Wealth Transfer Newsletter

CURRENT DEVELOPMENTS, HIGHLIGHTS AND LEGISLATIVE CHANGES
Wealth Transfer Practice Group
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Future of Estate and Gift Taxes The American Recovery and Reinvestment Act of 2009 Individual Accounts

Having just closed the first quarter of 2009, we have seen many significant developments and highlights that impact the wealth transfer planning area. President Obama and this Country face challenges of historic proportions with regard to the current state of the economy, and President Obama has also signed one of the most significant pieces of legislation to have been passed by Congress, the American Recovery and Reinvestment Act of 2009 (the "Stimulus Act"). The Stimulus Act is designed to provide relief and assistance to taxpayers, as well as to provide stimulus to our Country's economy.

We recognize that there is considerable information available with regard to the recently passed legislation and that you likely have read and heard a great deal about the Stimulus Act. Therefore, in this edition of the Newsletter, we will highlight for you portions of the Stimulus Act that we believe would be most relevant to our clients and advisors. In addition, we wanted to provide you with information regarding several proposed estate tax bills that have been introduced since January and that have only received limited media attention, but which will likely affect you. Further, the Stimulus Act is not the only bill that recently has been signed into law – the Worker, Retiree, and Employer Recovery Act which was passed and signed into law in late December, 2008, contains provisions that may impact a great number of you with regard to your retirement accounts and the required minimum distribution rules.

The Budget for 2009 – 2010 proposed by the new administration has many provisions that will impact taxes and potentially wealth transfer planning. With the considerable efforts put into the various bills, all with the goal of stimulating the economy and providing taxpayers with much needed relief, we are hopeful that the financial markets will begin to respond as investors and businesses react to the new opportunities that are now available. We are also hopeful that the enactment of the Budget will provide certainty in the estate and tax planning area.

Many of you have sustained losses in the stock market, and unfortunately, some of you have fallen victim to investment advisors who promised investment returns that were based on false, if not fictitious and fraudulent, information. Our Team and Firm have counseled some of you in these very unfortunate situations and want for all of you to know that we are available to do what we can to assist any of you that find you are the victim of such a fraud.

The members of our Team encourage you to contact any of us to discuss your concerns and questions and know that we are here for you and your families to provide advice and counsel.

Neill G. McBryde

The Future of the Estate and Gift Taxes

On June 7, 2001, then newly elected President Bush signed into law the "Economic Growth and Tax Relief Reconciliation Act" ("EGTRRA"), which incrementally increased the estate tax exemption amount from $675,000 per person in 2001 to $3,500,000 in 2009. Additionally, under EGTRRA the maximum estate tax rate declined from 55% in 2001 to 45% in 2009 and eliminated the 5% surcharge tax on estates exceeding $10 million. Finally, EGTRRA repealed the estate tax and generation skipping transfer tax as of January 1, 2010. However, EGTRRA contains a "sunset" provision, meaning that all changes to the estate tax laws under the act would be repealed as of January 1, 2011 and the estate tax rates and exclusion amounts would revert to 2001 levels as of January 1, 2011. As a result, since 2001, commentators have speculated that Congress would act before the estate tax was repealed in 2010 to create a more permanent estate tax solution. The commentators have been proven correct with the introduction of 3 bills in the first three months of this Congress and the ongoing budget negotiations.

Most significantly, on March 26, 2009 Senator Baucus (D-MT) introduced S. 722, entitled Permanent Estate Tax Relief, which Bill is in line with President Obama's budget proposals concerning the estate tax and otherwise generally contains provisions that most analysts believe will garner political and populist support. Specifically, S. 722 would set the estate tax exemption at $3.5 million per taxpayer effective for 2010 and beyond and would provide for the maximum estate tax rate of 45%. However, the estate tax exemption would again become unified with the gift tax exemption (allowing for gifts of up to $3.5 million without the imposition of tax) and would index the exemption amounts for inflation. Also notable, S. 722 would provide for portability of the unused portion of a spouse's estate tax exemption to the surviving spouse, thereby preventing the need to equalize the taxable estates of spouses or undertake other techniques in order to avoid wasting a spouse's exemption. In order to take advantage of the portability of the unused exemption, an estate tax return would be required to be filed and an election to transfer such unused exemption be made on the return.

