

May 2012

To Our Clients and Other Friends:

We are almost half-way through the year and that much closer to the scheduled expiration of important tax benefits at the end of 2012. The election year is well under way and, while taxes have not been the “lead” story, there is a constant undercurrent in the press and occasionally from the candidates concerning where we are, where we are going and where we should be going with regard to federal taxes. We will summarize in this Alert where we are now and where we are scheduled to go in the estate, gift and generation-skipping tax areas. As you will see, we believe that there are a number of planning opportunities available in 2012 that may not be available in future years.

#### Estate, Gift and Generation-Skipping Taxes

Although exemptions have dramatically increased and rates have decreased for these federal taxes in recent years, these taxes continue to be relevant to many of our clients and continue to be the subject of important planning. As of now, the exemptions for all three of these interrelated tax structures are \$5,120,000 per individual. In general, this means that a client who has not previously used any gift tax exemption (which was \$1 million from 2002 to 2010) may make taxable gifts totaling \$5,120,000 without incurring any gift tax; the estate of such an individual who dies with an estate not in excess of this amount will not incur any federal estate tax; and gifts in this amount can be made, during life or at death, to or for the benefit of grandchildren, without incurring any federal generation-skipping tax.

For now, these \$5,120,000 exemptions are scheduled to expire at the end of 2012, to be replaced by a \$1 million exemption with certain inflation adjustments. Whether or not that scheduled change will take place is the subject of much conjecture among politicians, tax experts and various pundits. What is known is that the larger exemptions are in place now and may or may not be in place after 2012.

The possible reduction in the exemptions from \$5,120,000 to \$1 million at the end of 2012 suggests that clients with large estates might consider a variety of planning options, including, for instance:

- 2012 gifts to children, grandchildren and others, either outright or in trust.
- 2012 gifts in trust for the potential benefit of the donor’s spouse.

#### “Portability” of Exemptions

For many years now, our clients often have planned for the use of their federal estate tax exemptions through a somewhat complex structure involving splitting the ownership of assets between spouses and structuring their wills or revocable trusts in a way that either requires or permits the assets of the first spouse to die to be held in trust for the sole or partial benefit of the surviving spouse. With such a plan, the exemption available to the first spouse to die will be preserved in the form of a trust for the benefit of the surviving spouse. Starting in January 2011, the law was changed to provide that the exemption otherwise available to the first spouse, if not used in his or her estate, could pass to the surviving spouse for possible use by that spouse at his or her death. Thus, the unused exemption can become “portable.”

While we are making use of this new rule when appropriate, we want to consider with each couple whether or not it makes sense to rely on portability to ensure full use of the exemption of both spouses. There

are a number of both tax and non-tax reasons for choosing the “old” planning method of creating a trust for the surviving spouse. For example, remarriage by the surviving spouse under some circumstances could result in the loss of the first spouse’s “portable” exemption; this loss would not occur had the first spouse to die created a trust at his or her death. Clients who wish to fully use both spouses’ generation-skipping tax exemption will need to create a trust at the first spouse’s death. Other clients, including many with children from a prior marriage, will want to create a trust at the first death to ensure that assets are distributed to certain beneficiaries at the surviving spouse’s death. Finally, this change in the law also is scheduled to expire at the end of 2012, and while it may be renewed, we cannot be certain. Still, in certain situations, or for certain types of assets, it may make sense to take advantage of the portability of the first spouse’s exemption.

### Planning Through Use of Low Interest Rates

As you probably know, interest rates are historically low right now. Many planning techniques depend on interest rates published monthly by the IRS. There are many ways to take advantage of these low interest rates.

As a simple example, in order for a loan from parent to child to be respected by the IRS for tax purposes, the interest rate must be equal to or exceed the rate published monthly by the IRS for loans with similar terms. In May 2012, the annual interest rate that must be charged in an 8 year term loan is only 1.30%.

Similarly, when certain types of gifts are made, both to individuals and to charities, the IRS publishes the so-called 7520 or “hurdle” rate for purposes of calculating the gift tax effects of those gifts. In May 2012, the hurdle rate is 1.6%. If a client creates a grantor retained annuity trust or “GRAT” in May, the total return on the assets in the trust must only exceed 1.6% per year for the GRAT to succeed in moving assets to others gift tax free.

### Developments at HTTS

On October 31, 2011, HTT&S celebrated its 17<sup>th</sup> anniversary. Many of you have been associated with the firm since we started out (some from before!) and we have appreciated the support, encouragement and friendship of all of you. We had a number of personnel changes in 2011 and early in 2012, including the addition of four lawyers, as a result of which the firm now has sixteen lawyers, six paralegals and fifteen other employees. This is a far cry from the total staff of thirteen that began the firm that long ago Halloween. Please take a look at our website, [www.htts.com](http://www.htts.com), for more information about our new lawyers and what is going on at the firm. We have revamped the website to include additional information about our lawyers and their speaking and writing in various professional venues.

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As always, our lawyers stand ready to work with you to determine whether any or all of these planning techniques can be useful to you and your family. Please feel free to contact your HTTS lawyer or any of us about these issues, or any other estate-related issues where you think we may be helpful.

Sincerely yours,

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