MECHANICS OF THE "CLAWBACK"
IS A $5,000,000 GIFT REALLY A $5,000,000 GIFT?

Presentation Hosted By
The Madison Group
March 2, 2011

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I. Introduction

A. The Tax Relief Unemployment Insurance Reauthorization and Job Creation Act of 2010 ("TRA") was enacted into law on December 17, 2010. To the surprise of many practitioners and commentators, §302(b) of TRA modified the gift tax regime for the years 2011 and 2012 by reducing the highest gift tax bracket to 35% and by increasing the gift tax applicable credit amount to $5,000,000. The TRA amendments to the gift tax regime, as well as to the estate tax and generation skipping transfer ("GST") tax regime, expire on December 31, 2012 (TRA §304); on January 1, 2013, the pre-TRA estate, gift and GST tax regime will again control (a 55% maximum gift and estate tax rate and a $1,000,000 applicable credit amount), unless Congress acts before then to change these rules.

B. In a vacuum, the TRA amendments to the gift tax regime permitting tax free gifts up to the $5,000,000 applicable credit amount, and imposing the reduced 35% maximum gift tax rate on gifts exceeding the applicable credit amount would seem to provide high net worth taxpayers with a tremendous opportunity to efficiently transfer wealth to or for the benefit of lower generation family members.

C. Unfortunately, 2011 and 2012 gift transactions cannot be made in a vacuum. §2001(b)(1)(B) (all code sections refer to the Internal Revenue Code) requires (and has always required) that adjusted taxable gifts be brought back into a decedent's estate as part of the estate tax calculation (this add-back calculation has been generically referred to as the "Clawback Rule"). There has been much confusion about whether the Clawback Rule will cause the tax benefits of 2011-2012 gifting transactions to be wiped out at a donor's death.

D. The second prong of the Clawback Rule, §2001(b)(2), which was amended by §302(d) of TRA, is the source of the confusion. Prior to the TRA amendment, §2001(b)(2) set forth a calculation intended to account for any differential between the marginal gift tax rate imposed for the year of the gift and a higher marginal estate tax rate imposed for the year of death. The TRA amendment added a new, second factor to the §2001(b)(2) equation, intended to account for any differential between the applicable credit amount available in the year of the gift and a lower applicable credit amount available in the year of death. Because the TRA rules are set to expire at the end of 2012, commencing in 2013, there is a possibility that a <u>higher</u> estate tax rate may be imposed as compared to the TRA gift tax rate, and that a <u>lower</u> estate tax applicable credit amount may be available as compared to the TRA gift tax applicable credit amount. These same disparities could occur if Congress acts prior to the expiration of the TRA rules by enacting a different tax regime, for example the regime in place in 2009 (45% top rate, $3,500,000 estate applicable credit amount).

E. As mentioned, the TRA amendments to §2001(b)(2) are set to expire on December 31, 2012, meaning that the pre-TRA provisions of §2001(b)(2) could return in 2013. If the pre-TRA version of §2001(b)(2) were to again become effective, then the TRA amendment intended to account for any difference between the date of gift applicable credit amount and the date of death applicable credit amount would expire. As was the case in 2010, commentators generally expect that Congress will act before December 31, 2012 to prevent a return to the pre-TRA gift and estate tax regime, but no one can reasonably predict an outcome at this point.

F. Thus arises a question of prime concern to practitioners: will adjustments under §2001(b)(2) in fact provide full credit at a donor's death for any differential between (a) tax rates where the maximum estate tax rate at donor's death is <u>higher</u> than the TRA gift tax rate, and (b) applicable credit amounts where the estate tax applicable credit amount at donor's death is <u>lower</u> than the TRA gift tax applicable credit amount?

G. The examples set forth below look at the mechanics of the Clawback Rule and its effect on 2011-2012 gift transactions.

II. <u>The Law</u>

A. The pre-TRA version of §2001(b), which is scheduled again became effective in 2013, states as follows:

> "(b) COMPUTATION OF TAX. - The tax imposed by this section shall be the amount equal to the excess (if any) of -
>
> (1) a tentative tax computed under subsection (c) on the sum of -
>
> (A) the amount of the taxable estate, and
>
> (B) the amount of the adjusted taxable gifts, over
>
> (2) the aggregate amount of tax which would have been payable under chapter 12 with respect to gifts made by the decedent after December 31, 1976, if the provisions of subsection (c) (as in effect at the decedent's death) had been applicable at the time of such gifts.
>
> For purposes of paragraph (1)(B), the term "adjusted taxable gifts" means the total amount of the taxable gifts (within the meaning of section 2503) made by the decedent after December 31, 1976, other than gifts which are includible in the gross estate of the decedent."

B. TRA §2001(b) and new subsection §2001(g) in place for 2011 and 2012, and as blacklined against the pre-TRA version of §2001(b) scheduled to again become effective in 2013, state as follows:

> "(b) COMPUTATION OF TAX. - The tax imposed by this section shall be the amount equal to the excess (if any) of -
>
> (1) a tentative tax computed under subsection (c) on the sum of -
>
> (A) the amount of the taxable estate, and
>
> (B) the amount of the adjusted taxable gifts, over

(2) the aggregate amount of tax which would have been payable under chapter 12 with respect to gifts made by the decedent after December 31, 1976, ~~if the provisions of subsection (c) (as in effect at the decedent's death)~~ if the modifications described in subsection (g) had been applicable at the time of such gifts.

For purposes of paragraph (1)(B), the term "adjusted taxable gifts" means the total amount of the taxable gifts (within the meaning of section 2503) made by the decedent after December 31, 1976, other than gifts which are includible in the gross estate of the decedent.

(g) MODIFICATIONS TO GIFT TAX PAYABLE TO REFLECT DIFFERENT TAX RATES. - For purposes of applying subsection (b)(2) with respect to 1 or more gifts, the rates of tax under subsection (c) in effect at the decedent's death shall, in lieu of the rates of tax in effect at the time of such gifts, be used both to compute -

(1) the tax imposed by chapter 12 with respect to such gifts, and

(2) the credit allowed against such tax under section 2505, including in computing -

(A) the applicable credit amount under section 2505(a)(1), and

(B) the sum of the amounts allowed as a credit for all preceding periods under section 2505(a)(2)" .

C. The philosophy behind §2001(b) has historically been two-fold.

1. First, §2001(b) is designed to ensure that a combined tax is imposed on a donor's lifetime gifts plus assets included in the donor's estate at death. The purpose of the combined tax calculation is to ensure that a donor's estate does not receive a duplicate benefit of the graduated gift and estate tax brackets. Adding adjusted gifts back into the taxable estate causes the tax rate imposed on the combined sum to be determined under a single graduated structure.

2. Second, the §2001(b) structure is designed to provide the estate with an offset for any gift taxes paid during a decedent's life. This calculation is a bit more complicated than merely subtracting the gift tax paid during life from the combined gift and estate tax amount calculated at death. If gift tax was paid during life at a rate lower than the rate imposed on the adjusted gifts added back into the estate, then to provide full credit for gift taxes paid, the gift taxes paid adjustment must be grossed up in the same manner as the tax on the adjusted gifts was grossed up due to the higher estate tax rate.

D. A new wrinkle has been introduced by TRA; not only may there be a difference in tax bracket rates to deal with under §2001(b), but now, for the first time, there may also be a difference created by a decrease between the applicable credit amount on the date of a gift ($5,000,000 for 2011 and 2012) and the date of death (for example, a scheduled $1,000,000 amount for 2013). Never before has the applicable credit differential been a factor; until 2011, the gift tax applicable credit amount was always lower than or equal to the estate tax applicable credit amount. The TRA amendment to §2001(b)(2) attempts to account for a possible variance in applicable credit amounts. But does the revised §2001(b) Clawback calculation really give full credit to a descendant's estate? The examples below examine this complex question.

