



TROVENA newsletter

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Ease Pressure On Loved Ones With Tax-Free Gifts

Today's severe economic crisis is taking its toll on virtually every segment of the population. Young newlyweds are finding it difficult to set aside funds for the down payment on a home, despite the now lower prices. Middle-aged parents are struggling to make ends meet and still squirrel away cash for their children's college costs. And older workers and retirees have seen their nest eggs eroded by the recent stock market downturn.

If you've been fortunate (and foresighted) enough to escape major damage to your own finances, you may want to consider helping family members overcome economic hurdles. Providing tax-free gifts could improve their situations while benefiting your own estate planning as well. If you stay within tax law boundaries, you don't have to pay gift tax on cash or property transferred to relatives or any other recipient. At the same time, the gifts will reduce the size of your taxable estate.

The value of the latter benefit depends on the future of the federal estate tax, which remains uncertain. The estate of an individual who dies in 2009 can shelter up to \$3.5 million of assets from federal estate tax. That's an increase from a \$2 million exemption in 2008, as stipulated by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), which calls for the outright repeal of the estate tax in 2010. But that provision of the legislation expires at the end of 2010, and in 2011, pre-EGTRRA rules return.

The estate tax exemption is scheduled to revert to just \$1 million, and the estate tax rate will rebound to 55% from the current 45% unless Congress acts to change the law.

While a legislative compromise on the estate tax is likely, the tax will almost certainly continue in some form. And that likelihood only increases the appeal of making gifts now to help loved ones hurt by the recession. In 2009 and 2010, you can provide tax-free gifts of as much

as \$13,000—in any combination of cash and property—to as many recipients as you choose. (A periodic inflation adjustment resulted in an increase in this exclusion amount from \$12,000 in 2008.) You don't even have to file any tax forms or otherwise inform the IRS about such gifts (if those are the only gifts made and unless gift splitting with a spouse is elected).

The chance to provide unlimited numbers of tax-free gifts could multiply the benefits not only for recipients but also to your estate plan. For instance, if you have two children and three grandchildren, giving each of them \$13,000 in 2010 adds up to a total of \$65,000. If your spouse also makes such gifts (or consents to a joint gift by filing a gift tax return), that exemption jumps to \$26,000 per relative and a total of \$130,000 for five, all without gift-tax consequences. Continue this gift-giving program for five years and you'll have cut the value of your estate by \$650,000 while providing generous assistance at a

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Designation Mania Fools Many, Few Act As Fiduciaries

The alphabet soup of professional credentials for advisors gets murkier by the month, making it more important than ever for investors to guard against deceptive designations.

No fewer than 88 professional designations are listed on the website of FINRA, the Financial Industry Regulatory Authority, including such titles as Certified Educator in Personal Finance, Certified Divorce Financial Analyst, and Chartered Advisor for Senior Living.

While many credentials are legitimate, some issuing organizations make very few demands on applicants. For instance, becoming a "Certified Senior Advisor" entails only taking a three-day course and passing a multiple-choice exam.

Don't put your faith in a professional designation without checking out what's required to earn it. The most credible designations, including Certified Financial Planner™ (CFP®), Certified Financial Analyst® (CFA®), and Certified Public Accountant (CPA), have strict ongoing continuing education requirements and codes of ethics.

Choosing a fiduciary advisor is also important. As fiduciaries, we must disclose and avoid conflicts of interest, and we are legally obligated to put your interests first. Our recommendations must be ideal for you, rather than "suitable," which is the standard for non-fiduciary advisors.

Cordially,

Christopher Van Slyke, CFP®
Scott Leonard, CFP®
Managing Partners

Do You Really Need That Inheritance?

Sometimes it pays just to say “no thanks” to a generous bequest—even from your own spouse. There may be estate planning benefits to having the assets go directly to contingent beneficiaries named by the decedent. If those beneficiaries are your children, this strategy could help them keep more of the bequest.

Officially declining an inheritance involves executing a legal document known as a “qualified disclaimer.” This refusal, which can apply to all or part of a bequest, must be executed within nine months of the donor’s death and before you’ve received any income from the inheritance. While this is generally a reactive measure, similar results can be obtained setting up a disclaimer trust as part of your estate plan.

One factor in deciding whether to refuse an inheritance is the uncertain future of the federal estate tax. Repealed for 2010, it will be revived in 2011 under unfavorable conditions.

The amount of an estate that’s exempt from federal tax, which was gradually increased to \$3.5 million for those who died in 2009, will drop back to \$1 million for 2011, unless Congress enacts new legislation.

Also, after gradually being

reduced to 45%, the top estate tax rate will return to 55%. The Obama administration and Congress will likely adjust the rules or change the timetable, but most experts expect the estate tax to continue to exist in some form. A qualified disclaimer or a disclaimer trust could help you prepare for whatever comes.



Suppose that under your current will, all of your assets are to go to your spouse if you die first, and vice versa. Then, at the death of the surviving spouse, the remaining

assets will be divided among your children. With this arrangement, there’s no estate tax due after the first death—because a spouse can inherit an unlimited amount tax free—and the surviving spouse’s estate can be reduced, for tax purposes, by whatever individual exemption is in effect at the time.