Also, on April 2nd, the Senate passed its fiscal year 2010 budget, which included amendments, passed by close votes, which would provide for a higher estate tax exemption of $5 million and a maximum estate tax rate of only 35%, provided such additional estate tax relief is matched with middle-income tax relief. The budget proposal passed by the House does not contain a similar provision with regard to the higher estate tax exemption and lower rate, and both the House and Senate budgets have been sent to conference for further resolution. As with the other proposed bills, the impact of the amendments is uncertain.

Of other note on this front, on January 9, 2009 Congressman Pomeroy (D -ND) introduced H.R. 436, otherwise known as the "Certain Estate Tax Relief Act of 2009," which would (i) eliminate the estate tax and generation skipping transfer tax repeal for 2010 (in other words, retain the estate and generation skipping transfer taxes); (ii) retain the estate tax exemption amount at $3,500,000 per person; (iii) retain the maximum estate tax rate at 45%; and, (iv) reinstate the pre-2001 5% surcharge on estates with over $10,000,000 in tax. More importantly, H.R. 436 would significantly impact some commonly implemented estate planning techniques, specifically those that rely upon valuation discounts by eliminating marketability discounts in determining the fair market value of an entity (such as a Limited Liability Company ("LLC") or Limited

Partnership) which contains "non-business assets" or passive assets such as marketable securities or real estate not used in a trade or business, as well as eliminate the discount for minority interest if the transferee or members of the family of the transferee have control of such entity.

Also, proposed regulations under the provisions of Internal Revenue Code Section 2704 are expected to be issued in the near term, which similarly may curtail or eliminate valuation discounts when finalized.

Since we do not know the exact timeline for Congress or Treasury to address the estate tax and the supplemental transfer tax issues surrounding it, we advise engaging in any estate planning that would involve entities currently subject to valuation discounts as soon as possible, if appropriate. We will continue to monitor these bills and developments and notify you as these bills make their way through the legislative process.

The American Recovery and Reinvestment Act of 2009: Making the Most of the Legislation to Stimulate Your Finances

The recently enacted "American Recovery and Reinvestment Act of 2009" contains a wide-ranging tax package that includes tax relief for low and moderate-income wage earners, individuals and families with college expenses, and home and car purchasers.

It also includes AMT relief, Business tax relief and expanded tax credits for certain energy efficient home improvements. The following is a general list of some of the Act's provisions, which we hope you will find useful:

- Economic recovery payment. Certain taxpayers are eligible to receive a payment of $250, including Social Security beneficiaries and SSI recipients receiving benefits from the Social Security Administration, and veterans receiving disability compensation or pension benefits from the U.S. Department of Veterans' Affairs.
- Expanded and revised higher education tax credit. The Act provides a $2,500 higher education tax credit for the first four years of college. The credit is based on 100% of the first $2,000 of tuition and related expenses (including books) paid during the tax year and 25% of the next $2,000 of tuition and related expenses paid during the tax year, subject to a phase-out for AGI (adjusted gross income) in excess of $80,000 ($160,000 for married couples filing jointly). 40% of the credit is refundable.
- Computers as an education expense. Computers, computer technology, and software, predominantly educational in nature, including Internet services, now qualify as qualified education expenses in Section 529 education plans for tax years beginning in 2009 and 2010.
- Expanded first-time credit for first-time home buyers. Last year, first-time home buyers were able to receive a refundable tax credit that was equivalent to an interest-free loan equal to 10% of the purchase price of a home (up to $75,000). Taxpayers receiving this tax credit were required to repay the credit over 15 years in equal installments (or earlier if the home was sold). The Act eliminates the repayment obligation for taxpayers that purchase homes on or after January 1, 2009, extends the availability of the credit through the end of November 2009, and increased the maximum value of the credit from $7,500 to $8,000. The credit phases out for taxpayers with AGI in excess of $75,000 ($150,000 in the case of a joint return).

