BLUM

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To our clients and friends:

It is said that the only certainty in this life is change, and this year has been no exception! As 2012 wound down with the "fiscal cliff" looming, we all wondered what Congress would do next with regard to the tax laws. Our question was answered with the American Taxpayer Relief Act of 2012 ("ATRA"), which has provided some certainty about the tax laws going forward. The $5 million gift, estate, and GST exemptions are now permanent and indexed for inflation. In the pages to follow, you will find how ATRA impacts you, as well as our top ten post-fiscal cliff planning tips.

The year 2012 also brought The Blum Firm and its attorneys many exciting changes and personal and professional accomplishments!

Marvin Blum was named by *D Magazine* as one of the Best Lawyers in Dallas. To be nominated, Marvin's Dallas-area peers were asked "Which Dallas lawyers, of those whose work you have witnessed firsthand, would you rank among the current best?" Marvin's experience, integrity, and hard work continue to put Marvin and The Blum Firm in the spotlight.

Gary Post was named as a Fellow in the American College of Trust and Estate Counsel (ACTEC), a national organization of lawyers elected to membership by "demonstrating the highest level of integrity, commitment to the profession and experience as trust and estate counselors." We are proud of Gary for receiving this great honor!

Amy Ott was named to a two year term on the Board of Directors of the Fort Worth Chapter of the Texas Society of CPAs. Congratulations, Amy!

Marvin Blum and **Kent McMahan** were recognized as 2012 Five Star Wealth Managers by *Texas Monthly* magazine.

Texas Monthly magazine also named **Marvin Blum, John Hunter, Gary Post, Kent McMahan,** and **Laurel Stephenson** as 2012 Super Lawyers! Marvin was named one of the Top 100 Super Lawyers in the State of Texas, while Marvin and Kent were both listed as Top 100 Super Lawyers in the Dallas/Fort Worth area. Marvin, Gary, Kent, and Laurel were recognized in the area of Estate Planning & Probate law, and John was recognized in the area of Tax law.

Steve Novak and **Amanda Holliday** were named as 2013 Rising Star Super Lawyers by *Texas Monthly* magazine, both in the area of Estate Planning & Probate.

Fort Worth, Texas magazine recognized ten of our attorneys as Top Attorneys. **Marvin Blum, Gary Post, John Hunter, Amanda Holliday, Cathy Moon, Laura Haley, Amy Ott, Rachel Saltsman,** and **Kandice Killion** were designated as Top Attorneys in the area of Probate, Estates, and Trusts. Marvin, John, and **Len Woodard** were designated as Top Attorneys in the area of Tax. Len was also recognized in the area of Corporate Finance/Mergers & Acquisition.

Marvin Blum joined the editorial advisory committee of *Trusts & Estates* magazine, a national publication for wealth management professionals serving the needs of high-net worth families, business owners, family offices, charitably inclined individuals, and non-profit corporations.

We were excited to have **Lora Davis** join our firm as a partner in the Dallas office. After practicing as a CPA for eight years, Lora graduated from SMU School of Law, magna cum laude. She is also Board Certified in Estate Planning and Probate Law. Lora clerked for a federal judge and spent fourteen years with Hughes and Luce prior to joining The Blum Firm. She has also served as President of the Dallas Estate Planning Council and is currently Vice Chair of the Estate and Gift Tax Committee of the State Bar of Texas Tax Section. In her free time, Lora enjoys spending time with her husband and twin teenaged boys.

Another great addition to our firm was **Julie Plemons**, who joined the Fort Worth office. Julie graduated with Honors from the University of Texas Law School in May of 2008 and received her LL.M. in Taxation from SMU School of Law in May of 2012. She graduated from Rice University with a Bachelor of Arts in Mathematical Economic Analysis. Prior to obtaining her LL.M., Julie worked for a law firm in Austin practicing in wills and estates, business structures, and tax. Julie grew up in Arlington and enjoys traveling, visiting art museums, hiking, and spending time with family and friends.

We also welcomed six new support staff members - **LaKresha Bates, Rebekah Iguaran, Tina Sepmoree, Mary Cooper, Michael Horan,** and **Scot Brown**. They have proven to be great additions to our firm!

