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Dear Friends:

It's a heck of a way to run a country! We have been waiting since 2001 for Congress to give us some certainty as to estate taxes. Now it is December, eight years later, and we still do not know how the story will end. You will recall that if no legislation passes this year, the estate tax vanishes on the stroke of midnight December 31, 2009 only to reappear one year later in its old form - a $1 million exemption and 55% top tax rate. So much for certainty in death and taxes . . .

ESTATE TAX EXTENSION?

On Thursday, December 2, 2009, the U.S. House of Representatives passed a Bill permanently extending the estate tax rules currently in effect. The Bill does the following - and nothing more: (a) makes the estate, gift and generation skipping taxes permanent; (b) makes permanent the 45% estate, gift and generation skipping tax rate bracket; (c) makes permanent the $3.5 million applicable exclusion amount (the exemption from estate tax); and (d) preserves the date of death value step-up basis rules. Assuming the Senate passes a Bill mirroring these provisions, couples who own assets as community property can continue to pass up to $7 million of assets at death, tax free, with proper tax-planned Wills. For the vast majority of Americans, the estate tax would not be a concern, especially after the economy has taken its toll on our investment assets!

Senate consideration of the estate tax legislation in the next few weeks, however, is very much up in the air. You may have heard they are busy debating health care reform. So, stay tuned to C-Span.

PLANNING IDEAS FOR LARGER ESTATES

As we indicated last year, there are some lifetime gifting techniques that are still quite attractive, given our lower stock market values and low interest rates. The Grantor Retained Annuity Trust ("GRAT") is especially useful for those who have assets they expect to appreciate significantly in value over the next few years. The Qualified Personal Residence Trust ("QPRT") can also work well for residences located in areas where the real estate market has felt a significant decline in value, such as California and Colorado. As always, the aggressive use of your $13,000 exemption for annual gifts can be a powerful tool as well. Clients with Family Limited Partnerships may want to consider using their annual exclusion gifts as well as the unused balance of their $1 million lifetime gift exclusion to give away interests in the partnership, given the availability of discounts. There is a significant possibility that those discounts (based on lack of marketability and minority

interests) may be eliminated in a more comprehensive estate tax bill next year. Those same discounts may also be helpful in sales of partnership interests to so-called Defective Grantor Trusts. Lastly, Charitable Lead Trusts are especially attractive given today's low interest rates. Please contact us as soon as possible if you have an interest in exploring any of these planning techniques.

NEW RULES FOR ROTH CONVERSIONS

Beginning in 2010, taxpayers will be able to convert part or all of a traditional retirement account (such as an IRA) into a ROTH IRA. Under the new rules, there is no income limit for ROTH conversions and taxpayers who convert in 2010 will be able to pay the income tax created by the conversion in installments (½ in 2011 and ½ in 2012) or opt out of the installments and tax the entire conversion in 2010, if it is more favorable. ROTH IRAs differ from traditional IRAs in that withdrawals from ROTH IRAs are generally tax free after the account owner has at least one ROTH IRA open for over five years and reaches the age of 59½. Another important ROTH IRA advantage is that there are no minimum distribution requirements when the owner reaches age 70½.

Conversion to a ROTH IRA is not tax beneficial for everyone. When you convert to a ROTH IRA, you pay income tax immediately rather than as the money is withdrawn. As a general rule, the conversion may be beneficial if you have sufficient assets outside of the IRA to pay the income tax resulting from the conversion, without incurring capital gains tax. Other things to consider are whether you anticipate a jump in your marginal income tax brackets, as between the tax rate in the year of conversion versus the tax rate in the years that you would have withdrawn from your IRA, and whether you have a long enough time horizon for withdrawal of the funds. Generally, the younger you are, the longer your ROTH IRA will have to increase in value to make up for the fact that income taxes were paid early.

2010 may be a perfect time to convert some of your IRAs into ROTHs. You might consider splitting your IRAs into several small accounts (by asset class), before converting them. Then by having a different investment strategy for each of the new ROTH accounts, you have the option to undo the conversion if any of the ROTH accounts drops dramatically in value, and leave the better preforming accounts as ROTHs. You have until October 15, 2011 for 2010 income tax returns to decide whether to reverse a conversion back to traditional IRA status. Check with your income tax advisors before any conversion to make sure it works for you.

We hope the New Year brings prosperity, health and hope for all of us, here and around the world.