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**TAKING ADVANTAGE OF 2011-2012 ESTATE AND GIFT TAX
OPPORTUNITIES**

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(For reference purposes, there is a glossary of common
estate planning terms at the end of this outline.)

I. GENERAL CONCEPTS IN ESTATE PLANNING:

- A. For California, a Probate is required if the decedent has real property exceeding \$25,000 or total other assets exceeding \$100,000 in value that are not held in Trust, as Joint Tenants With Right of Survivorship, as Community Property With Right of Survivorship, with Beneficiary designation (Retirement Plan, Life Insurance), Payable on Death (bank accounts) or Transfer on Death (brokerage accounts). For assets under those value limits, property can be transferred by Declaration signed at least 40 days after death.

- B. For 2011 and 2012 the Federal Estate Tax Exclusion is \$5,000,000 of Net Estate (Total Assets reduced by debts, charitable deductions, marital deduction and administration costs) for an Individual and \$10,000,000 for a married couple. The exclusion is indexed for inflation after 2011, but the law providing those exclusions expires at the end of 2012. The tax rate on the Net Estate in excess of the exclusion is 35%. If no new law is enacted before 2013, the exclusion will revert to \$1,000,000 amount with tax rates up to 55% of the Net Estate over the exclusion. California only imposes an Estate Tax if the Federal Estate Tax allows a State Death Tax Credit. That is no longer the case, so California effectively does not have an Estate Tax.

- C. A new concept of "Portability" has been enacted for 2011 and 2012. This allows the Estate of the second spouse to die to use his/her \$5,000,000 exclusion plus the unused portion from the first spouse to die. To take advantage of this provision, a Federal Estate Tax Return needs to be filed in the first spouse to die's Estate.
- D. The lifetime gift tax exclusion has been increased to \$5,000,000 for 2011 and 2012. Thereafter it goes back to \$1,000,000 unless new legislation is enacted. The annual exclusion is \$13,000 for 2011 (no Federal Gift Tax Return required). Taxable gifts (in excess of the annual exclusion) reduce the Federal Estate Tax exclusion.
- E. Generation Skipping Transfer Tax is also at a \$5,000,000 exclusion for 2011 and 2012. Thereafter it is goes back to \$1,000,000 with inflation adjustments unless new legislation is enacted.
- F. Property owned by a decedent gets a new income tax basis equal to fair market value upon death. The entire community property owned (both spouses' portion) receives the new income tax basis. Unless the fair market value is less than the income tax basis at time of death, this is a big advantage because it eliminates capital gains tax on an immediate sale and it provides a new start for depreciation purposes of assets that can be depreciated for income tax purposes. This provision was in place prior to 2010 and is in place after 2010. It had limited application in 2010.
- G. An individual's or married couple's tax deductions for charitable donations to public charities is limited to 50% of their adjusted gross income for the tax year, with any unused amount carried forward for up to five years. A contribution to a private foundation is limited to 30% of adjusted gross income for the tax year, with any unused amount carried forward for up to five years. Unless tax is recognized on capital gain portion, gifts of certain appreciated capital gain property to a 50% charity is limited to a 30% of AGI deduction, and gifts of certain appreciated capital gain property to a 30% charity is limited to a 20% of AGI deduction, with the unused amount carried forward up to five years.

II. BASIC ESTATE PLANS – SOME EXAMPLES:

- A. Individual or Couple with total assets less than the Federal Estate Tax with intent to leave property outright to Beneficiaries.
 - 1. Title all assets "Payable on Death" for bank accounts, "Transfer on Death" for brokerage accounts and "Joint Tenancy With Right of Survivorship" for Real Property. (Do the later only if the proposed

Joint Tenant does not have any actual or potential creditor problems.) Designate beneficiaries for all retirement plans and life insurance.

