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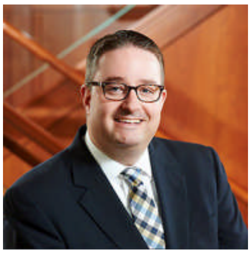

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Gifting Before the End of 2012

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The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (the "Act") became law in December 2010. The Act reinstated the federal estate and generation-skipping transfer taxes effective for decedent's dying and transfers made after December 31, 2009 and re-coupled the estate and gift tax exemptions for 2011 and 2012. The Act also increased the lifetime gift tax exemption to $5 million per person, which increased to $5.12 million per person for 2012 as a result of automatic inflation adjustments in the Act, and set the highest gift tax rate at 35% for transfers made after 2010 but before 2013.

Unfortunately, the compromise reached by Congress (and which culminated in the passage of the Act) only stays in place until **midnight on December 31, 2012**. Unless Congress acts to extend the provisions of the Act before the end of 2012, the gift tax rules in effect prior to 2001, which featured a $1 million lifetime gift tax exclusion with a top tax rate of 55%, will spring back into place. Therefore, for the balance of 2012 individuals with gifting in mind can take advantage of a **once-in-a-lifetime opportunity** to benefit their heirs at a reduced tax cost.

Generally, it is more tax efficient to make lifetime gifts than to pass assets at one's death, because the gift tax is tax-exclusive while the estate tax is tax-inclusive. For example, if we assume a flat 50% estate and gift tax rate, and you make a $4 million taxable gift during your lifetime, then you would pay $2 million of gift tax on the gift. Thus, you would have reduced your estate by a total of $6 million (1/3 to the federal government in the form of gift tax and 2/3 to the beneficiary of your gift). However, if you did not make the gift during your lifetime and died with the same $6 million, your estate would end up paying $3 million in estate tax, and your heirs would only receive the other $3 million. Therefore, while the rate of tax is the same you would pay more estate tax than gift tax, because the estate tax is tax-inclusive (you pay tax on the tax) while the gift tax is tax-exclusive (you do not pay tax on the tax), and leave less for your heirs.

There are a number of gifting strategies available to individuals who are willing and able to take advantage of them. Making low interest-rate loans to family members is a great way to transfer wealth from parents to children and grandchildren, because it enables the borrower to take advantage of interest rate arbitrage. Making gifts of appreciating assets and using one's $5.12 million lifetime gift tax exemption is also an excellent way to take advantage of the increased exemption, **but it may only be available until the end of 2012**.

About the Author: Mr. Fernandez focuses his practice on structuring and implementing estate and tax planning strategies for individuals and closely held businesses. His work includes assisting clients with all of the legal and tax aspects of the administration of decedent's estates. If you have any questions, please contact Mr. Fernandez (afernandez@wispearl.com) or one of the other attorneys in Wisler Pearlstine's Tax, Estate Planning and Administration Practice Groups.

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