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Re: 2012 Tax Update

Dear Clients and Colleagues,

This bulletin is an update on the most recent gift and estate tax developments, and presents our current thinking regarding wealth transfer planning in 2012. It also serves as a follow up to our "Tax Relief Act of 2010" bulletin of January 3, 2011, which can be accessed by clicking the "Family Wealth and Tax Planning" link on our firm website (www.hopkinscarley.com), and viewing the "Related Articles" on the right side of the screen.

<u>Increase In Gift and GST Tax Exemptions - $120,000 Per Person / $240,000 Per Couple</u>. A significant change for this year is that the gift tax and generation-skipping transfer tax ("GST tax") exemptions have increased by $120,000 for each individual [$240,000 for each married couple]. These exemptions are currently $5,120,000 for each individual [$10,240,000 for each married couple], reduced by prior lifetime taxable gifts. If you have previously exhausted your $5,000,000 exemption, then you may want to consider ways to take advantage of (and potentially "leverage") this new increase in the exemption.

<u>Historically, There Has Never Been a Better Time For Gift Planning.</u> Due to today's unique combination of depressed asset values, all-time low interest rates, and exceptionally high gift tax and GST tax exemptions, there has never been a better time to implement gift tax planning techniques in order to shift appreciation and value out of one's taxable estate. As explained in our 2011 bulletin, we believe that the best tax planning techniques to implement in this environment are irrevocable life insurance trusts ("ILITs"), grantor retained annuity trusts ("GRATs"), qualified personal residence trusts ("QPRTs"), and sales of property to so-called "intentionally defective grantor trusts" ("IDGTs"). Of course, simple gifts, either outright or to generation-skipping trusts, are also available.

<u>Plan Now Since The Window of Opportunity Might Close</u>. With that said, this "perfect storm" for gift tax planning may not last much longer. Both interest rates and asset values may have bottomed out and, barring remedial action by Congress and the President, the estate tax, gift tax and GST tax exemptions will be reduced from $5,120,000 to approximately $1,000,000 after 2012. In addition, the estate tax, gift tax and GST tax rates are scheduled to increase from 35% to 55% after 2012. To the extent that exemptions are not used this year, we believe that there is some risk that they will be lost.

Adding to this sense of urgency, the Obama Administration issued its Fiscal Year 2013 Revenue Proposals (the "Greenbook") on February 13, 2012. In its Greenbook, the administration proposes changes in law that would eliminate or significantly curtail the gift and estate tax benefits afforded by certain tax planning vehicles, including GRATs, family limited partnerships ("FLPs"), sales of property to IDGTs, and generation-skipping trusts. In past years, the administration has made similar proposals to limit the use of "zeroed-out" GRATs and FLPs; however, this is the first year the administration has made proposals that would drastically impact IDGTs and long-term generation-skipping trusts. If successful, the administration's proposal could cause assets held in an IDGT to be included in the settlor's taxable estate, assets distributed from an IDGT to beneficiaries during the settlor's lifetime to be subject to the federal gift tax, and all or a portion of a settlor's GST tax exemption allocated to a generation-skipping trust to expire after a set number of years. These changes would severely impact the tax benefits offered by such trusts, including the ability to "leverage" one's gift tax and GST tax exemptions, and the ability to keep the assets of such trusts from being included in the taxable estates of future generations.

With all of this said, the Greenbook proposals are not designed to impact trusts that have been established *prior to the date of enactment*. For these reasons, we are recommending that clients with sizable estates make structured gifts before the end of this year and prior to the date of enactment of any adverse laws proposed in the Greenbook in order to utilize their exemptions in today's unique economic and legal climate. If you have not done so already, we recommend that you contact us prior to **June 30, 2012** in order to set up a meeting to discuss potential gift tax planning opportunities. Meeting with us early in the year will enable us to determine and implement the optimal strategies for your particular situation.

<u>Annual Gift Exclusion.</u> The annual gift exclusion remains unchanged at $13,000 per recipient. So long as the donor gives no single recipient more than $13,000 [or $26,000 for a married couple splitting gifts] in cash or other assets, then no federal gift tax return needs to be filed by the donor(s) since no taxable gifts will have been made. With that said, there is no limit on gifts made for another person's tuition payments and medical expenses so long as payments are remitted directly to the respective institution or service provider.

Please note that although unlimited gifts may be made between spouses who are U.S. citizens, the annual exclusion for gifts from a U.S. citizen spouse to a non-U.S. citizen spouse in 2012 is only $139,000 per year.

<u>Urgency Regarding Unfiled Gift Tax Returns.</u> Please be aware that the I.R.S. and the Department of Justice have a national campaign underway to locate taxpayers who have failed to file gift tax returns for taxable gifts of property. In California especially, these efforts include an ongoing attempt by the I.R.S. to subpoena deeds and other records from state agencies in order to gain information regarding transferred interests in real estate. Accordingly, if you made any past transfers of real estate or other property to persons in excess of your annual gift tax exclusion and did not file a federal gift tax return for the year of transfer, please contact us as soon as possible so that we can provide assistance in bringing you into compliance.

April 17, 2012 Is Filing Deadline For 2011 Individual Income Tax and Gift Tax Returns. As you may know, the filing deadline for 2011 individual income tax returns (Form 1040) and gift tax returns (Form 709) is Tuesday, April 17, 2012. Although these returns are typically due on April 15, that date falls on a Sunday this year, which is followed by Emancipation Day on Monday, April 16.

Reminder to Check Title of Assets and Beneficiary Designations. As part of your annual tax preparation, you should confirm that the title on your financial accounts and real property is correct. For this purpose, any assets intended to be held in your revocable living trust must be titled in your name(s) as trustee(s) of the trust. Please also check to make sure beneficiary designations for life insurance and retirement accounts (pensions, 401(k), IRAs) are properly updated and, specifically, not left blank or “to my estate.” Please contact us if you have any beneficiary designation questions since these can vary on a case-by-case basis.

As always, we look forward to assisting you and your family in planning your estates. If you have any questions or would like to discuss any of the above in more detail, please feel free to contact one of our estate planning attorneys listed below:

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Sincerely,

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