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Insight

Wealth Management Commentary

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Saving Cinderella

Wealth transfer planning in the face of a looming deadline

Like the fairy tale princess Cinderella, whose carriage will turn back into a pumpkin at midnight, wealthy families are facing a looming deadline at year-end. When the clock strikes midnight on December 31st, the very favorable estate and gift tax laws of the last few years will disappear. Happily, though, the ball isn't over yet, and with some planning Cinderella can be saved.

The Pumpkin

For the past eleven years, the rules concerning the estate tax have been in a constant state of flux. During this period, the amount an individual can pass free of estate tax (the estate tax "exemption") has increased from $1 million, to $2 million, to $3.5 million, to an unlimited amount, and currently stands at $5.12 million. This year is no different. Without Congressional action, the current estate tax exemption of $5.12 million is slated to automatically revert to $1 million on January 1st. In addition to the drop in the exemption amount, the estate tax rate will increase from

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ASPIRIANT FEATURED AT WEALTH PLANNING CONFERENCE IN NYC

This year marks the 43rd Sidney Kess New York Estate, Tax & Financial Planning Conference sponsored by the UJA Federation. Jason Thomas, Aspiriant's Chief Investment Officer and Lisa Colletti, Director - Wealth Management, will join nationally recognized leaders in the wealth planning industry to discuss financial issues pertinent to this period of economic uncertainty. Their session, "Risk, Return & Retirement: Staying Strategic in the Face of Uncertainty" will outline ideas for motivating strategic action during trying times.

the current 35% rate to a whopping 55%, a double whammy that not only exposes more families to the estate tax, but also increases the amount of estate tax paid by all.

These changes were scheduled to kick in at the end of 2010; however, Congress acted at the last minute to extend the favorable estate tax regime for an additional two years. It is unclear whether Congress will do the same in 2012, and it's almost certain that nothing will occur prior to the upcoming election. As in 2010, when estate tax legislation was put in place on December 17th, it is possible that Congress may pass something very late this year, probably as part of larger legislation designed to avoid the highly publicized "fiscal cliff". Even if new legislation is passed prior to year end, it is unclear whether the exemption will be as generous as the current $5.12 million amount (the Obama administration has proposed a $3.5 million exemption).

While this backdrop creates many planning challenges, there are several different strategies for dealing with the uncertainty, which we highlight below. We're reaching out to clients this quarter to discuss planning strategies with those who'd like to take advantage of the current law. Many of these strategies require some lead time for execution, so it's important to begin these conversations soon.

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Saving Cinderella

The most straightforward way to lock in the high current estate tax exemption is to make a gift of the full $5.12 million prior to year-end. One can make gifts either outright or in trust. A trust must be irrevocable but does not need to give the intended beneficiary any immediate access to the assets. To the extent the gift is combined with other estate tax strategies, such as a "family limited partnership" or a "sale to a defective grantor trust", an individual can leverage the exemption to pass even more than $5.12 million out of their estate.

The problem with this simple strategy is that most clients either lack the appetite and/or cannot afford to irrevocably give away $5.12 million (or $10.24 million for a married couple) this year. Of course, one could give less than the $5.12 million maximum, but this doesn't maximize the opportunity that currently exists if Congress ultimately reduces the lifetime exemption amount.

Given the important question of affordability, many people are choosing to forego the potential advantage of making large gifts in 2012, at the risk of incurring a larger estate tax liability down the road. Fortunately, there are options for those who will *likely* have the financial ability to make large gifts to their children, but who don't want to irrevocably lose control of their assets just yet. In this situation, advanced techniques, including a "spousal access trust" or a "reverse defective grantor trust", enable people to take advantage of the current $5.12 million exemption while retaining some degree of access to the funds to support their own lifestyle expenses, if necessary.

A full description of these strategies is beyond the scope of this article, but your Aspiriant client service team can assist you with exploring them. Importantly, these sophisticated strategies take time to design and implement so anyone considering them should begin planning right away to ensure that the strategy is in place by year-end.

Happily ever after?

It's unclear how the estate tax environment will change in the coming months; however, it is clear that opportunities do exist to lock in the current exemption regardless of what happens in the future. Whether utilizing such strategies today is appropriate depends upon each client's unique financial resources and goals. As the clock nears midnight, we're eager to assist with developing a plan that's appropriate for you.

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