- Tax break for new car purchasers. Taxpayers may deduct State and local sales taxes paid on up to $49,500 for the purchase of a new automobile, including motorcycles, and motor homes. The deduction is available for vehicle purchases between February 17, 2009 and December 31, 2009 and phases-out for taxpayer's with AGI exceeding $125,000 ($250,000 for joint returns).
- Alternative minimum tax (AMT) patch. To hold the number of taxpayers subject to the AMT at bay, the AMT exemption amounts for 2009 are $46,700 for individuals, $70,950 for joint returns, and $35,475 for married persons filing separately
- Extension of bonus depreciation. The Legislation extends 2008's bonus depreciation rules by permitting businesses to immediately deduct 50% of the cost of depreciable property acquired and placed in service for use in the United States during the current year
- Extension of enhanced small business expensing (Section 179). A taxpayer may elect to expense the cost of capital expenditures incurred up to $250,000
- Expanded loss carryback of net operating losses for small businesses. For 2008, the Act extends the maximum NOL carryback period from two years to five years for small businesses with gross receipts of $15 million or less
- Delayed recognition of certain cancellation of debt income. Businesses may recognize cancellation of debt income ("CODI") over 10 years (defer tax on CODI for the first four or five years and recognize this income ratably over the following five tax years) for specified types of business debt repurchased by the business in 2009 or 2010
- Qualified small business stock. The Act increases the exclusion for gain from the sale of certain small business stock held for more than five years from 50% to 75% for stock issued after the enactment date and before 2011.
- S corp holding period. The holding period of assets subject to the built-in gains tax is temporarily shortened from 10 years to seven years.

We hope this information is helpful. If you would like more details about this or any other aspect of the Stimulus Act, please do not hesitate to call a member of our team.

Individual Retirement Accounts - Relief for Required Minimum Distributions and Additional Planning Opportunities with IRAs

On December 23, 2008 former President George Bush signed into law the Worker, Retiree, and Employer Recovery Act of 2008 (H.R. 7327). Pursuant to this Act, the required minimum distributions for the 2009 tax year were suspended. What this means is that taxpayers otherwise required to take distributions from their qualified plan accounts, including individual retirement accounts and defined contribution plans, can forego taking such distribution in 2009. However, for participants who attained the age of 70 in 2008, the 2008 required minimum distribution must be taken, although the deadline for taking such distribution has been extended to April 1, 2009. Thus, to the extent that participants do not need to take distributions from a qualified plan account, the full amount of which is taxable as ordinary income, participants should take advantage of this relief and forego taking a distribution from their qualified plan accounts in 2009.

Another benefit that this Act provides to taxpayers with qualified plan accounts is the greater ability to convert existing individual retirement accounts to Roth IRAs. First, with no required minimum distributions in 2009, the full balance of a participant's account may be converted to a Roth IRA, as required minimum distributions are not eligible for roll-over contributions to a Roth IRA. Next, taxpayer's with Adjusted Gross Income (AGI) of $100,000 or less are eligible to covert their traditional plan account to a Roth IRA. For conversion purposes, a taxpayer's distribution from their plan account is excluded, such that only income from other, sources is considered for the AGI limitations. Taxpayers' whose filing status is "married filing separately" are not eligible for the rollover. If you are considering converting a traditional IRA into a Roth IRA, you should be aware that the balance in the traditional plan account that is converted will be included in taxable income in the year of conversion (to the extent that the account balance reflects previously deducted contributions) and thus subject to income tax at ordinary income tax rates. However, for conversions occurring in 2010, the resulting income tax is payable over two tax years. Thus, for taxpayer's who qualify for the rollover conversion, you should consider the future tax benefits of exchanging a fully taxable traditional IRA for a Roth IRA, the distributions from which are not considered taxable income. With potentially historically low account values and anticipated higher income tax rates, this could present a great opportunity for permanent future tax savings.