Fiscal Cliff Legislation—a Mixed Bag

On January 2, President Obama signed into law the "American Taxpayer Relief Act of 2012," commonly referred to as the fiscal cliff legislation. Since this legislation raises rates and limits itemized deductions for high-income folks, one can question whether the Act should properly be titled a "Relief Act." Presumably the only justification for this titling is that the legislation did not raise rates and limit deductions for all taxpayers. Scant justification!

STABILITY FOR THE ESTATE TAX

However, this new legislation does at least stabilize the situation for those concerned about the estate tax. The maximum estate, gift, and generation-skipping transfer (GST) tax rate is now 40 percent, up from 35 percent. The lifetime exemption, however, remains at $5 million, indexed for inflation. It is also important to know that this legislation makes portability permanent, which means that the surviving spouse may elect to use his or her deceased spouse's unused gift and estate tax exemption, thereby maximizing both spouses' lifetime exemptions. Stated simply, a married couple can now pass on up to $10 million without having to worry about estate taxes. What's more, these rates and exemption levels are likely to remain permanent, free from the kind of constant tinkering we saw over the last 10 or so years.

From an estate planning perspective, this legislation is not the worst possible result. In its absence, rates were scheduled to go as high as 55 percent and the exemption would have been reduced to a paltry $1 million. However, it is a long way from a total repeal of estate taxes, a result long advocated by Cato scholars. Our scholars argue that the estate tax is unduly complex and administratively inefficient in that it raises small amounts of revenue while spawning a cottage industry of "estate tax planning." They also point out that it is inherently unfair since it is tantamount to double taxation—taxing assets already subject to income/capital gains taxes during life.

THE IRA CHARITABLE ROLLOVER IS BACK

The fiscal cliff legislative package brought back another old-timer: the IRA charitable rollover. Just to refresh your memory, this is the provision which allows both traditional and Roth IRA owners, age 70½ and older, to make tax-free transfers up to $100,000 directly from their IRAs to qualified charitable organization, such as Cato. Since a distribution made under this rule won't be included in income, you won't receive an income tax charitable deduction. The major advantage of this "direct to charity" set-up is that the amount donated won't be subject to the various limitations on itemized deductions.

Unlike the estate tax, this rollover provision is not permanent and it is currently available for 2013 only. Some complex transitional provisions also allowed folks to take advantage of it in their 2012 returns, based on specially designated January 2013 transactions. This transitional window is now closed—so it's 2013 or nothing. One can only hope that at some point Congress will decide to make this benefit permanent and stop the endless back and forth of expiration and reinstatement.

If you have question about these provisions or other estate planning matters, please contact Cato's director of planned giving, **Gayllis Ward** at **gward@cato.org** or **202-218-4631**. ■