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PRACTICAL PLANNER

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2012 PLANNING TIME CONCERNS

Summary: 2012 is the year of the estate plan. Here's some tips to make it really happen:

■ **If you snooze you lose**: Lots of folks have waited waaaay toooo long to address 2012 planning. Many are finding out the hard way that most good advisers are too booked to help 'em. But lots of folks that think they are well along the 2012 planning path are still asleep at the switch and haven't followed up on many critical and time sensitive components of what they (not their advisers) have to follow up on to get their deals done. 2012 is unparalleled in tax planning history. The hand holding your CPA, attorney, and wealth manager may have given you for planning in prior years just ain't happening this go-round. Everyone that is any good is really overwhelmed. Every pro will drop balls because there are so many flying. To get your planning completed, and to get it completed right, you have to follow up.

■ **It's Crunch Time**! OK Cap'n Crunch if you have 2012 gift planning still in the hopper, and you hope to complete it before year end, time is of the essence. The estate planning "machine" of local attorneys (e.g., who are needed for trusts in other states like Delaware), appraisers (real estate, business, discount, etc.), CPAs (e.g., cash flow projections which are essential for any note sale transaction or transfer of business interest), corporate counsel (essential to obtain lender, lease and other approvals and to draft the entity documentation essential to consummate a gift of an entity interest), trust companies (to review and approve trusts, serve in fiduciary capacities, open accounts), are all incredibly backlogged. Most appraisers and attorneys are no longer taking new matters for 2012. The closer we get to Auld Lang Syne the more this backlog will grow. It will become harder, if not impossible, to finish many 2012 transactions. Bob Keebler a smart well known CPA and retirement planning guru has expressed concern that those waiting too near year end to convert traditional IRAs to Roths may find that their requests won't get processed.

■ **Deadline May be Before Year End**: The election results, and President Obama's reiteration of his intent to have the wealthy bear more tax, has an ominous tone for anyone in the process of completing estate planning. No one knows what will happen in Washington. While it is possible that Congress will just kick the can down the road by extending the current estate tax regime, it is also possible that President Obama will push legislation through as part of addressing the fiscal cliff that will have a profound and negative impact on planning. Remember we got a new tax act in December 2010. Legislation to address the fiscal cliff could change the estate tax game rules before year end. Some provisions could be made effective as of the date of proposal, not enactment, which means you may lose the opportunity to implement a plan that is well underway. Sophisticated wealth transfers need to be completed ASAP. And many of the steps necessary are in your hands and are your responsibility. Speedy Gonzales gotta be your role model until New Years!

■ **Be Proactiv®**: Proactive is not just a zit cream. It's how you have to hustle to get your planning done this year. You must be personally proactive in pushing your advisory team (anyone and everyone involved in your planning) forward. You must make it a priority to personally set up meetings to sign documents, meet with advisers and push each phase of planning to conclusion. The volume of work everyone in the estate plan-

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CHECKLIST: POST-ELECT'N TIPS

Summary: President Obama has been reelected to a second term and has reiterated that he expects the wealthy to pay more income tax. Ordinary income tax rates may be raised by increasing the top two tax brackets to 36% and 39.6%. Capital gains tax rates increased for high-earners to 20%, plus the 3.8% surtax. The Republican position that rates should not be raised, even on the wealthiest taxpayers, might, to some extent depending on the shape of tax negotiations, morph into tighter restrictions on a range of deductions. Here's some planning tips to discuss with your CPA before year end.

√ **Medicare Tax**: In 2013, a 0.9% Medicare tax will be imposed on wages and self-employment income over $200,000 for singles and $250,000 for married couples and a 3.8% Medicare tax will apply to net investment income if your adjusted gross income (AGI) exceeds $200,000 single ($250,000 joint). Investment income derived as part of a trade or business is not subject to the new Medicare tax unless it results from investment of working capital. Discuss asset allocation decisions with your investment adviser, and business liquid holdings with your CPA. Trustees should review distribution policies with the

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ning machine is experiencing is unprecedented. There has never been a time in the history of the estate tax (no exaggeration) where you had to be more proactive, and more personally responsible, to assist and push your own planning to completion than now.

■ Steps to Consider: What must you do now to increase the likelihood that your 2012 planning will be completed? Ask your advisers what specific steps you can take, and review the points below and act immediately to the extent that these matters pertain to you. If you are not sure, call and/or email each adviser that may be involved.

■ Appointments: If you have a trust, shareholders agreement, deed or other legal document that has to be completed, call your estate, corporate, and real estate attorney, and schedule an appointment to review your documents, and a second appointment to sign. Get the key dates locked-in.

■ ID Numbers: If you have an entity that needs a tax identification number (EIN, TIN), call your CPA and get one assigned immediately as you will not be able to open a bank, brokerage or other account without it. Record the EIN on the front page of the document so that you'll have it available whenever needed.

