

Happy Holidays!
Historic Wealth Transfer Tax Relief

Farhad Aghdami
Williams Mullen
804.420.6440
aghdami@williamsmullen.com

John "Jay" H. Turner III
Williams Mullen
804.420.6480
jturner@williamsmullen.com



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Tax Relief Act of 2010

- Tax Relief, Unemployment Insurance, Reauthorization, and Job Creation Act of 2010
 - Reinstates Estate Tax with \$5 Million Exemption and a 35% Rate
 - Reunifies Estate and Gift Tax Exemption
 - Creates Portability of Estate Tax Exemption Between Spouses
 - Extends Income Tax Rates, Capital Gain Rates, and Qualified Dividend Preference to 2012



Estate, Gift and GST Tax

| Year | 2009 |
|----------------------|----------|
| Estate Tax Exemption | \$3.5MM |
| Tax Rate | 45% |
| Gift Tax Exemption | \$1.0 MM |
| Tax Rate | 45% |
| GST Tax Exemption | \$3.5MM |
| Tax Rate | 45% |



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| GST Tax Exemption | \$3.5MM | \$5.0MM |
| Tax Rate | 45% | 0% |

¹Executor May Elect Out of Estate Tax in 2010; Assets Subject to Carryover Basis; \$1.3 Million / \$3.0 Million Basis Adjustment



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²\$5.0MM Exemption Amount Indexed for Inflation Rounded to \$10,000



Estate, Gift and GST Tax

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| Estate Tax Exemption | \$3.5MM | \$5.0MM | \$5.0MM | \$5.0MM | \$1.0MM |
| Tax Rate | 45% | 35% | 35% | 35% | 55% |
| Gift Tax Exemption | \$1.0 MM | \$1.0MM | \$5.0MM | \$5.0MM | \$1.0MM |
| Tax Rate | 45% | 35% | 35% | 35% | 55% |
| GST Tax Exemption | \$3.5MM | \$5.0MM | \$5.0MM | \$5.0MM | \$1.0MM |
| Tax Rate | 45% | 0% | 35% | 35% | 55% |

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³GST Exemption Indexed for Inflation; 5% Surtax for Estates \$10-17MM



Extension of Time and Tax Rates

- Nine Month Extension of Time After Date of Enactment of Statute
 - File an Estate Tax Return (Under Either Regime)
 - File a Return for GST Tax Purposes
 - Payment of Estate Tax
 - Filing of a Disclaimer
- Includes a Provision to Deal With Calculation of Tax and Differences in Tax Rates



Spousal Portability Of Exemption

- Deceased Spouse May Transfer Unused Applicable Exemption Amount to Surviving Spouse
 - Applies to Decedents Dying After 2010
 - Executor of Deceased Spouse Must Make Irrevocable Election on Estate Tax Return
 - No Statute of Limitation for IRS to Examine Deceased First Spouse's Estate Tax Return
 - Consider Impact on Difficult to Value Assets



Spousal Portability Of Exemption

- No Portability of GST Exemption
 - Clients Seeking to Create Long-Term Trusts Need to Create a Trust at Death of First Spouse to Use Both Spouses' GST Exemption
- Multiple Spouse Rule
 - Surviving Spouse Can Only Use Unused Applicable Exclusion Amount From Last Deceased Spouse
 - Due Diligence Item Prior to Marriage?
 - Privity Requirement
 - Lifetime Gifting May Be OK



Portability

- Deceased Spouse's Applicable Exclusion Amount Not Indexed for Inflation
- What Happens if Law Repealed After 2012
- Unlike a Credit-Shelter Trust, Portable Applicable Exclusion Amount Does Not Shelter Income and Growth in Assets From Estate Taxation at Death of Second Spouse.
 - However, No Basis Adjustment at Second Spouse's Death With Credit Shelter Trust