III. Examples

A. As stated above, the following examples are intended to illustrate the mechanics of the Clawback Rule, both under TRA and pre-TRA law. These examples are not intended to suggest appropriate gifting strategies under the factual circumstances set forth; they are intended to illustrate the mechanics of the Clawback rules. Family considerations outside of the tax calculations are not analyzed.

1. **A owns $30,000,000 of assets; in 2011 A makes a gift of $10,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000. A dies in 2015 when the estate tax rate is 45%, the estate tax applicable credit amount is $3,500,000, and the TRA version of §2001(b) is retained (this example assumes Congress takes action prior to the expiration of the TRA rules); A's assets do not increase in value from 2011 to 2013.**

a. This example looks at whether the TRA §2001(b)(2) calculation gives full credit for differences in the marginal tax rates and applicable credit amounts for the year of gift and the year of death.

b. Gift tax calculation for a $10,000,000 gift made in 2011.

(i)	Tax on $10,000,000 $155,800 + 35% ($10M - 500,000)	$ 3,480,800
(ii)	§2505(a) credit $155,800 + 35% ($5M - 500,000)	(1,730,800)
(iii)	Gift tax paid	$ 1,750,000

(iv) Gift tax paid during life is "estate tax exclusive," meaning that the gift tax paid is never subjected to the estate tax (compare the estate tax, which is "inclusive", meaning that the gross estate is calculated without any reduction for estate tax paid). Thus, in this Example 1, the estate tax base will equal $28,250,000 which is equal to the original $30,000,000 of assets owned by A less the $1,750,000 gift tax paid.

(a) An important point to remember about the estate tax exclusive character of gift tax paid; if the donor dies within 3 years of the date of the gift, §2035(b) causes the amount of gift tax paid to be brought back into the donor's estate.

c. Analysis of the correct financial adjustment that should be made to offset the inclusion under §2001(b)(1) of adjusted gifts in the taxable estate.

(i) Estate tax calculation at A's death without the §2001(b)(2) offset.

(a) A's estate = \$30M - 10M (gift) - \$1,750,000 (gift tax paid)	\$18,250,000
(b) Tax on adjusted gift added back to estate under §2001(b)(1)(B) at 2013 date of death rate	
\$555,800 + 45% (\$10M - 1.5M)	\$ 4,380,800

(1) The philosophy of the adjusted gift inclusion under §2001(b)(1)(B) is to ensure that the gross estate is taxed at the higher marginal rates after first applying the graduated bracket structure to the adjusted gift amount.

(c) As reflected in (b) above, the 2013 date of death tax calculation against the 2011 adjusted taxable gifts exhausts the lower bracket rates. Thus the gross estate will be effectively taxed entirely at the highest 45% marginal rate.	
\$18,250,000 x 45%	8,212,500
(d) Tentative estate tax (again, ignoring the §2001(b)(2) adjustment)	\$12,593,300
(e) §2010(c) credit \$555,800 + 45% (\$3.5M - 1.5M)	(1,455,800)
(f) Estate tax payable without §2001(b)(2) adjustment	\$11,137,500

(ii) Financial adjustments that should be made to the estate tax calculation under (i) above to ensure that full credit is given for savings achieved by a 2011 35% gift tax rate and a 2011 \$5,000,000 gift tax applicable credit amount.

(a) <u>1st offset</u> - the actual amount of gift tax paid in 2011	1,750,000

(b) <u>2nd offset</u> - the difference in the tax calculation applicable to the adjusted taxable gift added back into the 2013 estate tax calculation and the actual tax calculation applicable to the gift in 2011.

2013:	$555,800 + 45% ($10M - 1.5M)	4,380,800	
2011:	$155,800 + 35% ($10M - 500,000)	(3,480,800)	900,000

(c) <u>3rd offset</u> - the difference in the applicable credit amount available for the actual 2011 gift and the applicable credit amount available for the 2013 estate.

2011:	$155,800 + 35% ($5M - 500,000)	1,730,800	
2013:	$555,800 + 45% ($3.5M - 1.5M)	(1,455,800)	
			275,000

(d) Amount of adjustment necessary to give full credit in 2013 for the difference in the 2011 gift tax rate and the 2011 gift tax applicable credit amount — $ 2,925,000

(e) Based on the foregoing, the §2011(b)(2) adjustment should provide a $2,925,000 offset to the estate tax calculation.

(1) Preliminary estate tax calculation (without §2001(b)(2) adjustment)	$11,137,500
(2) Adjustment that should apply under §2001(b)(2)	(2,925,000)
(3) Estate tax payable	$ 8,212,500

d. The following table compares the actual §2001(b) calculation under pre-TRA law and TRA.

Comparison			Pre-TRA Law	TRA Law
(1)	2011 gift tax paid on $10M gift at 35%			
	i)	Tax: $155,800 + 35% ($10M- 500,000)	$ 3,480,800	$ 3,480,800
	ii)	§2505(a) credit: $155,800 + 35% ($5M - 500,000)	(1,730,800)	(1,730,800)
	iii)	Gift tax paid	$ 1,750,000	$ 1,750,000
(2)	Value of estate			
	i)	$30M - 10M (gift) - 1,750,000 (gift tax)	$18,250,000	$18,250,000
(3)	A dies in 2013 (rate = 45%, credit amount = $3.5M)			
	i)	Gross estate	$18,250,000	$18,250,000
	ii)	Adjusted taxable gifts	10,000,000	10,000,000
	iii)	Tax base	$28,250,000	$28,250,000
	iv)	Tentative tax: $555,800 + 45% ($28,250,000 - 1.5M)	$12,593,300	$12,593,300
	v)	§2001(b)(2) adjustment		
		Pre-TRA: $555,800 + 45% ($10M - 1.5M) - 1,730,800*	(2,650,000)	
		TRA: $555,800 + 45% ($10M - 1.5M) - 1,455,800*		(2,925,000)
	vi)	Gross estate tax	$ 9,943,300	$ 9,668,300
	vii)	§2010(c) credit: $555,800 + 45% ($3.5M - 1.5M)	(1,455,800)	(1,455,800)
	viii)	Estate tax payable	$ 8,487,500	$ 8,212,500

*Arguably, the last entry in this equation accounting for the applicable credit amount will be limited to the tax amount calculated under the first part of the equation. Throughout these examples, the maximum applicable credit amount is used in these equations to better illustrate the difference between the TRA and the pre-TRA equations. This has no affect on the result of the equation.

e. TRA specifically amended §2001(b)(2) to provide an offset calculation for the <u>decrease</u> between the §2505(a) gift tax applicable credit amount (date of gift) and the §2010(c) estate tax applicable credit amount (date of death).

(i) The estate tax under the TRA calculation of $8,212,500 equals the proof calculation of $8,212,500.

(ii) The difference in tax between the pre-TRA calculation and the TRA calculation of $275,000 equals the proof offset amount for the applicable credit amount of $275,000.

(iii) From a practical standpoint, an adjustment for the applicable credit amount differential was never needed prior to 2011, because the gift tax applicable credit amount of $1,000,000 was always equal to or less than (but never higher than) the estate tax applicable credit amount.

(iv) Note the §2001(b)(2) pre-TRA calculations under the table above applies the gift tax rate for the year of death, but the applicable credit amount for the year of gift. As confirmation that this is the calculation intended by pre-TRA §2001(b)(2), the relevant worksheet of the pre-TRA 706 estate tax return is attached to this Article as Exhibit A (filled in to reflect the pre-TRA calculation).

2. **A owns $30,000,000 of assets; in 2011 A makes a gift of $10,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000. A dies in 2021 when the estate tax rate is 55%, the estate tax applicable credit amount is $1,000,000, and the pre-TRA version of §2001(b) applies (this example assumes Congress takes no action upon the expiration of the TRA rules); A's assets increase at the rate of 4% per year on an after tax basis from the 2011 year of gift to the 2021 year of death.**

a. This example looks at whether making a gift in 2011 taking advantage of the 35% rate and the $5,000,000 gift tax applicable credit amount will potentially provide an overall transfer tax savings in a worst case scenario where through Congressional inaction, the pre-TRA rules again become effective after 2012.

b. Estate tax calculation in 2021 under the facts of Example 2 where A makes a $10,000,000 gift in 2011.