■ Appraisals: If you have an appraisal that is in process, call your appraiser immediately and confirm a date that you will receive a valuation number. That figure is essential to your plan. Many 2012 estate plans have interrelated components. The appraisal you obtain will affect the value (percentage) of an entity or real property you hope to gift (or sell). This in turn affects what your corporate attorney must draft in entity documents and what your real estate attorney must draft on any deeds. Depending on the numbers, the structure of your transaction may have to change. If you're gifting close to the maximum $5.12M (or your remaining exemption), you may want to integrate a "defined value clause" into your planning. This is a mechanism used to minimize the fallout of an IRS challenge to the value of your gift. More complexity. Unless the excess value is paid over to a charity, its not particularly secure. More decisions, more documents, more complexity and not much time. You need to understand the options and the risks associated with each, and make a decision. Your estate planner can explain options for structuring these clauses (Wandry; excess to charity/private foundation, excess to QTIP or GRAT, etc.) but you have to make the call. To get the transfer done, you might defer receiving the full appraisal report until next year, and rely on a written letter providing just the valuation figures. There is some risk that if there is a change when the final report is completed a tax may be triggered. But that risk may well be worth taking because the options are so limited.

■ Approvals: Third party contractual approvals are essential for many transactions. You may not be permitted to transfer real estate, or an entity (e.g., LLC) that owns real estate, without lender approval. The loan docs for your business lines of credit may have covenants restricting transfers, dividends, and all sorts of stuff 2012 gift planning may violate. A tenant (e.g., an anchor tenant in a shopping center) may have rights to restrict your transfer of the ownership entity. If you have a franchise, the franchisor may have to approve any transfer. If you have not already obtained the necessary consents, you should have your corporate, real estate or other attorney address these issues on an urgent basis. Devise "Plan B" in case the approvals aren't received in time (gift cash to grantor trust now, swap in business later).

■ Securities: Open accounts with a check as an initial deposit before attempting to transfer securities. If you are transferring securities from one institution to another without having the same identity of accounts (e.g., you have stock at Bank A and want to transfer that stock to a trust in Trust Company X) you may encounter significant problems. Discuss the logistics and how to handle such transfers with the intended recipient institution now. Discuss the Patriot Act and "Know Your Customer" rules with your financial advisers. They can't short-cut regs. This due diligence stuff takes time. Call every financial institution involved in your planning to address these issues. PP

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...CHECKLIST: POST-ELECTION TAX TIPS

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trust's CPA as making distributions to beneficiaries under the tax threshold may save money.

√ Deductions: Analyze when to take deductions and losses. The usual rule to accelerate tax deductions and losses may not work. Because of possible tax increases the opposite approach might be best, but… If restrictions on deductions are enacted, then perhaps you should only defer deductions that aren't likely to be restricted. The reinstatement of the 3% AGI phase out of itemized deductions may also make many deductions of little value in 2013 regardless of other changes. The calculus of what to defer/accelerate is uncertain.

√ Harvesting Gains: Recognizing income, and harvesting capital gains, in 2012, before rate increases could be a smart move. Gift an existing installment note to a non-grantor trust and trigger the income tax at 2012's lower rates. Use derivative strategies and straddles to recognize gain in 2012. The straddle rules prevent you from taking a loss early, not from triggering gain early. Caution, the income triggered by gain harvesting in 2012 may impact the taxation of Social Security benefits for some. If you're elderly or terminally ill, gain harvesting may not make sense as it may be more advantageous to simply hold the securities until death and achieve a step up in income tax basis for heirs.

√ Depreciation: Bonus depreciation and Section 179 deductions are important to consider as you plan asset acquisitions near year end. If you plan to buy a new car, should you buy it now or in January 2013 when income tax rates are higher and when you may qualify for a Section 179 deduction?

√ Shifting Income: Income shifting to junior generations, and 2012 from 2013, may be advantageous. This should be considered when you make gifts, when trustees plan distributions from non-grantor trusts, etc. Family limited partnerships may morph into income shifting tools that they were before estate planners engineered FLPs into discount machines. If you can get paid this year instead of next, the income may be taxed at a lower rate. If you have a bond paying interest on January 1, sell that bond in December. The income will be taxed at 35% now, instead of at a 43.8% marginal tax rate in 2013. Sell bonds trading at a premium in 2012 when the premium is taxed at lower 15% capital gain rates. Repurchase the bond later. Asset location considerations should be evaluated. If the marginal tax rate on dividend paying stocks increases, it may prove advantageous to hold those stocks in qualified plans.