2. Prepare a Will as a back up for anything not titled properly or the joint tenants die simultaneously.
 3. Prepare a Springing Durable Power of Attorney (effective upon incapacity) or Uniform Statutory Power of Attorney (effective immediately).
 4. Prepare an Advance Health Care Directive.
- B. Individual or Couple with real property and/or other assets where titling for immediate transfer on death is not appropriate (because of proposed Joint Tenants with real or potential creditor problems or Federal Estate Tax Liability that needs to be paid without allocation between beneficiaries or not all assets are to be distributed immediately).
1. Prepare Living Trust (Revocable Inter Vivos Trust Agreement) with A/B/C Sub-trusts for a Couple. Title all assets except retirement plans and life insurance into Trust.
 2. Prepare a Will (“Pour Over”) to transfer any assets accidentally or intentionally left out of Trust into the Trust.
 3. Prepare a Springing Durable Power of Attorney (effective upon incapacity) or Uniform Statutory Power of Attorney (effective immediately).
 4. Prepare an Advance Health Care Directive.
- C. A person owns Life Insurance (or a couple owns second to die policy) to pay Federal Estate Taxes on his/her/their Estate—Note that Life Insurance owned by a decedent is included in the decedent’s Estate for Federal Estate Tax purposes. Therefore the policy needs to be owned by and be under control of someone other than the decedent, or the policy will not be of full benefit because part of the proceeds will need to be used to pay Federal Estate Tax on the policy proceeds taxed in the decedent’s Estate.
1. Create an Irrevocable Life Insurance Trust to own policy. (Trust provisions prevent misusing the policy proceeds from intended purpose.)

2. Have the spouse own policy as separate property or have children own policy.
 3. Create a partnership of the children to own policy. (Partnership provisions prevent one or more of children misusing the policy proceeds from intended purpose.)
- D. A person owns Life Insurance to pay family expenses or mortgage on his/her death.
1. Have ownership in other than insured's name to maximize proceeds available for intended uses.
 2. Cost of Premiums can be gifted to owner of policy by insured.
- III. The provision that allowed a direct distribution from the Individual Retirement Account of a person to a charity has been reinstated for 2010 and 2011 only.
- A. The IRA owner must be at least 70-1/2 years of age.
 - B. The maximum amount of charitable contribution can be \$100,000.
 - C. The distribution counts as part of the Required Minimum Distribution for the year.
 - D. Use of this provision is a better income tax strategy than withdrawing the funds from the IRA into the owner's personal account and then making a charitable gift.
 1. This provision allows a lower Adjusted Gross Income, which increases the itemized medical deduction and the itemized miscellaneous deduction by lowering the floor the amounts must exceed.
 2. This provision allows the equivalent of a charitable deduction without the limitation of 50% of Adjusted Gross Income for the tax deduction.
 3. A lower income level means that the second subsequent year's Medicare deduction from Social Security benefits will not be impacted by the IRA withdrawal. (The Medicare amount is graduated based upon income.)
- IV. TRUSTS AND OTHER DONATION FORMS WITH PARTIAL OR ENTIRE INTEREST GOING TO CHARITY:

A. Pooled Income Fund (run by charity) – Factual Situation:

1. Donor has appreciated property that is not producing adequate income compared to other assets.
2. Donor would like income for fixed term or until death of donor or donor and spouse.
3. Donor does not want to administer trust fund holding investment.
4. Donor feels charity can do a good job of administering funds and wants charity to have remainder of funds on death. (Sometimes charity will allow part of proceeds to go to one or more additional charities upon death if Donor wants more than one charity to benefit.)
5. Donor gives property to charity's Pooled Income Fund. The Fund sells the property (and pays no tax because it is a charity). The Fund makes periodic payments to Donor.
6. Donor receives a charitable deduction for remainder interest in Fund that will go to charity upon termination of payments.

B. Charitable Gift Annuity (run by charity) – Factual Situation:

1. Donor has appreciated property and desires to benefit himself/herself or someone else (spouse, child, friend) with regular income.
2. Donor does not want to give property outright to Donee.
3. Donor feels charity can do a good job of administering funds and wants charity to have remainder of funds on death. (Sometimes charity will allow part of proceeds to go to one or more additional charities upon death.)
4. Donor gives property to charity, which creates a Trust for a Charitable Gift Annuity. The Trust sells the property (and pays no tax because it is a charity). The Trust makes periodic payments to the person(s) designated by the Donor.
5. Donor receives a charitable deduction for remainder interest in Trust that will go to charity upon termination of payments.

C. Charitable Remainder Trust (CRT run by Donor or designee)–Factual Situation:

1. Donor has appreciated property that is not producing adequate income compared to other assets.
2. Donor would like income for fixed term or until death of donor or donor and spouse.
3. Donor wants to administer or be able to designate administrator of trust fund holding investment.
4. Donor creates a CRT (either CRAT or CRUT) and gives property to that Trust. The Trust sells the property (and pays no tax because it is a charity). The Trust makes periodic payments to Donor and any other designated beneficiaries for a fixed term or until death.
5. Donor receives a charitable deduction for remainder interest in Trust that will go to charity upon termination of payments.