Numbers to Know in 2013

Lifetime Gift Tax Exemption... $5,250,000
Estate Tax Exemption... $5,250,000
GST Tax Exemption... $5,250,000
Annual Gift Tax Exclusion... $14,000 per donee
Top Estate/Gift/GST Tax Rate... 40%

The *Fort Worth Business Press* recognized The Blum Firm as having the highest percentage of women attorneys in Tarrant County and ranking sixth in the overall number of women attorneys. We are pleased to be a trend-setter in promoting the careers of women attorneys.

As always, we appreciate the relationship we have with our friends and clients and look forward to serving you in the coming year. We wish you a happy and healthy 2013!

The Blum Firm, P.C.

Top Ten Post-Fiscal Cliff Planning Tips

The 2012 Tax Act: What You Need To Know

The American Tax Relief Act of 2012 ("ATRA") was signed into law on January 2, 2013. For the most part, ATRA makes permanent the gift and estate system that has been in place for the past two years. Below are some of the highlights of ATRA:

- TRANSFER TAX EXEMPTIONS - The gift, estate, and generation-skipping transfer ("GST") tax exemption amounts remain at $5 million per person. This amount is adjusted for inflation; in 2012 it was raised to $5.12 million, and it has been raised again in 2013 to $5.25 million. Those who utilized all of their exemptions via planning in 2012 now have an additional $130,000 of exemption to plan with this year.
- TRANSFER TAX RATES - The gift, estate, and GST tax rates have increased from a top rate of 35% in 2012 to a top rate of 40% in 2013.
- PORTABILITY - ATRA made the portability provisions of the 2010 law permanent. A surviving spouse may use the decedent spouse's unused estate tax exemption without relying upon a bypass trust. However, we still recommend that our clients do not rely upon this portability feature for several reasons, as discussed in more detail below.
- ROLLOVERS FROM INDIVIDUAL RETIREMENT ACCOUNTS TO CHARITIES - ATRA extended the charitable IRA rollover for 2012 and 2013. An individual who is $70\frac{1}{2}$ or over may make a distribution of $100,000 from his or her IRA directly to charity and have such distribution satisfy the MRD for that year.
- INCOME TAX CHANGES - ATRA raised the highest marginal rate for high-income taxpayers (single filers with AGI over $400,000 and joint filers with AGI over $450,000) from 35% to 39.6%. ATRA also raised the rate on qualified dividends and long-term capital gains for high-income taxpayers from 15% to 20%.

For those who raced to complete planning before the "fiscal cliff," rest assured that the planning you completed continues to be beneficial. If you gifted assets into trust, you removed the gifted amount plus appreciation on those assets from your estate as well as achieved asset protection for the assets gifted. For those of our clients who were unable to complete their planning before the end of 2012, now is an excellent time to do so.

With Portability, Do I Still Need A Bypass Trust?

With portability now permanent under ATRA, you may be wondering if having an estate plan that creates a separate trust to hold your exemption amount (a "bypass trust") for the surviving spouse is something you still need. The portability provisions allow a surviving spouse to use his or her deceased spouse's unused estate and gift tax exemption amount. For example, if you die owning $6 million but leave all of your assets to your spouse, then at your spouse's later death he or she will have $10.5 million of estate tax exemption available (his or her $5.25 million and your $5.25 million). In order to take advantage of this feature, each spouse's estate must file an estate tax return.

While leaving assets outright to a surviving spouse may be more simple, traditional bypass trust planning usually has more benefits, which include:

- Appreciation on assets held in a bypass trust escape estate tax at the surviving spouse's death;
- Assets retained in the bypass trust are protected from the surviving spouse's creditors;
- The deceased spouse can control how assets held in trust are disposed at the surviving spouse's death;
- Assets held in trust are more easily managed in the event of the surviving spouse's incapacity;
- The deceased spouse's remaining GST exemption can be allocated to the bypass trust to allow assets to pass to future generations free of tax; and
- Utilizing a bypass trust may eliminate the requirement to file an estate tax return for smaller estates.

These benefits would be lost if all assets were left outright to a surviving spouse. In addition, the surviving spouse's later remarriage could result in a loss of the ported exemption amount. If you have any questions about how the new portability provisions might impact your situation, please contact us for more information.