(1)	2011 gift tax paid on $10M gift at 35%		
	i)	Tax: $155,800 + 35% ($10M - 500,000)	$3,480,800
	ii)	§2505(a) credit: $155,800 + 35% ($5M - 500,000)	(1,730,800)
	iii)	Gift tax paid	$1,750,000
(2)	Value of estate		
	i)	Current value in 2011: $30M - 10M (gift) - 1,750,000 (gift tax)	$18,250,000
	ii)	Future value in 2021 of $18,250,000 at 4% per year	$27,014,458
(3)	A dies in 2021 (rate = 55%, credit amount = $1M)		
	i)	Gross estate	$27,014,458
	ii)	Adjusted taxable gifts	10,000,000
	iii)	Tax base	$37,014,458
	iv)	Tentative tax: $1,290,800 + 55% ($37,014,458 - 3M)	19,998,752
	v)	§2001(b)(2) adjustment	
		Pre-TRA: $1,290,800 + 55% ($10M - 3M) - 1,730,800	(3,410,000)
	vi)	Gross estate tax	$16,588,752
	vii)	§2001(c)(2) phase out adjustment ($16,588,752 - 10M) x 5%	329,438
	viii)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	ix)	Estate tax payable	$16,572,390

(4)	Assets distributed from A's estate ($27,014,458 - 16,572,390)	$10,442,068
(5)	Future value of $10,000,000 gift over 10 years at 4% per year	14,802,443
(6)	Total assets from A to A's family	$25,244,511

c. In the alternative, and for purposes of comparison to the Example 2 structure, assume A makes no gifts in 2011.

(i)	Future value of $30,000,000 over 10 years at 4% per year	$44,407,329
(ii)	Estate tax paid at A's death	
-	$1,290,800 + 55% ($44,407,329 - 3M)	24,064,831
-	§2001(c)(2) phase out adjustment ($17,184,000 - 10M) x 5%	359,200
-	§2010(c) credit $345,804 + 41% ($1M - 1M)	(345,800)
-	Total estate tax	$24,078,231
(iii)	Assets distributed after A's death ($44,407,329 - 24,078,231)	$20,329,098

d. Compare assets distributed to family if A makes $10,000,000 gift in 2011 vs. if A holds all assets until death with no gifting.

(i)	Assets assuming 2011 gift	$25,244,511
(ii)	Assets assuming no 2011 gift	20,329,098
(iii)	Additional assets to family utilizing 2011 gift strategy	$ 4,915,413

e. The comparison under Example 2 compares apples to apples; a straightforward cash gift by A of $10,000,000 vs. retaining that same $10,000,000 in A's estate until death. The benefits of the 2011 gifting transaction (as compared to a hold assets until death strategy) will increase exponentially if a leveraged gifting strategy is implemented. For example, assume the same $10,000,000 gift is made as part of a sale of family limited partnership interests to an intentional grantor trust. The discounted values inherent in the family limited partnership interests, the potential growth factor of the transferred assets over the applicable AFR rate, and, perhaps most significant, the transferor's payment of all income tax accruing from income generated by the transferred assets, should both leverage the asset growth passing tax-free to lower generations and reduce the taxable estate of the transferor. Never before have practitioners had the opportunity to make use of a $5,000,000 lifetime applicable credit amount. Even if the pre-TRA regime returns in 2013 so that estate tax is paid on some portion of the gifted applicable credit amount, tremendous tax savings are possible because the tax is deferred until the donor's death.

3. **A owns $10,000,000 of assets; in 2011 A makes a gift of $5,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000; A dies in 2013 when the estate tax rate is 55%, the estate tax applicable credit amount is $1,000,000, and the pre-TRA version of §2001(b) is in place.**

a. Perhaps this example more than any other illustrates the benefits of taking advantage of the 2011-2012 gift tax applicable credit amount. This example looks at whether making a 2011 gift up to the $5,000,000 gift tax applicable credit amount will potentially provide an overall transfer tax savings if pre-TRA §2001(b) applies in the year of a donor's death. No gift tax is paid in 2011. At first glance, this would seem to negate any advantage under the pre-TRA §2001(b)(2) calculation; pre-TRA §2001(b)(2) only accounts for a difference between gift and estate tax rates and not a difference in gift and estate tax applicable credit amounts. In fact, there is a significant tax savings. The gift tax rate / estate tax rate difference is still part of the pre-TRA §2001(b)(2) calculation where gifts within the gift tax applicable credit amount are added back to the estate as adjusted gifts.

b. The following table compares the calculation under pre-TRA law of the gift transaction described in this example vs. a structure where A makes no gift in 2011.

			Example 1 Gift	Example 2 No Gift
(1)	2012 gift tax paid on $5,000,000 gift at 35%			
	i)	Tax: $155,800 + 35% ($5M - 500,000)	$ 1,730,800	$ 0
	ii)	§2505(a) credit: $155,800 + 35% ($5M - 500,000)	(1,730,800)	(0)
	iii)	Gift tax paid	$ 0	$ 0
(2)	Value of estate			
	i)	$10M - 5M (gift) - 0 (gift tax)	$ 5,000,000	$10,000,000
(3)	A dies in 2013 (rate = 55%, credit amount = $1M)			
	i)	Gross estate	$ 5,000,000	$10,000,000
	ii)	Adjusted taxable gifts	5,000,000	0
	iii)	Tax base	$10,000,000	$10,000,000
	iv)	Tentative tax		
		Gift: $1,290,800 + 55% ($10M - 3M)	$ 5,140,800	
		No Gift: $1,290,800 + 55% ($10M - 3M)		5,140,800

	v)	§2001(b)(2) adjustment (Gift)		
		Pre-TRA: $1,290,800 + 55% ($5M - 3M) - 1,730,800	(660,000)	
	vi)	Gross estate tax	$ 4,480,800	$ 5,140,800
	vii)	§2010(c) credit: $345,800 + 41% ($1 - 1M)	(345,800)	(345,800)
	viii)	Estate tax payable	$ 4,135,000	$ 4,795,000
(4)	Assets distributed from A's estate			
		Gift: $5,000,000 - 4,135,000	$ 865,000	
		No Gift: $10,000,000 - 4,795,000		$ 5,205,000
(5)	Add $5,000,000 gift from 2011		5,000,000	0
(6)	Total assets from A to A's family		$ 5,865,000	$ 5,205,000

4. **A owns $10,000,000 of assets and A's spouse B owns $5,000,000 of assets; in 2011 A makes a gift of $5,000,000 to A and B's children when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000; A dies in 2013 when the estate tax rate is 55%, the estate tax applicable credit amount is $1,000,000; and the pre-TRA version of §2001(b) is in place. Under A's estate plan, the amount within A's estate tax applicable credit amount is allocated to a Family Trust with the balance allocated to a QTIP Marital Trust. B dies in 2015 under an estate tax regime that is the same as 2013.**

a. This example looks at how the pre-TRA version of §2001(b) may affect marital deduction planning.

b. §2056(b)(4)(A) provides that to the extent the interest passing to the surviving spouse must share the economic burden of the estate taxes incurred by the deceased spouse's estate, the estate tax amount must diminish the marital deduction amount. This leads to a very complex calculation because the marital deduction amount and the estate tax amount are interrelated; neither can be determined without the other. Software has been developed to make this calculation, but until updates taking into account the $5,000,000 gift tax applicable credit amount for 2011 and 2012 are available, the software calculation won't be accurate. This leads back to pre-computer days, when these interrelated calculations were solved by mathematical equation. The Service issued IRS Publication 904, last updated in 1990 (the Publication is no longer issued), which set forth a series of examples which applied either a trial and error method or an algebraic equation method for solving these amounts.

c. Estate tax calculation in 2013 and 2015 under the facts of Example 4 where A makes a gift of $5,000,000 in 2011.