But this wastes the exemption of the first spouse to die. Instead, the surviving spouse could disclaim an amount equal to the estate tax exemption, passing it directly to contingent beneficiaries. The first spouse’s exemption relieves the heirs of any current estate tax liability, and later the surviving spouse’s own exemption can be used.

Before disclaiming any assets, one’s current and future potential need for the disclaimed assets needs to be carefully analyzed by a financial planner, since this is an irrevocable decision. We can work with you and your attorney to consider whether turning down an inheritance might make sense for you, and help you follow the rules that govern the process.

Also, if your net worth nears or exceeds federal estate tax exemption limits, we can discuss how setting up a disclaimer trust now can benefit your heirs. ●

Be Charitable Without Cutting Inheritance

With the uncertainty of future estate tax laws, you may be understandably reluctant to lock yourself into long-term wealth transfer strategies. But some estate planning moves do more than slice your tax bill. With a charitable remainder trust (CRT), for example, you get the satisfaction of supporting a favorite philanthropy. You also stand to save a lot on income taxes. And you can make sure your heirs won’t lose out, either.

A CRT is relatively simple. You start with an irrevocable transfer of assets into the trust. Ideally, you should contribute an appreciated asset—stock

or real estate, for example, that would generate a taxable capital gain if it were sold outside the CRT. With a CRT, you don’t have to pay for those gains. Just keep in mind that irrevocable means just that. These assets aren’t coming back.

A trustee you appoint—an institution or an individual—controls the assets, and under the terms of the trust, you or other beneficiaries receive regular income. After 20 years, the maximum term allowed by the IRS, or upon the death of the last remaining beneficiary—whichever comes first—the trust assets go to the charity you selected. During your lifetime, you can

change the designated charity. You can also specify how it is to use the donation.

Suppose you and your spouse own real estate purchased two decades ago for \$200,000. You transfer the property, now worth \$1 million, into a CRT. The trust sells the property, invests the proceeds, and pays you and your spouse 8% (\$80,000) in annual income.

Your tax benefits include:

- Eliminated capital gains tax. As long as the appreciated assets are transferred to the CRT, a tax-exempt entity, before being sold, you don’t have to pay taxes on capital gains.

- An income tax deduction for

The Real Rules On Charitable Deductions

Cleaning out your closet could be a great way to cut your tax bill and be philanthropic at the same time. If you itemize deductions, you can write off charitable contributions of as much as 50% of this year's adjusted gross income, and if you exceed that amount, you can carry over the remainder for future tax years. You get the same benefits as an owner of a partnership, limited liability company, or S corporation when the business donates property to eligible charities. And a C corporation can take charitable deductions on its own tax return.

Still, Internal Revenue Service rules governing gifts of tangible personal property—anything you can see, touch, or feel, excluding land or a building—are complex, as a reading of Publication 526 quickly reveals. And you must keep copious records. With the IRS expanding its staff of auditors, it's important to know the requirements and follow them carefully.

The size of your deduction depends on myriad factors, such as whether the donated property is worth less now than when new—usually the case for a late model used car, for example, and most clothing. With such gifts, you can generally deduct the item's fair market value, or street value. Websites like autos.yahoo.com

can help you approximate what a car is worth, taking into account its age and condition; for clothing, the fair market price might be what you'd get selling to a thrift shop. For donations of household items, a deduction is allowed only if the item is in good condition.

When you give away non-business property that has appreciated, you may deduct its fair market value as long as you have owned the property for more than a year and the charity anticipates using it in a way related to its tax-exempt purpose. For instance, you qualify if an art museum accepts your artwork and agrees to display it. A big advantage of giving away appreciated collectibles such as fine art, vintage wines, and guitars signed by the Beatles, is that your profit from selling them would be taxed at 28%. That's almost double the 15% rate that applies to most capital gains.

You won't make out nearly as well with gifts of appreciated business property or if the charity plans to sell your donation. In such instances, you can usually deduct only the asset's basis. For business property, such as outdated computers, that's the original cost minus depreciation write-offs you've taken. For personal assets you've inherited, it's what the gift is worth on the day the executor values

the estate—either the date of death or six months later. For a gift you've received, the basis is what the original owner paid. So if your great aunt gives you a white mink coat she bought in 1958 for \$250, that's all you're entitled to deduct if you donate the fur for auction at a church fair, even if the coat fetches more.

For every non-cash gift, you'll need a receipt or acknowledgment from the charity showing the date and location of the donation and a reasonably-detailed description of the gift. For gifts of \$250 or more, the charity's written acknowledgment must also say whether you received goods or services in return.

With greater IRS scrutiny of high-income returns likely, it's wise to heed these rules

In addition, you must keep your own written records, including the terms of any conditions attached to your gift and how you figured your deduction. Deductions of more than \$500 require you to substantiate how and when you obtained the donated property, and your basis in it. If that's not available, you must explain why in an attachment to your tax return in order to get the deduction.

