the imposition of an estate tax may be preferable in an estate with low basis assets that will be sold in relatively short order. In very limited circumstances, it may even make sense for an estate that appears to be under the applicable exclusion amount to elect the carryover basis regime.[37] Whatever the facts of the particular case, the point is that this often will not be a black and white issue.

2. Extension of Deadlines Generally

Under ordinary circumstances, an estate tax will be due nine months from the date of death, plus any extensions.[38] Suffice it to say that 2010 was no ordinary year. More than nine months passed between the earliest deaths in 2010 and the enactment of the new law. This means that it would be impossible for many executors to comply with its terms in the absence of special provisions. To address this issue, the new law provides that the due date for the filing of an estate tax return and the payment of estate taxes "shall not be earlier than the date which is nine months after the date of the enactment of this Act."[39] That nine month deadline is September 19, 2011 (nine months after the enactment date of December 17, 2010, extended to September 19 because September 17 and 18 are a weekend). It is notable that nine months is the earliest deadline. Hopefully, a procedure for extensions will be established.

If the beneficiaries of an estate do not agree which regime should be applied, the executor may be in a predicament. The new law provides that the "election shall be made at such time and in such manner as the Secretary of the Treasury or the Secretary's delegate shall provide. Such an election once made shall be revocable only with the consent of the Secretary of the Treasury or the Secretary's delegate."[40] This does not make it clear whether the executor may make a contingent or protective election, pending the outcome of a petition for instructions. If the executor does make the carryover basis election, he or she would then apparently need the permission of the IRS to revoke it. In the absence of any authority on this issue, it seems a fair assumption that the IRS will not readily grant permission to revoke the election if it would result a lower tax bill. Presumably, the executor in this situation will need to pay any estate taxes that would otherwise be due if the carryover basis regime is not elected in order to avoid the imposition of penalties and interest should the election later be revoked.[41]

3. The Extension of the Deadline to Disclaim in Particular

In light of the new GST provisions, disclaimers may be a particularly useful tool to shift assets to younger generations with respect to the estates of decedents dying in 2010. The deadline for making a disclaimer for estate tax purposes is also extended to no earlier than nine months after the effective date of the new law.[42] This should not present a timing problem for California purposes, since a disclaimer need only be made within a "reasonable time" in order to be effective under California law.[43] In addition, a disclaimer that is effective under the Internal Revenue Code will always be effective for purposes of the California Probate Code.[44] In other states with a fixed nine month (or other) disclaimer period, a disclaimer that is allowed to be made later under the new law may be effective for federal tax purposes but not for states tax purposes.

However, a danger lurks just beneath the surface. Prior to the enactment of the new law, the beneficiaries may not have anticipated executing disclaimers. As a result, they may have treated the assets in a manner that now effectively precludes an effective disclaimer, such as accepting the benefits of the assets.[45] In that event, disclaimers may no longer be possible, even though the new law was not if effect at the time the action precluding a disclaimer was taken.[46]

III. THE GENERATION SKIPPING TRANSFER TAX

A. The New Law

As originally enacted, EGTRRA provided that the generation skipping transfer tax would not apply to transfers made during 2010.[47] This created some confusion, as it was unclear whether transfers into generation skipping trusts during 2010 would be forever exempt from generation skipping tax, or whether later transfers out of those trusts after the sunset period ended would be taxable terminations or taxable distributions causing GST tax.

The new law removed at least part of this ambiguity by repealing the provision that the generation skipping transfer tax would not apply in 2010, and providing instead that the tax rate for generation skipping transfers made in 2010 is zero.[48] It therefore is now clear that the "move down" rule[49] applies to 2010 transfers. For example, if a donor makes a gift in 2010 to a trust for grandchildren, the zero GST tax rate will mean that no tax is payable as a result of the initial gift. The move-down rule will cause the donor to be assigned to one generation above the grandchildren, so that the grandchildren are no longer skip persons and distributions to them will not trigger a GST tax. Note, however, that great-grandchildren and younger generations are still skip persons, so the 2010 generation skipping trust is not completely sheltered from GST tax.