(1)	2011 gift tax paid on $5M gift at 35%		
	i)	Tax: $155,800 + 35% ($5M - 500,000)	$ 1,730,800
	ii)	§2505(a) credit: $155,800 + 35% ($5M - 500,000)	(1,730,800)
	iii)	Gift tax paid	$ 0

(2)	Value of A's estate		
	i)	$10M - 5M (gift)	$ 5,000,000
(3)	A dies in 2013 (rate = 55%, credit amount = $1M)		
	i)	Tentative taxable estate	$ 5,000,000
	ii)	§2056 marital deduction (calculated by algebraic equation as prescribed under IRS Publication 904)	(1,922,222)
	iii)	Tentative taxable estate	$ 3,077,778
	iv)	Adjusted taxable gifts	5,000,000
	v)	Tax base	$ 8,077,778
	vi)	Tentative tax: $1,290,800 + 55% ($8,077,778 - 3M)	$ 4,083,578
	vii)	§2001(b)(2) adjustment	
		Pre-TRA: $1,290,800 + 55% ($5M - 3M) - 1,730,800	(660,000)
	viii)	Gross estate tax	$ 3,423,578
	ix)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	x)	Estate tax payable	$ 3,077,778
(4)	Assets distributed from A's estate to A's QTIP trust ($5M - 3,077,778))		$ 1,922,222
(5)	B dies in 2015 (rate = 55%, credit amount = $1M)		
	i)	Gross estate	
		- B's assets	$ 5,000,000
		- A's QTIP trust	1,922,222
		- Gross estate	$ 6,922,222
	ii)	Gross estate tax: $1,290,800 + 55% ($6,922,222 - 3M)	$ 3,448,022
	iii)	§2010 credit: $345,800 + 41% ($1M - 1M)	(345,800)
	iv)	Estate tax payable	$ 3,102,222
(6)	Assets distributed from B's estate and A's QTIP trust: ($6,922,222 - 3,102,222)		$ 3,820,000
(7)	Total assets distributed to A and B's family		
	i)	A's 2011 gift	$ 5,000,000
	ii)	B's estate (including A's QTIP trust)	3,820,000
	iii)	Total assets	$ 8,820,000

d. In the alternative, and for purposes of comparison to the Example 4 structure, assume A makes no gift in 2011.

(1)	A dies in 2013 (rate = 55%, credit amount = $1M)		
	i)	Gross estate	$10,000,000
	ii)	§2506 marital deduction	(9,000,000)
	iii)	Tax base	$ 1,000,000
	iv)	Gross estate tax	
		$345,800 + 41% ($1M - 1M)	$ 345,800
	v)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	vi)	Estate tax payable	$ 0
	vii)	Assets distributed from A's estate	
		- to Family Trust	$ 1,000,000
		- to Marital Trust	9,000,000
		- Total assets distributed	$10,000,000
(2)	B dies in 2015 (rate = 55%, credit amount = $1M)		
	i)	Gross estate	
		- B's estate	$ 5,000,000
		- A's QTIP trust	9,000,000
		- Total gross estate	$14,000,000
	ii)	Tax base	$14,000,000
	iii)	Tentative tax: $1,290,800 + 55% ($14M - 3M)	$ 7,340,800
	iv)	§2001(c)(2) adjustment: ($14M - 10M) x 5%	200,000
	v)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	vi	Estate tax payable	$ 7,195,000
(3)	Assets distributed from B's estate and A's QTIP trust ($14M - 7,195,000)		$ 6,805,000
(4)	Total assets distributed to A's and B's family		
	i)	A's Family Trust	$ 1,000,000
	ii)	B's estate (including A's QTIP trust)	6,805,000
	iii)	Total assets	$ 7,805,000

e. Compare assets distributed to family if A makes $5,000,000 gift in 2011 vs. if A holds all assets until death with no gifting

(i)	Assets assuming A's 2011 gift	$ 8,820,000
(ii)	Assets assuming no gift	7,800,000
(iii)	Additional assets to family utilizing 2011 gift strategy	$ 1,015,000

f. The comparison under Example 4 shows an overall advantage to the 2011 gifting strategies where the donor dies with a Family Trust / Marital Trust estate plan in a year when the pre-TRA §2001(b) applies. Nevertheless, a portion of the estate tax payment is accelerated to the date of the first spouse's death as opposed to the no gift strategy where all estate taxes are paid at the death of the surviving spouse. There may be situations where the asset growth that would have accrued to the tax payment at the first spouse's death would offset the additional assets preserved through the gifting strategy. Also, changes in the estate tax laws after A's death could affect the results shown in Example 4.

g. If the TRA version of §2001(b) were to apply to the 2011 estate tax calculation for A's estate, then the algebraic equation of IRS Publication 904 would yield a result that gives full credit to A's $5,000,000 2011 gift so that the $5,000,000 retained by A at death will be protected by the §2056 marital deduction.

(1)	2011 gift tax paid on $5M gift at 35%		
	i)	Tax: $155,800 + 35% ($5M - 500,000)	$ 1,730,800
	ii)	§2505(a) credit: $155,800 + 35% ($5M - 500,000)	(1,730,800)
	iii)	Gift tax paid	$ 0
(2)	Value of A's estate		
	i)	$10M - 5M (gift)	$ 5,000,000
(3)	A dies in 2013 (rate = 55%, credit amount = $1M)		
	i)	Tentative taxable estate	$ 5,000,000
	ii)	§2056 marital deduction (calculated by algebraic equation as prescribed under IRS Publication 904)	(5,000,000)
	iii)	Tentative taxable estate	$ 0
	iv)	Adjusted taxable gifts	5,000,000
	v)	Tax base	$ 5,000,000
	vi)	Tentative tax: $1,290,800 + 55% ($5M - 3M)	$ 2,390,800
	vii)	§2001(b)(2) adjustment	
		TRA: $1,290,800 + 55% ($5M - 3M) - 345,800	(2,045,000)
	viii)	Gross estate tax	$ 345,800
	ix)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	x)	Estate tax payable	$ 0
(4)	Assets distributed from A's estate to A's QTIP trust		$ 5,000,000

(5) B dies in 2015 (rate = 55%, credit amount = $1M)

i)	Gross estate	
	- B's assets	$ 5,000,000
	- A's QTIP trust	5,000,000
	- Gross estate	$10,000,000
ii)	Gross estate tax: $1,290,800 + 55% ($10M - 3M)	5,140,800
iii)	§2010 credit: $345,800 + 41% ($1M - 1M)	(345,800)
iv)	Estate tax payable	$ 4,795,000

(6) Assets distributed from B's estate and A's QTIP trust: ($10M - 4,795,000) $ 5,205,000

(7) Total assets distributed to A and B's family

i)	A's 2011 gift	$ 5,000,000
ii)	B's estate (including A's QTIP trust)	5,205,000
iii)	Total assets	$10,205,000

5. **A owns $5,000,000 of assets; in 2011 A makes a gift of $2,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000; A dies in 2013 when the estate tax rate is 55%, the estate tax applicable credit amount is $1,000,000, and the TRA version of §2001(b) is retained (this example assumes Congress takes action to preserve the TRA version of §2001(b)).**

a. This example examines whether the TRA §2001(b)(2) calculation gives full credit for a difference in applicable credit amounts where the gift amount is less than the gift tax applicable credit amount but more than the date of death estate tax applicable credit amount. In other words, will the TRA §2001(b)(2) calculation preserve the benefit of the gift tax applicable credit amount where no gift tax was paid in the year of the gift?

b. The following table compares the actual §2001(b) calculation under pre-TRA law and TRA.