If you deduct more than \$5,000 for a single donated item or group of similar items, such as a coin collection, you'll need a written appraisal and the qualified appraiser's signature on IRS Form 8283, which you must file with your tax return. Someone from the organization that received your gift must also sign the form and indicate whether the charity intends to put the property to an unrelated use.

So give, and your magnanimity will be rewarded—as long as you keep good records and don't overestimate the value of your generosity. ●

making a charitable donation. The amount of the deduction depends on the present value of the future gift, the ages of you and your spouse, prevailing interest rates, the type of charity, the amount of income you receive, the kind of gift, and the trust's terms.



- No estate tax. If you'd left your children the property instead, they might owe up to 45% of its value (based on the estate tax law for decedents dying in 2009).

Of course, even a bequest reduced

by taxes would be more than your kids get from the CRT. To remedy that, use part of your current tax savings to purchase a \$1 million "second-to-die" life insurance policy with an irrevocable life insurance trust naming your children as beneficiaries. The cost depends on the ages of you and your spouse and other factors. Then, when you and your spouse are both gone, the kids receive \$1 million in tax-free proceeds and the charity receives the trust assets. And, chances are, you'll be fondly remembered. ●

Estate Planning For A Non-Citizen Spouse

With estate laws in flux, planning is especially difficult right now. But it is even more complex if you or your spouse isn't a U.S. citizen. Special measures may be needed to avoid a large estate tax bill.

Under the rules of the landmark 2001 tax cut, the top tax rate on inheritances has been gradually reduced from 55% to 45%, while the maximum amount that can be passed along exempt from estate taxes has risen, to \$3.5 million in 2009. The estate tax is scheduled to expire in 2010 but will be revived in 2011, with a top rate of 55% and an exemption of \$1 million.

Although Congress is expected to take action on a permanent fix for estate rules, no one knows exactly what will happen. The only thing that's reasonably certain is that there will continue to be an unlimited marital deduction. That has been a constant of estate law—that a spouse may inherit unlimited wealth without any estate tax liability.

But that rule doesn't apply if your spouse is not a U.S. citizen. Even

permanent U.S. residents don't qualify for the unlimited marital deduction; instead, they may owe estate tax on inherited assets that exceed the normal exemption for bequests to non-spouses. There are, however, a couple of ways for non-citizens to sidestep problems.

Reduce a taxable estate through lifetime gifts to a spouse. If the citizen spouse has substantially more wealth than the non-citizen, a series of gifts could shift the balance. Tax rules allow tax-free gifts to a non-citizen spouse of up to \$133,000 in 2009. (The amount is indexed for inflation.) This is a strategy you'll need to establish early, and it may work best as a complement to the second approach.

Establish a qualified domestic trust (QDOT). This trust lets a non-citizen spouse take advantage of the deceased spouse's assets without paying estate tax. All trust income must be paid to the surviving spouse, and no estate tax is owed until the second

spouse dies and the remaining trust principal is distributed to heirs (usually the couple's children). To qualify for these advantages, the QDOT must meet these requirements.

- At least one trustee must be a U.S. citizen or a domestic corporation.
- The trust must be established no later than nine months after the first spouse's death.
- The executor must make an election for the QDOT on the deceased spouse's estate tax return.
- If QDOT assets exceed \$2 million, the

U.S. trustee must be a bank, or an individual trustee must furnish a bond or letter of credit equal to 65% of the value of trust assets.

If you or your spouse isn't a citizen, timely estate planning could be crucial. We can work with you and your attorney to make sure your estate plan takes that special circumstance into account and helps you avoid unnecessary taxes. ●



Tax-Free Gifts

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time when it may be sorely needed.

If the recipient is in a lower tax bracket, gifting shares of stock, mutual funds, or other assets that have appreciated will save you from paying capital gains taxes. But if you have assets with unrealized losses that you want to donate, it's better to sell them first so that you can deduct the loss on your tax return and give your gift in cash.

If you exceed the annual limit on tax-free gifts, you still won't necessarily owe money to the IRS. But larger gifts would count against your lifetime \$1 million gift-tax exemption, which might be put to better use in funding trusts or for other estate planning

purposes. Plus, you'll have to file a gift tax return—or potentially two gift tax returns if you're married.

Meanwhile, there are two special situations in which the normal giving limits don't apply. The first involves money you provide directly to an educational institution on behalf of a student. The second is for direct payments to health care providers.

The unlimited exemption for education payments means you won't owe gift tax if you cover college costs for children or grandchildren. Suppose your granddaughter is attending an Ivy League institution and the annual bill for tuition is \$50,000. You can pay that amount directly to the university and still give her an additional \$13,000 gift

(or \$26,000 with your spouse) that won't be subject to gift tax.

If children or grandchildren are still years away from college, an even better approach might be to fund a Section 529 college savings plan that names the child as beneficiary. Income earned by plan investments won't be taxed, and withdrawals to pay qualified educational expenses will also

be tax-free. Plus, a special provision allows five years' gifts to be sent to a 529 plan in one fell swoop. That means you and your spouse could immediately provide \$130,000 to jump-start a 529 plan without gift-tax consequences (provided you file a gift tax return to elect to front-load the gift). ●