Portability

\$5 Million Assets
\$5 Million Portable Exemption



Portability

10 Year Growth at 6%
\$3.95 Million
\$5 Million Assets
\$5 Million Portable Exemption



Portability

10 Year Growth at 6%
\$3.95 Million
\$5 Million Assets
\$5 Million Portable Exemption



\$1.38 MM Tax
35% Tax Rate



Portability

- Non-Tax Trust Benefits
 - Asset Protection
 - Tort Creditors
 - Contract Creditors
 - Claims of Former Spouses
 - Protection Against Diversion of Assets upon Remarriage
 - Professional Asset Management



Income Tax Provisions

- Extension of Income, Capital Gain, and Qualified Dividend Rate Preferences Through 2012
 - 35% Top Marginal Income Tax Rate
 - 15% Top Capital Gains Rate
 - 15% Qualified Dividend Rate
- Two Year AMT Patch for 2010-2011
 - Increases AMT Exemption from \$45,000 to \$72,450 for Married Filing Jointly



Charitable Provisions

- IRA Minimum Required Distributions to Charity
 - \$100,000 Distribution Directly to Charity
 - Can Make Distribution to Charity in January 2011 and Relates Back to 2010
- Extension of Increased Contribution Limits and Carry-forward Period for Conservation Easements



EGTRRA Extensions

- State Death Tax Deduction
 - No State Death Tax Credit
- GST Relief
 - Automatic Allocations
 - Severances
 - 9100 Relief
- Conservation Easements
- Section 6166 and 2032A Relief



What's Not In The Bill

- Ten Year Term for GRATs
- Limitations on Valuation Discounts
- Consistency of Basis Reporting By Beneficiaries
- Broader Relief for Family Farms and Family Businesses



What Does This Mean For Us?

- Certainty for Two Years, Until Déjà Vu Again
 - \$1 MM Exemption and 55% Rate in 2013
 - Any Reduction from 2012 Level Will Feel Like a Tax Increase
 - Election Year Politics
- Removes A Significant Portion of Population From Wealth Transfer Tax System
 - Large Exemption and Portability
 - Tie Estate/Gift Tax Rate to Top Income Tax Rate
 - Beginning of the End of Estate Tax?



Estate Tax Returns Filed in 2009

| | Non-Taxable | Taxable | Total |
|--------------------|---------------|---------------|---------------|
| Under \$2.0 MM | 749 | 555 | 1,304 |
| \$2.0 - \$3.5 MM | 10,831 | 6,999 | 17,830 |
| \$3.5 - \$5.0 MM | 3,279 | 2,862 | 6,141 |
| \$5.0 - \$10.0 MM | 2,692 | 2,644 | 5,336 |
| \$10.0 - \$20.0 MM | 843 | 1,015 | 1,857 |
| \$20.0 MM + | 409 | 637 | 1,045 |
| Total | 18,802 | 14,713 | 33,515 |

Source: IRS Statistics of Income – Estate Tax Returns Filed in 2009 Based on Tax Status and Size of Gross Estate



What Does This Mean For Us?

- Estates Smaller Than \$5 Million
 - “I Love You” Wills Or Disclaimer Based Plans
- Estates Between \$5 Million and \$10 Million
 - Credit Shelter Trust or Spousal Portability
- Estates Over \$10 Million
 - Business As Usual
 - Increased Exemptions Create More Options and Opportunities



Formula Clauses

- No Need to Address Repeal of Estate Tax After 2010
- Confirm Amount Passing to Beneficiaries Under Formulas Tied to Larger Exemption
- Increased Emphasis on Re-Titling of Assets and Funding of Trusts to Cover \$5 MM Exemption
 - Residences
 - Life Insurance
- Augmented Estate Claims



Insurance Trusts

- Allocation of GST Exemption For 2010 Gifts to Insurance Trust Was Problematic
 - No GST Exemption in 2010 to Allocate
 - Had to Consider Loans, Skipping Payments, Etc.
- Now, Simply Allocate GST Exemption
 - \$5 MM Exemption in 2010
- Large Gifts in 2011-2012 to Fund Premiums
- Continuing Need for ILITs?
 - Consider What Happens Upon Termination of ILIT



Things to Do Right Now

- Re-Evaluate Gifts in 2010
- GST Planning
- AFR Rate Planning – Loans and Sales
- GRATs
- CLATs
- Roth IRA Conversions