		Pre-TRA Law	TRA Law
(1)	2011 gift tax paid on $2M gift at 35%		
i)	Tax: $155,800 + 35% ($2M - 500,000)	$ 680,800	$ 680,800
ii)	§2505(a) credit: $155,800 + 35% ($2M - 500,000)	(680,800)	(680,800)
iii)	Gift tax paid	$ 0	$ 0
(2)	Value of estate		
i)	$5M - 2M (gift) - 0 (gift tax)	$ 3,000,000	$ 3,000,000

(3)	A dies in 2013 (rate = 55%, credit amount = $1M)		
i)	Gross estate	$ 3,000,000	$ 3,000,000
ii)	Adjusted taxable gifts	2,000,000	2,000,000
iii)	Tax base	$ 5,000,000	$ 5,000,000
iv)	Tentative tax: $1,290,800 + 55% ($5M - 3M)	2,390,800	2,390,800
v)	§2001(b)(2) adjustment		
	Pre-TRA: $780,800 + 49% ($2M - 2M) - 1,730,800	0	
	TRA: $780,800 + 49% ($2M - 2M) - 345,800		(435,000)
vi)	Gross estate tax	$ 2,390,800	$ 1,955,800
vii)	§2010(c) credit: $345,800 + 41% ($1 - 1M)	(345,800)	(345,800)
viii)	Estate tax payable	$ 2,045,000	$ 1,610,000

c. Proof regarding $435,000 §2001(b)(2) adjustment (see Example 1 for proof calculation discussion)

(i) <u>1st</u> offset - the actual amount of gift tax paid in 2011 $ 0

(ii) <u>2nd offset</u> - the difference in the tax calculation applicable to the adjusted taxable gift added back into the 2013 estate tax calculation and the actual rate tax calculation applicable to the gift in 2011. Although counterintuitive because no gift tax was actually paid, the offset for tax rate differential remains relevant because the tax is still technically charged; it is only not paid because it is offset by the §2505(a) credit.

2013:	$780,800 + 49% ($2M - 2M)	$780,800	
2011:	$155,800 + 35% ($2M - 500,000)	<u>(680,800)</u>	
			100,000

(iii) 3rd offset - the difference in the applicable credit amount available for the actual 2011 gift, and the applicable credit amount available for the 2013 estate.

2011:	\$155,800 + 35% (\$2M - 500,000)	\$680,800	
2013:	\$345,800 + 41% (\$1M - 1M)	(345,800)	
			335,000

(iv) Amount of adjustment necessary to give full credit in 2013 for the difference in the 2011 gift tax rate and applicable credit amount (compare the TRA calculation above under this example) \$ 435,000

6. **A owns \$5,000,000 of assets; in 2011 A makes a gift of \$2,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is \$5,000,000; A dies in 2013 when the estate tax rate is 55%, the estate tax applicable credit amount is \$1,000,000, and the TRA version of §2001(b) is not retained (this example, in contrast to Example 5, assumes Congress takes no action upon the expiration of the TRA rules).**

a. This example compares a gifting transaction which utilizes only the 2011 gift applicable credit amount (no gift tax is paid in 2011) to a structure under which the same assets are held until death where pre-TRA §2001(b) applies.

b. Under pre-TRA §2001(b)(2), credit is only given for the gift tax rate vs. estate tax rate differential, not for the difference between the gift tax applicable credit amount and the estate tax applicable credit amount. Under this example, the §2001(b)(2) calculation does not provide an offset benefit. Where the size of the gift in 2011 (\$2,000,000 in this example) does not generate a tax at the increased estate tax rate that is larger than the date of gift applicable credit amount, the pre-TRA §2001(b)(2) calculation will provide no benefit. Compare Example 3 where a \$5,000,000 gift in 2011 did provide an advantage in the estate tax calculation under the pre-TRA §2001(b)(2) calculations.

c. The estate tax calculation assuming a \$2,000,000 gift is made in 2011 is as set forth in the pre-TRA law calculation column under Example 5; the estate tax amount is \$2,045,000

d. The estate tax calculation assuming no gift is made in 2011 (so that the gross estate = $5,000,000) is as follows:

(i)	Estate tax calculation $1,290,800 + 55% ($5M - 3M)	$ 2,390,800
(ii)	§2010(c) credit $345,800 + 41% ($1M - 1M)	(345,800)
(iii)	Estate tax	$ 2,045,000

e. The estate tax in either case ($2,000,000 gift in 2011 vs. no gift in 2011) is $2,045,000. There is neither a benefit realized nor additional tax cost incurred from the 2011 gift transaction. Nevertheless, as discussed in Example 7, taking advantage of the increased gift tax applicable credit amount in 2011 may still preserve additional wealth for the donor's family.

7. **A owns $5,000,000 of assets; in 2011 A makes a gift of $2,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000. Instead of a cash gift of $2,000,000 as under Example 6, A's gift of a $2,000,000 value is based on an appraisal of a gifted limited partnership interest that provides a discounted valuation of one-third from the liquidation value of the gifted interests (liquidation value = $3,000,000) because of lack of marketability and lack of control factors; assets retained by A and assets gifted by A increase in value on an after income tax basis at 4% per year; A dies in 2013 when the estate tax rate is 55%, the estate tax applicable credit amount is $1,000,000, and the TRA version of §2001(b) is not retained (as under Example 6, this example assumes Congress takes no action upon the expiration of the TRA rules).**

a. As under Example 2, this example points out the potential tax benefits of making use of the 2011 increased gift tax applicable credit amount where the §2001(b)(2) calculation reverts to the worst case scenario under the pre-TRA rules. This example compares the Example 7 scenario to two other scenarios; (i) the same tax regime as under Example 7, but A makes no lifetime gifts (and as a consequence the estate cannot take advantage of valuation leveraging), and (ii) the value of the gift by A of family limited partnership interests is limited to the 2009 lifetime gift applicable credit amount of $1,000,000.

b. Estate tax calculation under facts of Example 7.

(1) 2011 gift tax paid on $2M gift at 35%

i)	Tax: $155,800 + 35% ($2M - 500,000)	$ 680,800
ii)	§2505(a) credit: $155,800 + 35% ($2M - 500,000)	(680,800)
iii)	Gift tax paid	$ 0

(2)	Value of estate	
i)	Current value in 2011 - $5M - 3M (non-discounted value of gift) - 0 (gift tax paid)	$2,000,000
ii)	Future value of $2,000,000 earning 4% per year over 2 years	2,163,200
(3)	A dies in 2013 (rate = 55%,credit amount = $1M)	
i)	Gross estate	$2,163,200
ii)	Adjusted taxable gifts	2,000,000
iii)	Tax base	$4,163,200
iv)	Tentative tax: $1,290,800 + 55% ($4,163,200 - 3M)	1,930,560
v)	§2001(b)(2) adjustment	
	Pre-TRA: $780,800 + 49% ($2M - 2M) - 1,730,800	0
vi)	Gross estate tax	$1,930,560
vii)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
viii)	Estate tax payable	$1,584,760
(4)	Assets distributed from A's estate ($2,163,200 - 1,584,760)	$ 578,440
(5)	Future value of $3,000,000 gift over 2 years at 4% per year	3,244,800
(6)	Total assets from A to A's family	$3,823,240

c. In the alternative, and for purposes of comparison to the Example 7 structure, assume A makes no gift in 2011 and no discount valuation leverage is available to A's estate.

(i)	Future value of $5,000,000 over 2 years at 4% per year	$5,408,000
(ii)	Estate tax paid at A's death	
-	$1,290,800 + 55% ($5,408,000 - 3M)	2,615,200
-	§2010(c) credit $345,800 + 41% ($1M - 1M)	(345,800)
-	Total estate tax	$2,269,400
(iii)	Assets distributed after A's death ($5,408,000 - $2,269,400)	$3,138,600

d. In the alternative, and for purposes of comparison to the Example 7 structure, assume A's gift in 2011 is of a $1,000,000 limited partnership interest as valued by a one-third discount from liquidation value (where liquidation value is $1,500,000), Under the 2009 gift tax regime, the $1,000,000 gift amount was the maximum that could be made without incurring gift tax.