√ Roth Conversions: If you're converting your IRA into a Roth IRA, do it at today's lower rates. Generally, convert by asset class to take advantage of market volatility. Roth IRAs are not subject to the required minimum distribution (RMD) rules that regular IRAs are subject to at age 70.5 so they're groovier for doctors and others worried about asset protection. Beneficiaries can realize tax free withdrawals from Roth IRAs, but not from regular IRAs. From an estate tax planning perspective, funding a bypass or applicable exclusion trust with a Roth IRA is much more efficient since they are full dollars, whereas funding with a regular IRA is not only more complex but it underutilizes the benefit because the dollars involved are partial or pre-tax dollars. PP

RECENT DEVELOPMENTS

■Self-Settled Trusts: A recent Illinois case ruled unfavorably on the use of a self-settled trust. Rush Univ. Med. Center v. Sessions, ____ N.E. 2d ____, 2012 IL 112906, 2012 WL 4127261 (Ill, Sept. 20, 2012). Some have concluded that the use of a self-settled trust in a asset protection jurisdiction ("DAPT") for residents of non-DAPT jurisdictions is not viable. Others have pointed out that the result in Rush U was not unexpected in that it is consistent with prior bad fact cases attacking self-settled trusts. The reality is that before and after Rush U DAPTs were and remain unproven. Only after the Supreme Court rules on the application of the Full Faith and Credit clause of the Constitution as to whether a DAPT jurisdiction has to respect the judgment from the non-DAPT jurisdiction, will it be confirmed whether creditors can reach a DAPT, and hence whether transfers to a DAPT will be removed from your estate for a non-DAPT resident. The Court's evaluation of the use of self-settled trusts under the common law rule was supported by a number of Illinois cases. Marriage of Chapman, 297 Ill. App. 3d 611, 620 (1988), and Crane v. Illinois Merchants Trust Co., 238 Ill. App. 257 (1925). The court stated the common law rule as follows: "Traditional law is that if a settlor creates a trust for the settlor's own benefit and inserts a spendthrift clause, the clause is void as to the then-existing and future creditors, and creditors can reach the settlor's interest under the trust." The court noted that this conclusion did not require that the transfer be a fraudulent conveyance. Clearly the planning and implementation in the case was flawed. Holding real estate in Illinois, and having the grantor as a trustee and trustee protector was inadvisable. Perhaps restrictions can be incorporated into a self-settled trusts, e.g., that you cannot benefit unless you're not married, or that no distributions can be made to you until after ten years and a day after funding (to fall outside the period when a bankruptcy trustee can avoid a transfer to a self-settled trust), etc., may make the trust as not being self-settled if those events have not been triggered. PP

PRACTICAL PLANNER NEWSLETTER
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- Publications: Estate and Financial Planning for People Living with COPD available on Demos Health. All proceeds paid to the COPD Foundation. This book was written under the auspices of our charity www.chronicillnessplanning.org.
- Seminars: We're planning a 2013 chronic illness speaking tour—NJ to South Dakota. If your charity or professional organization along the way would like a presentation email us as we are developing an itinerary. Email shenkman@shenkmanlaw.com.

Creative solutions that coordinate all your planning goals:
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PLANNING POTPOURRI

■ We Weren't Standing on all 4 Paws: We got barked at about our pet trust article. Pet trust documents which are free standing have a much different set of laws than when pet trusts are formed under your will. Thanks to pet lawyer expert and friend Rachel Hirschfeld, Esq. http://www.PetTrustLawyer.com

■ Grantor to Grantor Trust Dies: The income on a grantor trust is taxed to you as grantor. If you sell assets to a grantor trust for a note no income is triggered because it's a grantor trust. What happens when you die? After your death it can't be a grantor trust. As a safety measure consider electing out of the installment sales method in the year of the grantor's death since there is no tax that year. Some might argue that you can't elect out of installment sale treatment since no sale occurred for income tax purposes. This might prevent the IRS from arguing that gain should be recognized in a later tax year when grantor trust status didn't apply. Thanks to Steven Siegel, Esq. Morristown, NJ.

■ GRAT and Defined Value Clause: Defined value clauses are a mechanism to limit the risk of an IRS audit adjustment on hard to value assets transferred to a trust. The approach is to have the excess value paid over to a non-taxable recipient. While case law has supported this when the excess is paid over to charity some tax experts believe that the excess can be paid over to a zeroed out grantor retained annuity trust. This raises issues. If the hard to value asset ends up in a GRAT as a result of an audit the term of the trust must be long enough that there will be liquidity to pay the annuity amount. If there is inadequate liquidity the annuity would have to be paid in kind. This might require an appraisal each year to make the payment. This would be costly. GRATs cannot receive additional contributions. An impermissible additional contribution will disqualify the GRAT. So the argument is that the transfer under the defined value clause is deemed effective the date of the formation of the GRAT and the sale (which is why they should be signed the same day). There is no assurance that the IRS will buy this. In choosing the GRAT term it might be advisable to have the GRAT term extend longer than the likely period during which an IRS audit might result in a valuation adjustment shifting assets into the GRAT. It would seem "odd" to have stock paid over to a GRAT that has already ended under its own terms. PP