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FEDERAL ESTATE TAXES AND OREGON INHERITANCE TAXES

More Changes Ahead

**“Anyone may so arrange his affairs so that his taxes shall be as low as possible;
he is not bound to choose that pattern which best pays the treasury.
There is not even a patriotic duty to increase one's taxes.”**

- Learned Hand, Author and Jurist

The federal estate tax is scheduled for repeal in 2010; however, the repeal is for *one year only*. Changes to the federal estate tax law have triggered changes to the Oregon inheritance tax, which may come as an unwelcome tax bill for some Oregon taxpayers.

FEDERAL ESTATE TAXES. Federal estate taxes are imposed on the transfer of assets at death; however, the federal law provides a *credit* against the federal estate tax. In 2007, this credit allows one to transfer up to \$2 million in assets at death free from federal estate tax. The tax-free exemption amount is increasing as follows:

| Year | Federal (tax-free) Exemption Amount | Minimum and Maximum Tax Rates |
|-------------|---|--|
| 2005 | \$1,500,000 | 45 - 47% |
| 2006 | \$2,000,000 | 46 - 46% |
| 2007 | \$2,000,000 | 45% |
| 2008 | \$2,000,000 | 45% |
| 2009 | \$3,500,000 | 45% |
| 2010 | Estate Tax is repealed for one year as of 1/1/10 and replaced with carry-over basis regime | |
| 2011 | \$1,000,000 | 41 - 55% |

A married couple has the additional benefit of the *unlimited marital deduction*, which permits a husband and wife to transfer assets to one another, either during life or at death, free of federal gift and estate taxes. The marital deduction is actually a *deferral* of federal estate taxes, if any, until the death of the surviving spouse. In simple terms, *with proper tax planning*, a married couple in 2007 can transfer to children or others up to \$4 million of their assets, or two times the tax-free amount, free of federal estate taxes. Moreover, a married couple can defer federal estate taxes on the amount above \$4 million until the death of the surviving spouse.

OREGON INHERITANCE TAXES. In 2003, the Oregon legislature changed Oregon's inheritance tax law. Specifically, to avoid loss of tax revenue resulting from changes to the federal estate tax, the Oregon legislature disconnected from the federal law and lowered the state exemption amount, which increases the amount of assets subject to potential Oregon inheritance tax.

For example, if a person dies in 2007 with a taxable estate valued at \$2 million, no federal estate tax is due because the 2007 federal exemption amount is \$2 million. However, the Oregon exemption amount in 2007 is limited to *\$1 million*. Consequently, in 2007, a \$2 million estate will incur an Oregon inheritance tax of \$99,600.

| Year | Oregon Exemption Amounts | Oregon Minimum and Maximum Tax Rates |
|-------------|-------------------------------------|---|
| 2005 | \$950,000 | 6.4 - 16% |
| 2006 | \$1,000,000 | 7.2 - 16% |
| 2007 | \$1,000,000 | 7.2 - 16% |
| 2008 | \$1,000,000 | 7.2 - 16% |
| 2009 | \$1,000,000 | 9.6 - 16% |
| 2010 | \$1,000,000 | 9.6 - 16% |
| 2011 | \$1,000,000 | 5.6 - 16% |

SPECIAL NOTE TO MARRIED COUPLES: Tax planning wills and trusts for married couples prepared prior to November, 2003 do not address the recent changes in the Oregon inheritance tax law. Consequently, those documents should be reviewed and updated.

WHAT NEXT? Congress and the President may make further changes to the federal estate tax law. Some speculate that Congress will vote to accelerate the repeal of the federal estate tax. Others expect a vote to freeze the federal exemption amount at \$5 million or possibly \$7 million. One thing is certain, long range tax planning is challenging in this time of uncertainty and change. I recommend that individuals and married couples review their estate plans annually and obtain current legal and tax advice to optimize tax savings under current law and ensure the estate plan works as intended.