(1)	2011 gift tax paid on 2011 gift		
	i)	Tax: $155,800 + 35% ($1M - 500,000)	$ 330,800
	ii)	§2505(a) credit: $155,800 + 35% ($1M - 500,000)	(330,800)
	iii)	Gift tax paid	$ 0
(2)	Value of estate		
	i)	Current value in 2011: $5M - 1.5M (gift) - 0 (gift tax paid)	$3,500,000
	ii)	Future value of $3,500,000 earning 4% per year over 2 years	3,785,600
(3)	A dies in 2013 (rate = 55%,credit amount = $1M)		
	i)	Gross estate	$3,785,600
	ii)	Adjusted taxable gifts	1,000,000
	iii)	Tax base	$4,785,600
	iv)	Tentative tax: $1,290,800 + 55% ($4,785,600 - 3M)	2,272,880
	v)	§2001(b)(2) adjustment	
		Pre-TRA: $345,800 + 41% ($1M - 1M) - 1,730,800	0
	vi)	Gross estate tax	$2,272,880
	vii)	§2010(c) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	viii)	Estate tax payable	$1,927,080
(4)	Assets distributed from A's estate ($3,785,600 - 1,927,080)		$1,858,520
(5)	Future value of $1,500,000 gift over 2 years at 4% per year		1,622,400
(6)	Total assets from A to A's family		$3,480,920

e. Compare assets distributed to family if A makes a $2,000,000 gift in 2011 vs. if A holds all assets until death with no gifting.

(i)	Assets assuming $2,000,000 gift in 2011	$3,823,240
(ii)	Assets assuming no 2011 gift	(3,138,600)
(iii)	Additional assets to family utilizing 2011 $2,000,000 gifting strategy	$ 684,640

f. Compare assets distributed to family if A makes a $2,000,000 gift in 2011 vs. if A makes a $1,000,000 gift in 2011.

(i)	Assets assuming $2,000,000 gift	$3,823,240
(ii)	Assets assuming $1,000,000 gift	(3,480,920)
(iii)	Additional assets to family utilizing 2011 $2,000,000 gifting strategy	$ 342,320

g. Under the factual structure of Example 7, A's gift transaction in 2011, even assuming that the pre-TRA §2001(b) rules apply at A's death, preserves more asset value to A's family than if A holds all assets until death. Nevertheless, a potential inequity with regard to the source of the estate tax payment needs to be kept in mind under the gifting strategy. Under the Example 7 calculation, the obligation for the entire $1,584,760 estate tax is born by A's estate, even though a significant portion of the estate tax obligation is attributable to the inclusion of the 2011 $2,000,000 gift as part of the tax base. The result is that the recipients of A's estate receive only $578,440 of an aggregate $2,163,200 gross estate value, and the gift recipients retain the full $3,000,000 gift value without reduction for gift or estate tax.

8. **A owns $5,000,000 of assets; in 2011 A makes a gift of $1,000,000 when the gift tax rate is 35% and the gift tax applicable credit amount is $5,000,000. A dies in 2013 when the estate tax rate is 55%, the estate tax applicable credit amount is $1,000,000, and the TRA version of §2001(b) is retained (this example assumes Congress takes action to preserve the TRA version of §2001(b)(2)).**

a. This example shows that where no gift tax is paid in the year of gift and the gift tax applicable credit amount used is less than the available credit either at the time of the gift or at the time of death, no adjustment occurs under either TRA §2001(b)(2) or pre-TRA §2001(b)(2); the non-adjustment makes sense given that the donor did not take advantage of a lower tax rate or a higher gift tax credit amount in the year of the gift.

b. The following table compares the actual §2001(b)(2) calculation under pre-TRA law and TRA.

			Pre-TRA Law	TRA Law
(1)	2011 gift tax paid on $1,000,000 gift			
	i)	Tax: $155,800 + 35% ($1M- 500,000)	$ 330,800	$ 330,800
	ii)	§2505(a) credit: $155,800 + 35% ($1M - 500,000)	(330,800)	(330,800)
	iii)	Gift tax paid	$ 0	$ 0
(2)	Value of estate			
	i)	$5M - 1M (gift) - 0 (gift tax)	$ 4,000,000	$ 4,000,000

(3) A dies in 2013 (rate = 55%, credit amount = $1M)

i)	Gross estate	$ 4,000,000	$ 4,000,000
ii)	Adjusted taxable gifts	1,000,000	1,000,000
iii)	Tax base	$ 5,000,000	$ 5,000,000
iv)	Tentative tax: $1,290,800 + 55% ($5M - 3M)	2,390,800	2,390,800
v)	§2001(b)(2) adjustment		
	Pre-TRA: $345,800 + 41% ($1M - 1M) - 1,730,800	0	
	TRA: $345,800 + 41% ($1M - 1M) - 345,800		0
vi)	Gross estate tax	$ 2,390,800	$ 2,390,800
vii)	§2010(c) credit: $345,800 + 41% ($1 - 1M)	(345,800)	(345,800)
viii)	Estate tax payable	$ 2,045,000	$ 2,045,000

c. Proof regarding calculation of §2010(b)(2) adjustment, which in this example = 0 (see Example 1 for proof calculation discussion).

(i) 1st offset - the actual amount of gift tax paid in 2011 $ 0

(ii) 2nd offset - the difference in the tax calculation applicable to the adjusted taxable gift added back into the 2013 estate tax calculation and the actual tax calculation applicable to the gift in 2011. Although counterintuitive because no gift tax was actually paid, the offset for tax rate differential remains relevant because the tax is still technically charged; it is only not paid because it is offset by the §2505(a) credit.

2013:	$345,800 + 41% ($1M - 1M)	$ 345,800	
2011:	$155,800 + 35% ($1M - 500,000)	330,800	
			15,000

(iii) 3rd offset - the difference in the applicable credit amount available for the actual 2011 gift, and the applicable credit amount available for the 2013 estate. The reason for the negative adjustment in this

3rd offset calculation is that in each year, the applicable credit amount is limited to the tax amount calculated under the second offset.

2011:	$155,800 + 35% ($1M - 500,000)	$ 330,800	
2013:	$345,800 + 41% ($1M - 1M)	345,800	
			(15,000)

(iv) Amount of adjustment necessary to give full credit in 2013 for the differential in the 2011 gift tax rate and the 2011 gift tax applicable credit amount $ 0

9. **A owns $30,000,000 of assets; in 2009 A makes a gift of $10,000,000 when the gift tax applicable rate is 45% and the gift tax applicable credit amount is $1,000,000. A dies in 2013 when the estate tax rate is 35%, the estate tax applicable credit amount is $5,000,000 and the TRA version of §2001(b) applies (this example assumes Congress takes action prior to the expiration of the TRA rules). A's assets do not increase in value from 2009 to 2013.**

a. This example shows that §2001(b)(2) does not provide the donor's estate with a dollar for dollar offset for gift taxes paid if the gift tax paid is greater than the estate tax effectively calculated on the §2001(b)(1)(B) adjusted gift. This circumstance could arise because either the marginal estate tax rate for the year of death is lower than the marginal gift tax rate for the year of gift, or where the estate tax applicable credit amount for the year of death is higher than the gift tax applicable credit amount for the year of gift. In this example, both of these circumstances occur.

b. Estate tax calculation at A's death in 2013.

(1)	2009 gift tax paid on $10,000,000 gift at 45%		
	i)	Tax: $555,800 + 45% ($10M - 1.5)	$4,380,800
	ii)	§2505(a) credit: $345,800 + 41% ($1M - 1M)	(345,800)
	iii)	Gift tax paid	$4,035,000
(2)	Value of estate		
	i)	$30M - 10M (gift) - 4,035,000 (gift tax)	$15,965,000
(3)	A dies in 2013 (rate = 35%,credit amount = $5M)		
	i)	Gross estate	$15,965,000
	ii)	Adjusted taxable gifts	10,000,000
	iii)	Tax base	$25,965,000

iv)	Tentative tax: $155,800 + 35% ($25,965,000 - 500,000)	9,068,550
v)	§2001(b)(2) adjustment	
	TRA: $155,800 + 35% ($10M - 500,000) - 1,730,800	(1,750,000)
vii)	Gross estate tax	$ 7,318,550
ix)	§2010(c) credit: $155,800 + 35% ($5M - 500,000)	(1,730,800)
x)	Estate tax payable	$ 5,587,750

c. Compare gift tax actually paid in 2009 to §2001(b)(2) adjustment for gift taxes paid in 2013.

