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YEAR-END PLANNING OPPORTUNITIES – DECEMBER 7, 2010

Dear Clients and Friends:

As 2010 draws to a close, it appears that there is finally an agreement in Washington to extend the Bush-era income tax rates. The latest word, as of the date of this letter, indicates that the income tax rates will likely be extended for two years for all taxpayers, including high-income earners. In addition, it appears that the estate tax exemption amount will be $5,000,000 for individuals dying in 2011 or 2012. The top estate tax rate would be 35%. Although not the subject of much of the current media coverage on the issue, it is likely that the estate tax exemption amount and rates will also apply to the generation-skipping transfer ("GST") tax for transfers to grandchildren and other younger beneficiaries. At the moment, it does not appear that the gift tax will be re-unified with the estate tax. As a result, the $1 million gift tax exemption and the 35% tax rate is likely to remain in place, at least over the next two years.

As we learn more about the new law, we will be sure to provide a more complete discussion of the subject through alerts that we will post on our website (www.blairandpotts.com). We would encourage you to visit the site periodically for any updates. If you would like us to mail you a copy of any future alerts, please give us a call. In the meantime, we would welcome the opportunity to explore with you how the projected changes in the law might impact your plan.

The following tax and estate planning techniques remain worthy of discussion and your consideration.

Roth IRA Conversion. Traditionally, higher-income taxpayers were not allowed to convert their retirement accounts to Roth accounts, but beginning in 2010, income restrictions were abolished and any taxpayer may now convert his or her traditional retirement account into a Roth account. In order to convert to a Roth account, income tax must be paid on the converted funds. For conversions taking place in 2010, taxpayers may either pay the entire tax in 2010 or have 50% of the income taxed in 2011 and 50% taxed in 2012. If your personal income tax exposure were likely to increase for 2011 or 2012, it might be most beneficial to pay income tax now and avoid higher future tax rates.

There are several key differences between a traditional IRA and a Roth IRA, most notably the income tax treatment of the contributions and distributions, and the requirement to take withdrawals during your lifetime. With respect to a traditional IRA, contributions are deductible for income tax purposes (subject to numerous limitations) and the earnings and appreciation on such contributions are not subject to income taxes until a distribution is received. In contrast, a contribution to a Roth IRA is not deductible on your income tax return and you are not required to receive distributions during your lifetime. As a result, the assets of a Roth IRA can continue to grow tax-free during your lifetime. If you receive a timely distribution from a Roth IRA during your lifetime, it will not be subject to income taxes.

In addition, because the conversion may be undone anytime before year 2010 tax returns are due, a taxpayer has a safeguard if circumstances arise that would diminish the benefits of the conversion.

Annual Exclusion Gifts. There is still time to make your 2010 annual exclusion gifts before December ends. The 2010 annual gift tax exclusion amount is $13,000 per recipient, or $26,000 per recipient for married couples electing to split gifts. The $13,000 amount will remain the same for 2011. The annual exclusion amount for gifts to a non-citizen spouse is $134,000 in 2010 and will be increased to $136,000 in 2011. As a reminder, your annual exclusion gifts are in addition to your federal gift and estate tax exemptions, and therefore can be a very effective means for reducing your taxable estate without triggering any gift tax.

Trust Distributions to "Skip" Persons and Outright Gifts to Grandchildren. Trustees and beneficiaries of trusts that are not exempt from GST tax should be aware that distributions can be made to "skip" persons (usually the grandchildren or great-grandchildren of the trust's Grantor) in 2010 without the imposition of GST tax. The repeal is only effective in 2010, and beginning in 2011 distributions to "skip" persons may be subject to a high GST tax rate.

In addition, large outright gifts to grandchildren can also be made before year-end without the imposition of GST tax, assuming you are comfortable making outright gifts to your grandchildren. Please note, however, that this assumes that Congress will not retroactively impose the GST tax on transfers made in 2010.

Low-Interest Loans to Family Members. You can transfer significant value to family members during your lifetime without incurring any transfer tax liability by making loans utilizing the historically low Applicable Federal Rates ("AFR"). The AFRs are the lowest interest rates that may be charged without having a transaction characterized as a gift, and will be much lower than the interest rates charged by a bank or other lending institution. Now might be the right time to consider helping a younger family member take advantage of today's depressed real estate prices by acting as the family bank.

Grantor Retained Annuity Trusts. If you are interested in gifting much larger amounts to your children with little or no gift tax consequences, you may choose to create a Grantor Retained Annuity Trust ("GRAT"). This technique involves transferring property (i.e., stock, bonds, closely-held business interests, etc.) to a trust while retaining the right to receive an annuity for a specified term of years. The transfer to the trust is a taxable gift, but the value of the gift is reduced by your retained right to receive annuity payments. A GRAT may be drafted so that the value of your retained interest equals the entire value of the property contributed to the trust. This arrangement is commonly referred to as a "zeroed out" GRAT. In determining the value of your retained interest, the Internal Revenue Service requires that you use the AFR for the month in which the transfer is made. If you survive the GRAT term and the value of the trust's assets appreciates at a greater rate than the AFR, the excess appreciation will pass to your beneficiaries transfer tax-free.

Please note that over the course of the past year, several proposals have been introduced in Congress that would both prohibit "zeroed out" GRATs and also require longer GRAT terms (i.e., 10 years). These changes will limit the effectiveness of a GRAT as part of your estate plan. Clients considering a GRAT may choose to act immediately in order to take advantage of the current, more beneficial GRAT law. The December AFR for a GRAT is 1.8%, which is an historically low rate.

Charitable Giving. If you are considering giving a gift to charity, you may wish to consider creating a Charitable Lead Trust, a Charitable Remainder Trust or a Private Foundation. A Charitable Lead Trust provides for payments to charity for a term of years with the remainder to be paid to the non-charitable beneficiaries at the end of the term. A Charitable Remainder Trust would allow you to provide an income stream to a non-charitable beneficiary for a period of time with the remainder to be paid to charity. A Private Foundation would allow you to retain control over the gift and have a lasting impact on the community or on the charitable area of your choice. Some of the advantages of these techniques are (i) the fulfillment of your charitable goals, (ii) a current income tax charitable deduction, (iii) no capital gains tax upon the sale of the gifted property by the Charitable Trust or Private Foundation, and (iv) the removal of property from your estate for federal estate tax purposes.

It is worth noting that Congress is currently considering extending the "charitable rollover" that existed in 2009 for distributions in 2010 from an Individual Retirement Account made directly to a tax-exempt charity. Currently taxpayers do not have this option when making their 2010 charitable contributions. Of course, we will report back if the law is changed.

To learn more, please call us or visit our website at www.blairandpotts.com.

Happy Holidays!

Blair & Potts