Short Course On the New 3.8% Investment Income Tax

Along with higher tax rates imposed by ATRA, an additional 3.8% tax on net investment income applies to certain taxpayers this year. Although called the "Medicare Surtax," the funds raised by the tax are not specifically allocated to the Medicare Trust Fund but are retained in the General Fund. This new tax (the net investment income or "NII" tax) is imposed on the net investment income of individuals whose total AGI exceeds $200,000 in the case of single taxpayers and $250,000 in the case of married taxpayers filing a joint return. The NII tax also applies to the undistributed net investment income of trusts and estates to the extent that AGI exceeds $11,950.

The types of investment income taxed generally include interest, dividends, royalties, rents, income from passive activities, and short and long term capital gains. Similar types of income allocated from pass-through entities, such as partnerships and limited liability companies, are also subject to the tax. Those affected by the additional tax should consider income tax planning to reduce or eliminate the impact of these taxes, such as:

- Investing in municipal bonds and other tax-exempt investments;
- Investing in tax deferred vehicles, such as retirement plans and life insurance;
- Using available tax deferral techniques when selling assets;
- Regrouping passive activities; and
- Making trust distributions to optimize marginal tax rates (keeping in mind the purposes of the trust).

Specific planning options will vary depending on your individual circumstances. Please contact us for more information on how this tax will affect you.

S Corporation Becomes The Entity Of Choice

Business owners take note — In 2013 there is only one entity choice if you want to avoid both self-employment tax AND the new 3.8% net investment income tax. As discussed above, the net investment income tax will apply to trade or business income in a passive activity. Taxpayers who actively participate (more than 500 hours/year) in their business will not be subject to the net investment income tax on the business profits but will remain subject to the self-employment tax UNLESS they operate in S corporate form. S corporation income is not subject to the self-employment tax. If you actively participate in a business that will generate significant income in 2013, we strongly encourage you to consider converting that business to an S corporation. The election for S corporation status must be made by March 15, 2013 to be effective for 2013. For example, if your business earns $1 million and you draw $250,000 as a salary and $750,000 as an S Corp distribution, you will save $28,000 per year by avoiding 3.8% payroll/NII tax on the S Corp distribution.

Elderly Parents And Adult Children Need Estate Plans Too

Often, elderly parents have an outdated or incomplete estate plan, or, worse, no estate plan at all. At the other end of the spectrum, children in their early adulthood often feel estate planning is not needed until the child has established a career, gotten married, started a family, or accumulated substantial assets, and thus also may not have an estate plan. Everyone who is over age 18 should have an estate plan.

At a minimum, the estate plan should include a Power of Attorney and Medical Power of Attorney (appointing individuals to make financial and medical decisions if your parent/child is unable), a HIPAA Authorization (allowing the release of medical information to named individuals), a Directive to Physicians (a/k/a "Living Will"), and a Will. Finally, if you have a parent who is looking to remarry in his or her later years, or if your child will potentially inherit assets, a pre-marital or post-marital agreement should be considered to protect separate property assets from becoming community property assets (which may become subject to division upon divorce or may pass to a surviving spouse).

If a parent or an adult child does not have an estate plan and something unforeseen happens, the process to have a guardian appointed to take care of his or her financial and personal needs, or the process to retitle assets upon death, will most likely be very difficult and expensive. Please contact us to discuss how we can assist your family members with their planning.

Conservation Easements: Protect Your Land While Reducing Taxes

As Texans, our land is often more than a financial asset, it is part of our history and our community. One of the most effective means to conserve and protect private property is a conservation easement. A conservation easement is a legally enforceable land preservation agreement between a landowner and either a nonprofit conservation organization or a government agency. By imposing a conservation easement on your land, you may be entitled to both a charitable income tax deduction and a reduction in the value of your estate for estate tax purposes. If you are interested in preserving your land and reducing taxes, we can help you determine whether a conservation easement is right for you.

Use a Captive Insurance Company To Manage Risks And Increase Wealth

A captive insurance company is an insurance company formed by the owners of a business to help manage insurable risks, and which can also provide income and estate tax benefits to the owners and their families. The business pays insurance premiums to the captive insurance company for insurance coverage, which is deductible by the business. If the annual premium is $1.2 million or less, the captive insurance company can avoid recognizing taxable income on the amount of the annual premium and the business can deduct the full amount. The captive insurance company can then enter into an arrangement with a reinsurer to pass on some of the risk to a third party insurer. The captive insurance company can be owned by a trust for the benefit of the business owner's family so that the increase in value of the captive insurance company occurs outside of the taxable estate.