2009 gift tax	$ 4,035,000
2013 §2001(b)(2) adjustment	(1,750,000)
	$ 2,285,000

d. These calculations show that A paid $2,285,000 of gift tax for which A's estate does not receive an offset under the 2013 estate tax calculation.

e. There are a few factors to consider that may partially make up for the $2,285,000 out of pocket loss for the excess gift taxes paid.

(i) Estate tax is not paid on the $4,035,000 of gift tax paid in 2009 (payment of gift tax is estate tax exclusive). If A had made no gift in 2009, then the equivalent of the $4,035,000 would have been subject to estate tax (assuming A did not otherwise spend it during life).

(a) Estimated estate tax saved by excluding gift tax payment from gross estate.

$4,035,000 x 35%	$1,412,250

(ii) If, as opposed to the general facts of this example, the assets gifted in 2009 increase in value at an after tax rate of 4% per year, then additional value will be removed from A's estate through the gift.

(a) Value removed from A's estate if gifted assets increase in value from 2009 to 2013 at after tax rate of 4% per year. $1,698,586

(b) Additional value (not considered here) may be removed from A's taxable estate if the gift consists of assets valued under discount principals such as gifts of family limited partnership interests.

(iii) To compare apples to apples, the asset growth that would have accrued from the 2009 gift payment would be lost to A's estate.

(a) Loss of growth on 2009 gift tax payment from 2009 to 2013 at after tax rate of 4% per year. (685,380)

(b) Another offsetting factor to consider is the loss of a stepped up basis that would have applied to the gifted assets had they remained in A's estate until death. __________

(iv) Net value to A's estate of offsetting factors outlined above $2,425,456

IV. Summary

A. After the year-end events or non-events of 2009 and 2010, few would dare to predict how or whether Congress will act prior to the expiration of the TRA rules at the end of 2012. Nevertheless, a couple of factors tilt the probabilities toward a retention of the TRA version of §2001(b)(2) going forward in 2013.

1. The philosophy or spirit of §2001(b)(2) has always been to provide an equitable credit under the estate tax calculation for the gift tax regime as in effect on the date of the gift, to the extent that regime was more favorable than the estate tax regime under which the adjusted gifts were added into the tax base.

2. Pre-TRA §2001(b)(2) addressed this philosophy by accounting for the difference between a more favorable gift tax rate for the year of gift vs. the estate tax rate for the year of death. There was no need to account for a difference in applicable credit amounts because (until the 2011 TRA rules became effective) the gift tax applicable credit amount was never more favorable than the estate tax applicable credit amount.

3. By enacting the TRA version of §2001(b)(2) Congress did nothing more than coordinate the historic philosophy behind §2001(b)(2) with the never before seen prospect that the gift tax applicable credit amount available for the year of gift may be more favorable than the date of death applicable credit amount.

4. The foregoing suggests two things: first, that Congress, by enacting the TRA version of §2001(b)(2), evidenced its intention to honor the historic spirit of §2001(b)(2); second, that a return to the pre-TRA version of §2001(b)(2) in 2013 would violate that same spirit.

B. If the TRA version of §2001(b)(2) is extended on a permanent basis beyond 2012, the benefits of significant gifting transactions in 2011 and 2012 will be preserved under the date of death estate tax calculation. Less obvious, there are opportunities to preserve family wealth through the same gifting transactions even in the event of a return to the pre-TRA version of §2001(b)(2).

Line 7 Worksheet—Gift Tax on Gifts Made After 1976

a. Calendar year or calendar quarter / Total pre-1977 taxable gifts. Enter the amount from line 1, Worksheet TG	b. Total taxable gifts for prior periods (from Form 709, Part 2, Tax Computation, line 2)	c. Taxable gifts for this period (from Form 709, Part 2, Tax Computation, line 1) (see below)	d. Tax payable using Table A (see above)	e. Unused unified credit (applicable credit amount) for this period (see below)	f. Tax payable for this period (subtract col. e from col. d)
0	10,000,000	10,000,000	4,380,800	1,730,800	2,650,000

1. Total gift taxes payable on gifts made after 1976 (combine the amounts in column f)	1	2,650,000
2. Gift taxes paid by the decedent on gifts that qualify for "special treatment." Enter the amount from line 2, column e, Worksheet TG	2	0
3. Subtract line 2 from line 1	3	0
4. Gift tax paid by decedent's spouse on split gifts included on Schedule G. Enter the amount from line 2, column f, Worksheet TG	4	0
5. Add lines 3 and 4. Enter here and on line 7 of the Tax Computation of Form 706	5	2,650,000

Columns b and c. In addition to gifts reported on Form 709, you must include in these columns any taxable gifts in excess of the annual exclusion that were not reported on Form 709.

Column d. To figure the "tax payable" for this column, you must use Table A in these instructions, as it applies to the year of the decedent's death rather than to the year the gifts were actually made. To compute the entry for column d, you should figure the "tax payable" on the amount in column b and subtract it from the "tax payable" on the amounts in columns b and c added together. Enter the difference in column d.

"Tax payable" as used here is a hypothetical amount and does not necessarily reflect tax actually paid. Figure "tax payable" only on gifts made after 1976. Do not include any tax paid or payable on gifts made before 1977. However, if the decedent made taxable gifts before January 1, 1977, a special computation is required. The amount of gift tax payable (line 7) should be determined by applying the unified rate schedule, in effect at date of death, to the cumulative lifetime taxable transfers made both before January 1, 1977, and after December 31, 1976, and then subtracting the taxes payable on the lifetime transfers made before December 31, 1976.

To calculate the tax, enter the amount for the appropriate year from column c of the worksheet on line 1 of the Tax Computation of the Form 709. Enter the amount from column b on line 2 of the Tax Computation. Complete the Tax Computation through the tax due before any reduction for the unified credit (applicable credit amount) and enter that amount in column d, above.

Column e. To figure the unused unified credit (applicable credit amount), use the unified credit (applicable credit amount) in effect for the year the gift was made. This amount should be on line 12 of the Tax Computation of the Form 709 filed for the gift.

not carry the totals forward from one schedule to the next.

- Enter the total, or totals, for each schedule on page 3, Part 5—Recapitulation.
- Do not complete the "Alternate valuation date" or "Alternate value" columns of any schedule unless you elected alternate valuation on line 1 of Part 3—Elections by the Executor.
- When you complete the return, staple all the required pages together in the proper order.

Part 1—Decedent and Executor (Page 1 of Form 706)

Line 2

Enter the SSN assigned specifically to the decedent. You cannot use the SSN assigned to the decedent's spouse. If the decedent did not have an SSN, the executor should obtain one for the decedent by filing Form SS-5, with a local Social Security Administration office.

Line 6a. Name of Executor

If there is more than one executor, enter the name of the executor to be contacted by the IRS. List the other executors' names, addresses, and SSNs (if applicable) on an attached sheet.

Line 6b. Executor's Address

Use Form 8822 to report a change of the executor's address.

Line 6c. Executor's Social Security Number

Only individual executors should complete this line. If there is more than one individual executor, all should list their SSNs on an attached sheet.

Part 2—Tax Computation (Page 1 of Form 706)

In general, the estate tax is figured by applying the unified rates shown in Table A on page 4 to the total of transfers both during life and at death, and then subtracting the gift taxes.

Note. You must complete Part 2—Tax Computation.

Line 1

If you elected alternate valuation on line 1, Part 3—Elections by the Executor, enter the amount you entered in the "Alternate value" column of item 12 of Part 5—Recapitulation. Otherwise, enter the amount from the "Value at date of death" column.