D. Charitable Lead Trust (CLT run by Donor or designee)–Factual Situation:

1. Donor has appreciated property that is not needed for income purposes.
2. Donor would like to benefit one or more charities with income for fixed term (e.g. 20 years).
3. Donor wants to administer or be able to designate administrator of trust fund holding property or proceeds from sale of property.
4. Donor creates a CLT (either CLAT or CLUT) and gives property to that Trust. The Trust keeps or sells the property (and pays no tax if it sells the property because it is a charity). The Trust makes periodic payments to the charity(ies). Upon expiration of the term, the Trust is terminated and the assets goes to the Donor's designated heirs.
5. Donor receives a charitable deduction for the present interest in Trust that will go to charity. The gift value to the designated heirs is minimized because it is valued as a remainder interest.

E. Charitable Foundation–Factual Situation:

1. Donor has appreciated property or other assets that are not needed for income tax purposes.
 2. Donor would like to benefit one or more charities annually, but wants to choose between various charities and amounts given to them.
 3. Donor may desire family participation in making decisions on charitable contributions to develop family culture of charitable giving.
 4. Donor wants to control the administration of the fund holding assets. Donor manages private foundation, although there are businesses that will do this for a fee.
 5. Donor creates a charitable private foundation and obtains tax-exempt status. The Donor then transfers the property to the foundation. The foundation sells the property (and pays no tax because it is a charity). The foundation makes payments to the charity(ies) designated by the Donor.
 6. Donor receives a charitable deduction for the value of the donation, but donation amount is limited to 30% of adjusted gross income because it is a private foundation.
- F. Donor Advised Fund (contribution to certain charities set up for this type of donation such as the Marin Community Foundation, Fidelity's Charitable Foundation or Schwab's Charitable Foundation)—Factual Situation:
1. Donor has appreciated property or other assets that are not needed for income purposes.
 2. Donor would like to benefit one or more charities annually, but wants to choose between various charities and amounts given to them.
 3. Donor may desire family participation in making decisions on charitable contributions to develop family culture of charitable giving.
 4. Donor does not want to administer fund holding assets.

5. Donor transfers the property to the charitable organization that sets up the Donor Advised Fund. The charity sells the property (and pays no tax because it is a charity). The Fund makes payments to the charity(ies) designated by the Donor.
6. Donor receives a charitable deduction for the value of the donation.

Estate Planning Glossary of Terms

Advance Health Care Directive A form created by the California Probate Code that is a medical Power of Attorney and sets forth the desires of the Principal regarding various lifetime and after death treatment.

Agent The person(s) you designate to represent you (make decisions) if you are unable or unwilling to represent yourself.

Annuity Regular payment of a fixed amount of money to a person. It may be for a fixed period of time or for the person's lifetime.

Attorney in Fact The Agent designated under a Power of Attorney.

Beneficiary The person(s)/entity(ies) entitled to receive income and or principal from a trust, probate estate, retirement plan, or life insurance. The California Probate Code defines "Beneficiary" to mean a person to whom a donative transfer of property is made or that person's successor in interest, and:

- (a) As it relates to the intestate estate of a decedent, means an heir.
- (b) As it relates to the testate estate of a decedent, means a devisee.
- (c) As it relates to a trust, means a person who has any present or future interest, vested or contingent.
- (d) As it relates to a charitable trust, includes any person entitled to enforce the trust.

Bequest A provision in a Will or Trust designating a specific person or persons who are to receive an asset designated in that document.

Charitable Lead Trust (CLT) The charity receives the income interest for a fixed number of years, and upon expiration of that term, non-charitable beneficiaries receive the balance of the trust. To receive a charitable deduction for the income interest donated, the donor must be taxable on that income interest under the Grantor Trust Rules and the income payment must use a guaranteed annuity or unitrust amount.

Charitable Remainder Trust (CRT) A trust set up to make current income distributions to one or more non-charitable income beneficiaries and to pay the remainder to a charity upon the expiration of the trust's term or death of the income

beneficiaries, which cannot be less than ten percent of the Trusts initial corpus. The donor can be Trustee.

Charitable Remainder Annuity Trust A form of CRT called a CRAT where the income beneficiary receives a fixed amount each year, which may not be less than five percent of the initial corpus.

Charitable Remainder UniTrust A form of CRT called a CRUT where the income beneficiary receives a fixed percentage of the Trust principal at the end of the prior year. The fixed percentage must be at least five percent.