For transfers in 2011 and 2012, and for lifetime transfers in 2010, the generation skipping transfer tax exemption will be $5 million, and the tax rate will be 35 percent.[50] However, at least one commentator has observed that a new ambiguity may have been created with respect to the estates of decedents who died in 2010.[51]

B. A Possible Ambiguity

The concern is that, to the extent that the executor elects to apply the carryover basis provisions for a decedent dying in 2010, the $5 million GST exemption arguably may not be available. It seems clear that the decedent will be the transferor for GST purposes, regardless of whether the executor makes the carryover basis election.[52] However, the GST exemption is tied to the estate tax exemption.[53] Since the carryover basis election makes the estate tax provisions (and therefore the estate tax exemption) inapplicable, it could be argued that the GST exemption is inapplicable.[54] This would not present a problem for a direct skip from the estate of a decedent who died in 2010, since the GST rate is zero percent under the new law.[55] However, it could be asserted that taxable distributions and taxable terminations in future years would be wholly unprotected because no GST exemption could be allocated to the assets. For example, if a decedent establishes a trust for a child, with remainder to grandchildren at the child's death, there is no immediate GST tax as a result of the decedent's death, but later vesting of the grandchildren's interests when the child dies will be a taxable termination. If the GST tax is in effect at that time, and the trust has not been protected with an allocation of the decedent's GST exemption at the time of death, then the distributions to the grandchildren will be taxable.

It is more likely that Congress did not intend to make the GST exemption unavailable by rendering inapplicable the estate tax provision which cross references it.[56] For example, the Joint Committee Technical Explanation of the new law specifically states that "[t]he $5 million generation skipping transfer tax exemption is available in 2010 regardless of whether the executor of an estate of a decedent who dies in 2010 makes the election described below to apply the EGTRRA 2010 estate tax rules and section 1022 basis rules [i.e., to be subject to carryover basis and not to estate tax]."[57] That said, the new law is not the model of clarity on this point.

C. Planning for the Future - and the Past

The increased GST exemption presents significant opportunities. For larger estates that most likely will be subject to estate and GST taxes in any event, the ability to transfer $5 million outside of the transfer tax system may be very attractive. This is especially true in light of the reversion to a $1 million GST exemption in 2013. However, opportunities exist even if additional gifts are not contemplated. To the extent that gifts were made in previous years that were not protected by the allocation of GST exemption, the new law permits a late allocation to protect previous transfers.[58] This may be useful to protect assets in trusts with mixed inclusion ratios or which could not be protected due to the lower GST exemption amount at the time a particular transfer was made.

For this reason, it makes sense to evaluate whether a late allocation of GST exemption should be made to transfers that have already been completed. Even if the GST exemption does revert to $1 million in 2013, it is exceedingly unlikely that Congress would attempt to strip GST exemption away from assets to which it has already been allocated. In other words, the increased GST exemption may be a "use it or lose it" proposition.

Conversely, if a direct skip gift was made to a generation skipping trust in 2010, it may be necessary to timely file a gift tax return for 2010 to elect out of the automatic allocation of GST exemption to that gift. The GST automatic allocation rules were reinstated by the new law, effective for 2009.[59] Even though the GST tax rate is zero for 2010, so that no GST tax would be payable even without an allocation of GST exemption to the gift, the law apparently would automatically allocate GST exemption to that direct skip gift, wasting part of the $5 million exemption.

IV. CONCLUSION

As evidenced by the events of recent years, estate planning is an art, not a science. That will continue to be the case for the foreseeable future. There are a number of possible approaches that could be used to deal with the uncertain future of the transfer tax system. Whatever course the practitioner ultimately decides to use, yet another sunset means that clients will need to ensure that their estate plans keep pace with whatever the future holds. Perhaps one day Congress will give us a lasting solution. Until then, uncertainty will remain the rule, and we can only do our best to follow and understand the changing rules.

Sausalito, California

1 Pub.L. No. 111-312 (Dec. 17, 2010). For ease of reference the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 will be referred to as the "new law," or the "2010 Tax Act."

2 Pub.L. No 107-16 (June 7, 2001).

3 It bears more than a passing mention that the debate over the future of the estate tax will occur in the midst of the 2012 presidential election season. In addition, the political climate could change dramatically by then, as two years is an eternity in the political life cycle.

4 2010 Tax Act, *supra*, §§ 302(a)(1) and (a)(2), modifying Internal Revenue Code (IRC), §§ 2010(c) and 2001(c), respectively.

5 2010 Tax Act, *supra*, §§ 301(b), 302(b).

6 2010 Tax Act, *supra*, §§ 101(a), 304.

