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NEWSLETTER
FALL 2005

A Reminder About Making Year-End Gifts

The end of the year is an ideal time to consider making gifts to family members, other loved ones, or charities. That's because at this time of the year, many of you will know your financial picture for the year and will know how much you can afford to give.

Children and Loved Ones: Many of you have advised me that you are interested in helping your children during their lives rather than just passing on your assets at death. This makes sense for many reasons: a child may need funds now for a down payment on a home; repairing or replacing property damaged as a result of a hurricane or other natural disaster; starting a business; tuition; or medical expenses. **Lifetime gifting can save Federal and state death taxes and, in some cases, income taxes.** And it's often possible to structure gifts so that no gift tax will be payable. So, if one or more of these circumstances is present, and you feel you have sufficient means, you may wish to consider making gifts to family members or charities.

The Annual Exclusion from Gift Tax: From a gift tax perspective, **the first $11,000 of gifts you make to each donee in calendar year 2005 is excluded from the amount of your taxable gifts.** If you're married, you and your spouse can combine your gifting ("gift splitting" in IRS parlance) and give $22,000 together to each donee. **You can reduce your potential estate taxes by making annual exclusion gifts** because the cash (or other assets) comprising the gifts, and the post-transfer growth in their value, are removed from your estate at no transfer tax cost. (Footnote: Based on inflation data released in September this year, the annual exclusion amount will increase to $12,000 for gifts made in 2006.)

Although $1.5 million is exempt from Federal estate tax this year (and the amount goes up to $2 million next year through 2008), when you add the value of your home, other real estate, business assets, retirement benefits, savings, investments, and other personal property items, coupled with the proceeds of a life insurance policy that may be includible in your estate, you may be within reach of the Federal estate tax. Moreover, state death tax exemptions may be lower than the Federal exemption. New York State is $1 million and New Jersey is $675,000.so that even if a gift is not needed to save Federal estate tax, it could save your estate state death taxes.

Completion of the Gift: Any of you who have or plan to take advantage of the annual exclusion to make a gift to one or more individuals this year must **make sure**

that you "complete" the gift this year. This can be a problem where a gift is made by check. A gift to a noncharitable donee that is made by check is complete on the earlier of (a) the date on which the donor has so parted with "dominion and control" under state law as to leave in the donor no power to change its disposition, or (b) the date on which the donee deposits the check (or cashes the check against available funds of the donee) or presents the check for payment, if it is established that: (1) the check was paid by the drawee bank when first presented to the drawee bank for payment; (2) the donor was alive when the check was paid by the drawee bank; (3) the donor intended to make a gift; (4) delivery of the check by the donor was unconditional; and (5) the check was deposited, cashed, or presented in the calendar year for which completed gift treatment is sought and within a reasonable time of issuance. Complicated enough, isn't it?

Therefore, **we recommend that, if you make a gift by check near the end of 2005** and you want to take advantage of the annual exclusion this year, you **urge your donees to deposit their check before year end**, so that there's no doubt as to when you made the gift.

Tuition and Medical Gifts: **Making a direct payment of another individual's tuition or medical expenses is not a taxable gift.** Remember that contributions to tax-favored **qualified tuition programs (e.g., 529 Plans) and Coverdell education savings accounts don't qualify for this tuition exclusion.** They are treated instead as present gifts that can qualify for the gift tax annual exclusion, with the option of spreading contributions in a single year over a five-year period.

Income tax saving: Sometimes, gifts can save family income taxes. Take a gift of stock to a grandchild, for example. For Federal tax purposes, long-term gain on a sale of the stock by the grandchild may be taxed at 5% whereas it could be taxed at 15% if the grandparent retained the stock and sold it. The spread could be 10% or as much as 35% for gain taxable as ordinary income. For gift property that yields income, savings can be realized if the donee is in a lower marginal bracket than the donor. Maximum savings will be realized, however, for a gift to a child of the donor only if the child is at least 14 by the end of the year in which the income is received. For a child who is still under 14 at that time, some of the income may be taxed at the parent's highest marginal rate as a result of the "kiddie tax" but some savings may be still possible.

Charitable Contributions: Charitable contributions can be tremendously effective in reducing your income taxes, but the Internal Revenue Code (the "Code") imposes certain limitations on deductions from income taxes for charitable contributions. In response to the devastation caused by Hurricane Katrina, Congress enacted the Katrina Emergency Tax Relief Act ("KETRA"?), which **temporarily suspends the limitations on income tax deductions for charitable contributions to public charities in certain cases.** The suspension to the limits is open to **all tax payers** in the United States and **includes charities that are not related to Katrina** or other hurricane relief efforts. **The suspension, however, ends on December 31, 2005.**

The Rules Before and After KETRA: As a general rule, income tax deductions for charitable contributions are limited to something called your **contribution base**. That's your adjusted gross income ("AGI") computed without regard to any net operating loss carryback ("NOL") you may have. If you don't have

NOL, then we are talking about your AGI. The deduction for **cash** contributions to **public** charities is limited to **50%** of your AGI, while the deduction for contributions of **property** (not cash) to **public** charities is generally limited to **30%** of your AGI. If your contribution is larger than these amounts, you can carry over for five years any amounts that cannot be deducted in the year of the contribution. Also, as deductions for charitable contributions are itemized deductions, they are subject to being reduced by 3% of your AGI in excess of $145,950 (for 2005), but not more than 80% of the deduction.

The Rules Under KETRA: KETRA temporarily suspends the **50%** limitation on charitable contributions of **cash to certain public charities for any "qualified contributions."** A "qualified contribution" is any **cash donation to a public charity *other than* a donor advised fund, supporting organization or private nonoperating foundation made between August 28, 2005 and December 31, 2005.** In addition, the 3% of AGI rule does not apply. But the suspension does factor in non-qualifying contributions. Thus, for qualified contributions made during this period, **you may elect to deduct this year an amount up to 100% of your contribution base**, minus the total amount of other charitable contributions deductible for the year (non ?qualified contributions?). If the total amount of qualified contributions exceeds this limitation, you can carry over the excess to the five succeeding tax years. And, you can still make property contributions to public charities and make cash and property contributions to private charities subject to the limitations in the Code and applicable state law, if any.

For New York State taxpayers, the increased federal charitable deduction would generally be allowed in computing their state and local income tax liability. However, in the case of a taxpayer whose New York State AGI exceeds $100,000 ($200,000 if married filing jointly), the overall itemized deduction is subject to reduction by up to 50% by the New York State Tax Law.

These rules are complicated, especially if you have deduction carry over from prior years, have made gifts to private foundations or to split interest charitable trusts, or have exceeded the 2005 charitable deduction limitations that were in effect prior to the effective date of KETRA. In addition, other planning opportunities exist under KETRA. We encourage you to speak with us or your accountant to take full advantage of these potentially tax saving opportunities.

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