Community Property A property rights structure followed by some states (including California) that gives a spouse a one-half interest in all property acquired by efforts of the other spouse after marriage and prior to separation. These provisions can be modified by an agreement of the spouses entered into prior or after marriage. Ownership of assets that use this form can add the provision “with right of survivorship” which allows transfer of the deceased spouse’s interest to the surviving spouse upon death of the first spouse without probate.

Conservatee A person who a Court finds incompetent to handle his/her own affairs and for whom a Conservator has been appointed.

Conservator A person appointed by a Court to manage the affairs (of the person and/or of the estate) of a person who a Court has found to be incompetent to handle his/her own affairs.

Contingent Subject to a condition that must occur before the event/act can happen.

Corpus See Principal, definition no. 2.

Custodian A person named to handle the funds of a minor (usually under the Uniform Transfer to Minor’s Act) or of an Individual Retirement Account (IRA).

Deed of Trust Document recorded to create encumbrance/lien that secures a mortgage from a lender

Devisee See Beneficiary.

Disclaimer The act of refusing to accept property transferred to a person by Will or Trust or other transfer document. To be effective for Federal Estate Tax purposes the disclaimer must be signed within nine months of the death of the decedent or time of proposed gift, and before the person receives any benefit from the transfer.

Donee Recipient of a gift.

<u>Donor</u>	A person or entity that makes a gift.
<u>Durable</u>	Used in connection with a Power of Attorney to mean an instrument that remains in effect even if the Principal becomes incapacitated.
<u>Estate</u>	(a) An interest in real property. (b) The assets of a decedent that are subject to probate. (c) The decedent’s assets subject to Estate Tax.
<u>Estate Tax</u>	A tax imposed on transfers from a decedent to the beneficiaries of his/her assets and interests deemed owned at death (such as: (1) property that has been gifted but where an interest is retained by the decedent until death; and (2) life insurance owned by the decedent on his/her own life). There are unlimited exclusions for transfer to spouse and to charities, and there is a lifetime exclusion that is set by statute and changes periodically.
<u>Executor</u>	The person(s) named in a Will to administer an Estate in probate.
<u>Fiduciary</u>	Somebody who is entrusted with the management of property or with the power to act on behalf of and for the benefit of another. The California Probate Code defines “Fiduciary” to mean a personal representative, trustee, guardian, conservator, attorney-in-fact under a power of attorney, custodian under the California Uniform Transfer to Minors Act or other legal representative subject to the Probate Code.
<u>Future Interest</u>	A right to property that is not available for immediate benefit or use, and will become available upon the occurrence of a designated future event.
<u>Generation Skipping Transfer Tax</u>	If a transfer is made to a “skip” generation (two or more generations below the transferor--such as grandchild), then a separate tax is imposed on the transfer. There is an exclusion amount which is not subject to the tax. Trusts that deal with these transfers have elaborate provisions to minimize the impact of the GSST.
<u>Gift Tax</u>	A tax imposed on transfers from the Donor to Donee during the donor’s lifetime of either a present or a future interest in property. There are numerous exclusions such as an annual exclusion amount for present gifts (where the Donee receives immediate benefit of the transfer), charitable gifts, unlimited transfers between spouses that are United States Citizens, and a lifetime exclusion. Gift Tax returns must be filed whenever the lifetime exclusion is utilized or exceeded. The Donee receives the lower of the Donor’s income tax basis or fair market value of the property as the Donee’s income tax basis in the property received. Transfers utilizing the lifetime exclusion are also reduced from the exclusion from Estate Tax and Generation Skipping Transfer Tax if applicable at the value of the property at the time of transfer. (Future appreciation after the gift is made is not reduced from the exclusion.)

