



Toledo
Community
Foundation

Inspiring and Connecting Thoughtful Giving

Toledo Community

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About Your Foundation

Since 1973, **Toledo Community Foundation** has provided individuals, families and businesses interested in the well-being of our community with an *efficient, effective, low-cost, professionally managed* mechanism to achieve their charitable goals.

For philanthropists wishing to maximize the impact and life of their charitable gifts, the Foundation provides *resources for thoughtful giving*. Using its expertise and personalized services, **Toledo Community Foundation** helps donors transform their philanthropic impulse to measurable community impact. Beyond the gifting of assets, the Foundation helps donors identify issues of importance to them and *inspires engagement* with community organizations addressing these issues, thereby maximizing the impact of charitable gifts and creating a greater sense of fulfillment.

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Two-Year Bonus

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Financial Planning

The 2010 Tax Act (The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010), signed into law by President Obama in December, is the most significant change in the estate-tax system in quite some time. Yet some of the conclusions and a significant part of the advice your clients have read in the media are misleading.

Estate planning remains vital to preserve the hard-earned wealth of your clients and their families. Educating them about the new options and opportunities will continue to be important.

OVERVIEW OF TAX CHANGES

The gift, estate and generation-skipping transfer (GST) exemption amounts are now and will remain the same through 2012 at \$5 million (\$10 million with portability, the right given to the surviving spouse to use the deceased spouse's unused estate-tax exclusion). The gift, estate and GST tax rate has been reduced to 35%, down from the 55% originally scheduled to take effect in 2011.

Clients should be aware that these new generous changes are only temporary. They end in 2012, and in 2013 a \$1 million exemption and 55% rate return, assuming no intervening action by Congress. (The GST exemption will increase for inflation to around \$1.4 million.)

Advisors have to help clients plan for this continued estate-tax roller coaster. Failing to take the best advantage of these exemptions could undermine estate planning. Any wealthy client should evaluate the risk of not using the large exclusion while it is available. Making gifts now can remove future appreciation from an estate and minimize the tax damage in later years.

UPDATE PLANS

All clients should review and revise their estate plans and documents in light of this legislation. No client should assume that existing documents will meet their goals. Most probably won't.

The ramifications of the 2010 Tax Act are broad and often surprising. Everything from insurance coverage, old irrevocable trusts, recently signed wills, powers of attorney, prenuptial agreements and business buy-sell agreements must be reviewed. Corrective planning steps will be important for most taxpayers. Those who adopt a wait-an- see approach may find they've defaulted to a wait-and-pay approach.

ASSET PROTECTION AND GIFTING

The next two years present an historic opportunity for wealth transfer. For ultrahigh-net-worth taxpayers, a unique convergence of positive planning attributes—the retention of favorable rules for grantor-retained annuity trusts (GRATs), discounts in valuation, low interest rates and the granting of a \$5 million gift exemption—may only be available for a short time.

"2011 to 2012 provides the best opportunity for physicians, professionals and others concerned about asset protection to safeguard their wealth—it has produced the 'perfect storm' for asset protection and estate planning," says Jonathan Blattmachr, a director for Eagle River Associates and Alaska Trust Company and a former Partner at Milbank Tweed Hadley & McCloy. For the first time, the new \$5 million gift exemption provides an opportunity for clients desiring asset protection to shift significant wealth into domestic asset protection trusts without the burden of a confiscatory gift tax.

But should clients make large gifts in 2011 and, perhaps, avoid complex and costly estate planning later? While making a large gift is seductively simple, this plan could prove inadequate. Planners should help clients evaluate whether making large gifts now is appropriate.

DON'T PROCRASTINATE

When clients hear that the 2010 Tax Act generosity only lasts two years, many will assume that they can defer planning until the end of 2012. But the passage of time does not only concern estate-tax laws. Economic changes are also crucial to meeting planning goals.

GRATs, charitable lead annuity trusts (CLATS), family loans and other estate planning techniques are interest rate sensitive. The interest rate used in some transactions has increased noticeably since December, when the long-term rate was set at 3.53%. For identical transactions in January, the long-term rate increased to 3.88%. Further increases in future interest rates will significantly erode the leverage that important planning strategies can achieve.

Time really is of the essence in pursuing planning. Planners who can help clients understand the impact of potential interest rate increases on estate planning will help clients move forward while it is more advantageous.

CHANGES COMING?

How will the new tax law affect various estate planning strategies? Here's a brief look at what to tell clients:

* GRATs. GRATs remain a viable planning technique for many wealthy clients. While most advisors anticipated GRATs would be restricted or eliminated, they were spared in the 2010 Tax Act. But the reprieve may only last until the end of 2012, so wealthy clients for whom GRATs are appropriate should aggressively plan on using them appropriately.

Advisors must help these clients evaluate GRATs under the new paradigm. What are the pros and cons of using GRATs compared with outright gifts or installment sales to grantor trusts in light of the new \$5 million exclusion?

If the assets inside the GRAT don't outperform the required federal interest rate benchmark or if the taxpayer dies during the retained annuity term, the technique does not work. With a simple outright gift, any positive growth will be outside the client's estate. And an installment sale to a grantor trust also likely will outperform a GRAT because the interest rate used is lower, the technique may well produce benefits even if the client dies before the loan from the sale is repaid and unlike with a GRAT, the taxpayer's GST exemption can be effectively employed.

* Life insurance. Some clients will undoubtedly conclude that with a \$5 million exclusion they can cancel life insurance carried to fund the estate-tax burden on their wealth. But clients should not jump to conclusions. The estate-tax system hasn't disappeared, and may roar back

with a vengeance in 2013.

Planners should reevaluate client life insurance coverage, though. It's important to take a new look at projections to reassess life insurance needs and to evaluate whether trusts that were formed as grantor trusts (your client pays the income tax on trust income) should be changed to non-grantor trusts.

If a client has a significant insurance policy outside of a trust, or costly policies inside a trust, the new \$5 million exclusion could revolutionize insurance planning. Financing or split-dollar insurance arrangements might be best unwound by making a simple gift to an insurance trust that will not be taxed on account of the new higher gift-tax exemption.

* Trusts. Planners have long recommended using bypass and marital deduction trusts in estate planning. Why mess with a winning formula?

Most of your client's wills should continue to include these trusts. Planners should endeavor to explain to clients why the new estate-tax portability provisions, while beneficial, are traps for the unwary taxpayer and should never be relied upon in lieu of traditional bypass trust planning.

The 2010 Tax Act has fundamentally changed estate planning, but only for two years. Clients who take aggressive advantage of what might prove a tax anomaly may benefit tremendously. Advisors should endeavor to help clients understand the complexity of the changes, and the opportunities they present.

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