If the business manages risks well and the captive insurance company is not required to use its assets to pay claims, the premiums paid by the business to the captive insurance company can be invested and continue to grow. At some point, the captive insurance company can pay out a dividend to its shareholders of surplus funds. If the shareholder is a trust that is not includable in the business owner's estate, the surplus funds will be protected from estate tax at the business owner's death. Contact us to discuss how you can take advantage of this structure.

Consider Funding Your Living Trust During Life

A Living Trust is often called a "will substitute." However, a Living Trust that is <u>funded during life</u> offers benefits that a conventional Will cannot provide. Those benefits include:

- a smooth transition of asset management authority in the event of incapacity — the successor trustee can manage your assets in that event;
- asset privacy at death — assets held in a Living Trust are not required to be listed on a probate inventory (which is public) at death;
- avoidance of an ancillary probate for out-of-state real property (or avoidance of probate altogether, if fully funded); and
- the enhanced possibility of a tax-free non-pro rata division of the community estate after the first spouse's death.

You must retitle assets into the name of the Living Trust for it to be funded. Merely signing a Living Trust does not fund it. Care should be taken to avoid nullifying any casualty insurance coverage or triggering an acceleration clause in a loan document. Please call us to discuss creating a Living Trust or funding your existing Living Trust.

Time May Be Running Out To Use Grantor Trusts

In 2012, President Obama's Administration published its revenue proposals (popularly referred to as the "Greenbook"). The Greenbook is essentially a "wish list" of fiscal policies that the President and the IRS would like to implement in the upcoming year. The 2012 Greenbook included several sweeping proposals which would affect grantor trusts.

Under the current laws, a grantor trust is an extremely popular estate planning tool that is structured so that the trust assets are not subject to estate tax at the creator's death, but the creator is obligated to pay the trust's income tax. This allows the grantor trust assets to grow outside of the creator's estate without being depleted by income taxes, and the payment of the income taxes by the creator is not treated as a gift to the grantor trust. As a result, grantor trusts can be used to shift significant wealth to future generations.

Under the 2012 Greenbook Proposals, (1) the assets of the grantor trust would be included in the gross estate of the creator for estate tax purposes, (2) distributions from the grantor trust during the life of the creator would be subject to gift tax, and (3) termination of the trust's status as a grantor trust during the creator's life would result in the entire value of the trust being subject to gift tax. For grantor trusts created under Section 678 of the Internal Revenue Code ("678 Trusts"), the beneficiary is deemed the grantor of the trust for income tax purposes, and the assets in the trust would be included in the beneficiary's estate upon his or her death. These changes should only apply to trusts created on or after the date that new laws are implemented by Congress. Although these ideas are not yet law, grantor trusts are on the President's and the IRS's radar, making it more important than ever to take advantage of this technique now.

Imagine There Is No Income Tax

Just like the Beatles song, Imagine there is no income tax... that you have a significant portion of your most valuable assets growing income tax free. Best of all, there would be no income tax even when you spend the assets. It would be similar to owning a very large Roth IRA, except we all know that there are limits on how much can go into an IRA. Did you know that you can have the same benefits with assets owned inside a life insurance policy? It's true. Under the Internal Revenue Code, the cash value of a life insurance policy can be invested in almost anything, even illiquid assets. Furthermore, several reputable insurance companies offer "private placement" life insurance contracts that will allow such investments. Call us if you would like to know more.

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Top Ten Post-Fiscal Cliff Planning Tips

Super Lawyers


MEET OUR 2012 SUPER LAWYERS

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M. LAUREL STEPHENSON, J.D.
Estate Planning
SUPER LAWYER ('12)

Texas lawyers were asked to nominate the best lawyers that they have *personally observed* in action. *Texas Monthly* magazine publishes the results and five of our lawyers were selected as SUPER LAWYERS, and two were selected as RISING STAR SUPER LAWYERS!


MEET OUR 2013 RISING STARS

STEVEN W. NOVAK, J.D.
Estate Planning
RISING STAR ('06 - '13)

AMANDA L. HOLLIDAY, J.D., C.P.A.
Estate Planning
RISING STAR ('08 - '13)

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Top Ten Post-Fiscal Cliff Planning Tips is provided by The Blum Firm, P.C. to provide current information about developments in tax and estate planning.