7 See, e.g., Drafting California Revocable Trusts (Cont.Ed.Bar 4th ed. 2003) § 11.43.

8 Treas. Reg. § 1.661(a)-2(f)(1) and § 1.1014-4(a)(3); Rev. Rul. 56-270, 1956-1 C.B. 325; Rev. Rul. 60-87, 1960-1 C.B. 286; *Kenan v. Comm'r* (2d Cir. 1940) 114 F.2d 217. Capital gains incurred in connection with funding a pecuniary amount is commonly referred to as "Kenan gain."

9 Even assuming that the applicable exclusion amount remains constant, this requires the drafter to anticipate the value of the estate upon the death of the first spouse.

10 If an estate has a value of $1 million, the entire estate may pass free of estate taxes, regardless of whether the applicable exclusion amount is $1 million or $5 million (assuming that none of the applicable exclusion amount was consumed by inter vivos gifts). A pecuniary marital-residual credit formula will therefore minimize exposure to Kenan gain under either scenario. Conversely, the marital share will be the larger portion of a $100 million estate, regardless of whether the applicable exclusion amount is $1 million or $5 million. A pecuniary credit-residual marital formula will therefore minimize exposure to Kenan gain in that case.

11 For example, a $12 million estate could present such a challenge. Assuming that the deceased spouse's half of the estate is valued at $6 million, if the applicable exclusion amount is $1 million, the credit trust would receive $1 million and the marital trust would receive $5 million. By contrast, an applicable exclusion amount of $5 million would mean that the credit trust would receive $5 million and the marital trust would receive $1 million. It should be noted that these examples use the values on the date of death for the sake of simplicity. In reality, a number of other factors (not the least of which are appreciation and depreciation) will impact the actual target amounts. See California Trust Administration (Cont.Ed.Bar 2d ed. 2001) §14.18 et seq.

12 There are no capital gains consequences because the amounts funded into the separate subtrusts are not expressed by reference to a pecuniary amount, and consequently *Kenan* and its related authority does not apply. However, fractional share formulas present their own set of problems. Under a "strict fractional" formula, a fractional share of each and every asset must be funded into

each of the subtrusts, a process which may be arduous to say the least. While a fractional "pick and choose" formula permits non pro rata funding based upon the aggregate value of all assets, it requires that each and every asset be appraised both on the date of death and the date of funding. Again, this can be an arduous process. "Fairly representative" funding produces the same result. For further discussion, see California Trust Administration (Cont.Ed.Bar 2d ed. 2001) §§ 14.29, 14.33.

13 For example, if the applicable exclusion amount remains at $5 million, a $5 million estate would receive no benefit from inter vivos gifting because its assets would not be subject to estate taxes in any event. To make matters worse, the gifted assets would only have a carryover basis, rather than the stepped up basis they would have received if the decedent had owned them at death. IRC, §§ 1014, 1015(a); Treas. Regs. §§ 1.1014-1 - 1.1014.8; 1.1015-1.

14 See, e.g. discussion in LISI Estate Planning Newsletter #1732 (December 15, 2010) at http://www.leimbergservices.com.

15 IRC, § 2505(a).

16 See LISI Estate Planning Newsletter #1704 (September 30, 2010) at http://www.leimbergservices.com

17 2010 Tax Act, *supra*, § 302(d).

18 2010 Tax Act, *supra*, §§ 303.

19 For an excellent discussion regarding the implications of portability under a previous proposal, see Kovar, *Do You Speak "Portability"? Discussing Clients' Estate Plans in a New Language* (Spring, 2009) Trusts and Estates Quarterly Vol. 15, Issue 1, p. 6.

20 2010 Tax Act, *supra*, §§ 101(a), 304.

21 2010 Tax Act, *supra*, § 302(a)(1).

22 The sunset date contained in EGTRRA § 901 was extended to December 31, 2012 by the 2010 Tax Act § 101(a)(1). The remaining provisions of the new law left the portions of EGTRRA identified in the immediately following notes untouched, which resulted in their extension through December 31, 2012.

23 EGTRRA, *supra*, §551, amending IRC, § 2031(c)(8).

24 EGTRRA, *supra*, §§571 – 573, amending IRC, § 6166.

25 EGTRRA, *supra*, §532, amending IRC § 2011 and adding IRC, § 2058.

26 See California Trust Administration (Cont.Ed.Bar 2d ed. 2001) §12.3.

27 EGTRRA, *supra*, §562, amending IRC, § 2642(a)(3).

28 EGTRRA, *supra*, §561, amending IRC, § 2632(b), adding IRC § 2632(c).

29 EGTRRA, *supra*, §561, adding IRC, § 2632(d).

30 EGTRRA, *supra*, §564, adding IRC, § 2642(g).

31 The new law does not modify the gift tax regime for transfers made in 2010.

32 The term "executor" is used as in IRC§ 2203 and means an executor or administrator of the decedent's estate or, if there is none, any person in actual or constructive possession of any of the decedent's property – most typically the trustee of a decedent's revocable trust.