Helping you achieve, maintain and defend a leadership position.

Baker Hostetler

David L. Starbuck

David L. Starbuck maintains an active practice counseling individual and closely held business clients regarding taxation and business transaction planning matters. In serving his clientele, Mr. Starbuck drafts taxed advantaged trust structures and advises on sophisticated business succession techniques, including family limited partnerships, defective grantor trusts, intra-family asset sales and buy/sell agreements. He assists his clients regarding choice of entity planning, real estate transactions, charitable giving, incentive trust analysis, life insurance planning, corporate partnership and limited liability company restructures and fiduciary matters. Mr. Starbuck also represents a variety of financial institutions, advising them on trust adminstration, taxation and reformation matters.

A frequent presenter, Mr. Starbuck teaches each year at the University of Denver College of Law, Graduate Tax Program, in the areas of estate and gift taxation and estate planning. He has lectured both locally and nationally, most recently at the National AICPA Valuation Conference, in the areas of family limited partnership planning and generation skipping tax planning.

In the firm's Denver office, Mr. Starbuck serves as the coordinator of the tax group and as the legal services partner for the combined business and tax groups.

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- LL.M., University of Denver, 1987, Graduate Tax Program
- J.D., University of Denver College of Law, 1983, Order of St. Ives
- B.A., Western State College, 1977, *magna cum laude*

PRACTICE STRENGTHS

- Trusts and Estates
- Transactional Tax
- Real Estate Transactions
- Private Wealth Planning

The Madison Group, Inc.

Principals & Directors

NEAL C. GROFF
Founder & Chairman

Throughout his forty year career in the industry, Neal has been nationally recognized for his work in the area of wealth preservation, wealth transfer, and business continuity planning. He has served on the product committees of several major insurance companies, advising them in developing new and improving existing products. He served on the advisory board for Family Office Exchange and has been a leading industry resource to its members since its inception in 1989. Neal is a long tenured member of the Association of Advanced Life Underwriters, the leading legislative and technical arm of the life insurance industry, where he serves on the Business Insurance and Estate Planning Committee.
Neal's current practice includes a special focus on large family offices and privately-held businesses.

Additionally, Neal has a strong commitment to supporting organizations that enrich the arts, advance healthcare, nurture and inspire our youth, and increase civic pride and responsibility. He currently serves as the Rocky Mountain Regional Committee Chair of the US Ski and Snowboard Team, and on the Development Committee of the Vail Valley Foundation. Neal has served as a member of the Board of Directors for Boy Scouts of America, Colorado Symphony Orchestra, Colorado UpLIFT, Leaders Challenge and the U.S. Air Force Academy Foundation. He is a founding member of The Economic Club of Colorado and Colorado Concern.

Neal received a Bachelor of Science degree in Finance at the University of Colorado, and holds a Chartered Life Underwriter designation. He is a Registered Representative of M Holdings Securities, Inc.

MARK J. RICHARDS
Vice Chairman

Mark is highly regarded as an advisor to affluent individuals, family owned businesses, and privately held companies. Since 1980, Mark has distinguished his career with numerous speaking engagements, professional accomplishments and community service. He serves on the Board of Directors for the Denver Economic Club and is a Board Emeritus member for the Starlight Foundation. Prior to joining The Madison Group, Inc., Mark was founder and president of The M. J. Richards Company, a Denver based financial services organization.

Mark holds a Bachelor of Science degree in Finance from the State University of New York. He is a member of the Association of Advanced Life Underwriters, and holds the professional designations of Certified Financial Planner, Chartered Life Underwriter, Chartered Financial Consultant, Advanced Estate Planner, LegacyTM Wealth Coach, The Ultimate Gift ExperienceTM Ambassador, and is a Registered Representative of M Holdings Securities, Inc.

SUSAN D. CARR
President & CEO

As President and Chief Operating Officer, Sue manages the firm's Design Team as well as all internal operations of the firm. Sue brings her expertise in sophisticated wealth transfer design to The Madison Group's clientele. Prior to her work with The Madison Group, Sue served as Vice President and Financial Analyst for a private company, providing analysis and recommendation on a variety of business planning and investment opportunities.

Sue is a Certified Financial Planner (CFP) and a member of the Association for Advanced Life Underwriting (AALU). She holds a magna cum laude Bachelor of Science in Microbiology with a minor in chemistry from the University of Memphis. She holds a Masters of Business Administration from the University of Colorado.

TIMOTHY J. BELBER, JD
Director, Family Wealth Services Group

Growing up in a family of extremely limited financial resources, Tim experienced first-hand the impact messages about financial capital can have on one's development. Learning gratitude in an environment of financial scarcity has allowed him to help self-made families align the power of their intangible assets with the use of their tangible financial assets.

During six years of military school, Tim learned the importance of showing up ready in life. He learned the core leadership, planning and execution skills it takes to succeed in such an environment – one in which excuses and lack of preparedness were intolerable.

Tim is a member of The Society of Financial Service Professionals (1983), The Legacy Wealth Coach Network (2000) and The Copper Beech Tree Society (2004). He speaks frequently on the subject of incorporating ethics and values into long term financial and estate plans.

Tim earned a business degree from the Wharton School at the University of Pennsylvania and law degree from Seton Hall University. Tim has been married to Donna for 31 years and together they have been friend and guardian to numerous dogs. Tim speaks fluent Italian. He is an avid fly fisherman, cyclist, reader and traveler.

SEAN P. MULLEN, MSFS

Director of Financial Services

As Director of Financial Services, Sean is responsible for product overview as well as securities compliance and related issues. Sean is also a member of the firm's Design Team, developing highly detailed financial models under a variety of assumptions to provide the underlying rationale and recommendation of long-term financial strategies to the firm's clients. Sean has over 10 years of various experience in the financial services industry. Prior to joining The Madison Group, Sean was a case design analyst for a Fortune 50 financial services and insurance company.

Sean is FINRA Certified: Series 7, 63 and 65 and maintains a life, annuity and health insurance license in the state of Colorado. Sean received his Bachelor of Science degree in Finance with minors in Accounting and Economics from the University of Colorado, Boulder. Sean also has his Masters of Science degree in Financial Services from the University of Phoenix, College of Financial Planning. Sean is a Registered Representative of M Holdings Securities, Inc.

SHAWN M. TIDWELL, CPA

Director of Case Design

As Director of Case Design, Shawn works with affluent families, executives and their advisors on estate planning, intergenerational wealth transfer planning and business succession planning. He advocates strategies that serve to reinforce the client's core values to subsequent generations. Shawn works cooperatively with the clients existing advisors, providing highly sophisticated models and planning strategies, and advocating the sophisticated application of life insurance as a unique asset class for improved tax savings, portfolio efficiency and risk protection.

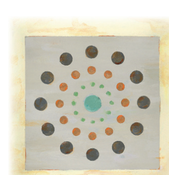
Shawn's previous experience includes investment manager at a national securities firm and CPA at an accounting big-four firm. He graduated with honors from Bucknell University with a BS in Accounting, and is currently completing his Maters of Taxation degree at the University of Denver. While at Bucknell, Shawn was a starter on the Division 1-AA football team and was a member of a hand-selected group of students who managed a portion of the investments of the university's endowment. Shawn and his wife, Wylie, are parents to three young children and reside in the Denver suburbs.

THE MADISON GROUP is one of the largest independent financial firms in the United States dedicated to comprehensive wealth preservation. We specialize in providing affluent families, family offices, business owners, and key executives with exceptional, tax-efficient wealth transfer and business continuity strategies.

We help our clients accomplish financial goals such as:

- *Values-based planning*
- *Wealth transfer*
- *Family business succession planning*
- *Efficient charitable giving*
- *Asset protection and wealth preservation*

As seasoned financial professionals specializing in the unique needs of the affluent, we have the experience, knowledge and analytical proficiency to help your client families attain ultimate results with unprecedented efficiency.



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