Gifts in 2010

- No Rush to Make Taxable Gifts in 2010
 - Reunification of Exemption to \$5 MM in 2011
 - Tax Rate Will Be 35% in 2011-2012
- Except for Really Big GST Gifts
 - GST Tax Rate is 0% in 2010
 - Gifts Over \$1 MM Subject to Gift Tax, But Not GST Tax
 - So a Really Big Direct Skip GST Gift in 2010 May Make Sense if Client is Willing to Pay 35% Gift Tax



GST Planning

- GST Tax Rate is 0% in 2010
 - Make Distributions Out of Non-Exempt Trusts in 2010
 - Terminate Non-Exempt Trusts in 2010
- Consider Disclaimer of Assets Passing from 2010 Decedents



AFR Rate Planning - Loans/Sales

- Consider Lending Money to Family Members at Applicable Federal Rate
 - Refinance Existing Loans
- Consider Selling Business or Real Estate Assets to Family Members at Applicable Federal Rate
 - Freeze Value of Distressed Assets



Applicable Federal Rates

| Year | Short-Term | Mid-Term | Long-Term |
|------|------------|----------|-----------|
| 1990 | 7.80% | 8.50% | 8.87% |
| 1995 | 5.65% | 5.91% | 6.36% |
| 2000 | 6.10% | 5.87% | 5.98% |
| 2005 | 4.34% | 4.52% | 4.79% |
| 2010 | 0.32% | 1.53% | 3.53% |

Annual Rates for December of Each Applicable Year Listed; Short-Term Rate Used for Loans of Less 3 Years; Mid-Term Rate Used for Loans Between 3 and 9 Years; Long-Term Rate Used for Loans Greater Than 9 Years.



GRATs

| Year | 7520 Rate | Annuity | Remainder |
|------|-----------|-----------|-----------|
| 1990 | 10.20% | \$577,734 | \$ - |
| 1995 | 7.20% | \$554,631 | \$12,767 |
| 2000 | 7.00% | \$553,097 | \$15,957 |
| 2005 | 5.40% | \$540,862 | \$41,406 |
| 2010 | 1.80% | \$513,531 | \$98,254 |

Assumes 2 Year *Walton* style GRAT with level payments funded with \$1 MM and 8% annual return.



CLATs

| Year | 7520 Rate | Annuity | Remainder |
|------|-----------|-----------|-------------|
| 1990 | 10.20% | \$111,860 | \$ - |
| 1995 | 7.20% | \$87,370 | \$ 461,209 |
| 2000 | 7.00% | \$85,820 | \$ 574,523 |
| 2005 | 5.40% | \$73,830 | \$1,451,863 |
| 2010 | 1.80% | \$50,020 | \$3,191,716 |

25 Year Charitable Lead Annuity Trust funded with \$1 MM and 8% annual return



Roth IRA

- Contributions Build Up Income Tax Free
- Distributions are Income Tax-Free
- Original Account Owner Not Subject to Minimum Required Distributions
 - Beneficiaries Required to Take Distributions on a “Stretch” Basis



Roth IRA

- Income Limitation on Roth IRA Conversion Waived in 2010
- Income Tax Recognized on Conversion Can be Deferred to 2011 and 2012
 - Tax Paid in 2012 and 2013
 - Extension of Tax Cuts for Two Years Produces No Rate Differential



Candidates for Roth Conversion

- Can Pay Income Tax on Conversion from Other Assets
- Don't Need Income from IRA
- Wish to Transfer Stretch IRA
- Will Have Comparable Tax Rates in Retirement
- Have Offsetting Deductions – Charitable or NOLs



Conclusion

- Wealth Transfer Tax Planning Opportunities Abound
 - GST Planning in Last Days of 2010
 - Gifting In 2011 and 2012
 - Re-Evaluate Need for Sophisticated Planning Given Large Exemptions
- Portability Has Elusive Appeal, But Many Pitfalls
- Narrow Application of Estate Tax to a Small Group May Lead to Its Demise



Questions?

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