<u>Grant Deed</u>	Formal document conveying real property from one party to another. There is an implied warranty of ownership. This conveys all present and future rights in the property of the Grantor to the Grantee.
<u>Grantee</u>	Somebody to whom something is transferred in a legal transaction. Generally it refers to a person receiving real property through a Grant Deed, Quit Claim Deed or other document.
<u>Grantor</u>	Somebody from whom something is transferred in a legal transaction. Generally it refers to a person transferring real property through a Grant Deed, Quit Claim Deed or other document. In some uses it means “Settlor”.
<u>Guardian</u>	A person appointed by a Court to handle the affairs of a minor (person under 18) if no parent is living, or when a parent is living if required because of some other legal rights being transferred to the child (e.g. a large personal injury award).
<u>Heir</u>	See Beneficiary.
<u>Inter Vivos Trust</u>	A trust created during lifetime, also called a “living trust”.
<u>Intestate Succession</u>	The method of distribution of property of a decedent that is not transferred by any other provision (Will, Trust, Beneficiary Designation, Joint Tenancy with Right of Survivorship, Community Property with Right of Survivorship, or Payable on Death account designation). Each state has its own method of intestate succession.
<u>Irrevocable Life Insurance Trust (ILIT)</u>	An irrevocable trust established to own a life insurance policy whose structure is designed to avoid having the policy included in the estate of the insured for Federal Estate Tax purposes.
<u>Issue</u>	Children or Grandchildren and all lineal descendants by birth or adoption.
<u>Joint Tenancy</u>	A form of ownership of property usually with “rights of survivorship” where the interest of a deceased joint tenant passes to the surviving joint tenant(s) without probate. It is assumed that each joint tenant has an equal interest in the property with the other joint tenant(s).
<u>Living Trust</u>	A trust established during a person’s lifetime. Also see Inter Vivos Trust.
<u>Pay on Death/Transfer on Death</u>	A designation added to title of certain assets (such as bank accounts for p.o.d. and security accounts for t.o.d.) that allows transfer upon death of the owner to a designated beneficiary without probate.
<u>Pooled Income Fund</u>	A Trust established to pay income to one or more non-charitable beneficiaries and the remainder going to a charity upon the expiration of

the term or death of the income beneficiaries. The charity must be Trustee. Generally there are multiple donors to the fund receiving benefits.

Power of Appointment The legal right to decide who will receive someone else's property. This is usually provided for in a Trust or Will.

Power of Attorney A legal document in which one person (Principal) authorizes someone else (Agent/Attorney in Fact) to act for the Principal. The terms and conditions under which the Agent/Attorney in Fact can act are set forth in the document.

Present Interest A right to property that is available for immediate benefit or use.

Principal

1. Someone for whom a representative ("Agent") acts for in a legal matter.
2. The assets in a Trust or investment. Also called "corpus".

Probate A Court proceeding in which the authenticity of the decedent's Will is established, an Executor or Administrator is appointed to administer the Estate during probate, debts of the decedent and taxes due are paid, the beneficiaries of the estate are identified, and the remaining assets of the estate are distributed to those beneficiaries.

Probate Code The California statutes that set forth the requirements of a Will, Trust, and forms of Power of Attorney. It provides the process for declaring a missing person as deceased, and probating a decedent's assets whether by Will or intestate succession. It sets forth the requirements and process for handling Guardianships and Conservatorships, administration of trusts, and gifts held by Custodians for minors.

QTIP (Qualified Terminable Interest Property) Trust A Trust for a spouse providing all income for life. It is designed to postpone payment of estate taxes until the death of the Donee spouse through use of the marital deduction for Federal Estate Tax purposes. It can only be used for U.S. Citizen spouses unless certain statutory provisions are met.

Quit Claim Deed Formal document conveying any interest of the Grantor in real property to the Grantee. There is no implied warranty of ownership. This conveys all the Grantor's present but not future rights in the property to the Grantee.

Rule Against Perpetuities Based upon the English Common Law, a legal doctrine followed by most states including California that limits the duration of a trust to the lesser of 99 years or 21 years after the death of a "life in being" at the time the trust is created. When that time period passes, the trust must be distributed. A trust that can extend beyond that time period because the state does not follow the rule against perpetuities is called a "dynasty trust".

<u>Settlor</u>	Creator of Trust.
<u>Springing</u>	Used in connection with a Power of Attorney to mean an instrument that becomes effective upon the incapacity of the Principal.
<u>Tenant in Common</u>	A form of ownership of property that allows each owner to transfer that ownership by sale, gift, Will or Trust and not go automatically to the other co-owners upon death.
<u>Trust</u>	Legal relationship between a Settlor, Trustee and Beneficiary. The trust may be created by a document called a Trust Agreement, or it may be imposed by law.
<u>Trustee</u>	Person administering a Trust, who has a fiduciary responsibility to the Settlor and Beneficiary.
<u>Trustor</u>	See “ Settlor ”
<u>Vested</u>	An indefeasible (absolute) interest in property.
<u>Will</u>	Document meeting specified legal requirements that sets forth a person’s last wishes. A “ Pour-Over Will ” places any items not specifically titled as Trust assets into Trust and it may identify specific bequests by power of appointment (from Trust). A “ Holographic Will ” means a Will that is entirely handwritten, dated and signed by the person (does not require witnesses), and only some states such as California recognize its validity. A “ Statutory Will ” is a form of Will set forth in the Probate Code that contains blank lines for completion and covers some basic situations of persons needing a Will.