33 2010 Tax Act, *supra*, § 301(c).

34 IRC, § 1022.

35 Of course, whether the cost of preparing both returns makes sense will require a fact specific analysis.

36 IRC, §§ 1014, 1015(a); Treas. Regs. §§ 1.1014-1 - 1.1014.8; 1.1015-1.

37 For example, the estate of a decedent with relatively high basis assets that may face a challenge on audit which could result in the imposition of an estate tax may prefer the carryover basis regime, particularly if the $1.3 million (and possible additional $3 million spousal) basis step up would result in a full step up in basis in any event.

38 IRC, § 6075(a); Treas. Regs. §§ 20.6018-1(d) and 20.6075-1.

39 2010 Tax Act, *supra*, § 301(d)(1).

40 2010 Tax Act, *supra*, § 301(c).

41 It is possible that an abatement of penalties may be available under appropriate circumstances, but counting on that seems a risky approach.

42 2010 Tax Act, *supra*, § 301(d)(i)(C).

43 Probate Code, § 279(a).

44 Probate Code § 295 provides: "Notwithstanding any other provision of this part, if as a result of a disclaimer or transfer the disclaimed or transferred interest is treated pursuant to the provisions of Title 26 of the United States Code, as now or hereafter amended, or any successor statute thereto, and the regulations promulgated thereunder, as never having been transferred to the beneficiary, then the disclaimer or transfer is effective as a disclaimer under this part."

45 IRC, § 2518(b); Probate Code, § 285. By reference to IRC § 2518(b), the new law makes it clear that all requirements for a disclaimer other than the nine month deadline must be met.

46 It should be borne in mind that the size of the estate of the beneficiary, and not just the decedent, should be analyzed for purposes of deciding whether a disclaimer makes sense. The idea behind a generation skipping transfer is to avoid the imposition of gift or estate tax at the first generation below that of the decedent (i.e., at the beneficiary's generation). As a result, a disclaimer may make sense even when the decedent has a very modest estate.

47 EGTRRA, *supra*, § 501(b), adding IRC § 2664 ("This chapter shall not apply to generation-skipping transfers after December 31, 2009.").

48 2010 Tax Act, *supra*, §§ 301, 302(c). Section 302(c) provides: "In the case of any generation-skipping transfer made after December 31, 2009, and before January 1, 2011, the applicable rate determined under section 2641(a) of the Internal Revenue Code of 1986 shall be zero."

49 IRC, § 2653(a).

50 2010 Tax Act, *supra*, §§ 303(b)(2); IRC, §§ 2641, 2001(c) (as amended by 2010 Tax Act, § 302(a)(2)).

51 See Aucutt, *On the Brink Once More* (presented December 22, 2010, ALI-ABA), p. 7.

52 The new law provides that "(f)or purposes of section 2652(a)(1) of such Code, the determination of whether any property is subject to the tax imposed by such chapter 11 shall be made without regard to any election made under this subsection." 2010 Tax Act, *supra*, § 301(c).

53 Under IRC § 2361(c), the GST exemption is tied to the estate tax exemption amount, and under IRC § 2641(a)(1) the GST rate is the maximum estate tax rate (35 percent under the new law). (As noted in the text accompanying note 21, the estate tax now includes an inflation adjustment, but the two year sunset of the bill means that this could only apply in 2012 in the absence of further legislation.)

54 In particular, the new law provides that the executor "may elect to apply such Code as though the amendments made by subsection (a) [repealing the EGTRRA provisions making the estate tax inapplicable and imposing carryover basis during 2010] do not apply with respect to chapter 11 of such Code and with respect to property acquired or passing from such decedent (within the meaning of section 1014(b) of such Code)." 2010 Tax Act, *supra*, § 301(c).

55 2010 Tax Act, *supra*, § 302(c).

56 See Aucutt, *supra*, p. 7.

57 Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions Contained in the "Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010" Scheduled for Consideration by the United States Senate* (JCX-55-10), December 10, 2010, p. 50, n. 53.

58 2010 Tax Act, *supra*, § 101(a)(1), extending the application of EGTRRA §561.

59 See note 28, *supra*.