



Balancing Bet-to-Live and Bet-to-Die Strategies

Presented By:

Robert S. Keebler, CPA, MST, AEP

Stephen J. Bigge, CPA CSEP

Keebler & Associates, LLP

Phone: (920) 593-1701

E-mail: robert.keebler@keeblerandassociates.com

Circular 230 Disclosure: To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. federal tax advice contained in this communication, including attachments, was not written to be used and cannot be used for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein. If you would like a written opinion upon which you can rely for the purpose of avoiding penalties, please contact us.

2012 Estate/Gift Tax Overview

	2011	2012	2013
Top gift tax rate	35%	35%	40%
Gift tax exemption	\$5,000,000	\$5,120,000	\$5,250,000
Top estate tax rate	35%	35%	40%
Estate tax exemption	\$5,000,000	\$5,120,000	\$5,250,000
GST tax rate	35%	35%	40%
GST exemption	\$5,000,000	\$5,120,000	\$5,250,000

2012 Estate/Gift Tax Overview

Other Changes That Could Occur in 2013

- Mandatory minimum GRAT term of 10 years
- No “zeroed-out” GRATs
- No multi-generational dynasty trusts
- No valuation adjustments on transfers of closely-held interests

Balancing Bet-to-Live and Bet-to-Die Strategies



***It's a Balancing Act...
Bet to Live? Bet to Die?***

Balancing Bet-to-Live and Bet-to-Die Strategies

IMPACT OF POTENTIAL FUTURE LEGISLATION

Starting as early as the 2013 tax year, there is a possibility that certain estate planning opportunities may be diminished or possibly eliminated. These opportunities include (albeit not all-inclusive):

- Mandatory minimum GRAT term of 10 years
- No “zeroed-out” GRATs
- No multi-generational dynasty trusts
- No valuation adjustments on transfers of closely-held interests

Balancing Bet-to-Live and Bet-to-Die Strategies

KEY STRATEGIES

“Bet-to-Live” Strategies

- Lifetime Gifts
 - Annual Exclusion Gifts
 - Lifetime Gift Tax Exemption Gifts
 - Taxable Gifts
- Grantor Retained Annuity Trust (GRAT)
- Dynasty Trust
- Sale to an Intentionally Defective Grantor Trust (IDGT)

Balancing Bet-to-Live and Bet-to-Die Strategies

KEY STRATEGIES

“Bet to Die” Strategies

- Self-Canceling Installment Note (SCIN)
- Private Annuity
- Charitable Lead Trusts
- Life Insurance

Balancing Bet-to-Live and Bet-to-Die Strategies

LIFETIME GIFTS

Balancing Bet-to-Live and Bet-to-Die Strategies

LIFETIME GIFT TAX EXEMPTION GIFTS

- During a taxpayer's lifetime, he/she may make "taxable gifts" (i.e. gifts that exceed the annual exclusion gift amount) up to a specified amount (\$5,250,000 in 2013) without having to pay gift tax
 - This transfer is referred to as an "lifetime gift tax exemption gift"
 - For married taxpayers, the aggregate lifetime gift tax exemption is basically doubled (i.e. \$10,500,000 in 2013)

Balancing Bet-to-Live and Bet-to-Die Strategies

LIFETIME GIFT TAX EXEMPTION GIFTS

- Although lifetime taxable gifts may be sheltered from gift tax because of the lifetime gift tax exemption, the aggregate of such lifetime taxable gifts made by the taxpayer is included in the taxpayer's gross estate
 - However, only the original values of the taxable gifts are included in the gross estate (not the current values of the gifts)
- The post-gift future appreciation is **not** included in the taxpayer's gross estate

Balancing Bet-to-Live and Bet-to-Die Strategies

LIFETIME GIFT TAX EXEMPTION GIFTS

LIFETIME GIFT TAX EXEMPTION GIFT EXAMPLE

A single taxpayer makes a \$5,000,000 taxable gift to a trust for the benefit of his children. The table below illustrates the total amount that is removed from the taxpayer's gross estate over a period of time:

	Total Wealth Removed From Gross Estate		
	0% Growth	4% Growth	8% Growth
	Rate	Rate	Rate
Year 5	\$ 5,000,000	\$ 6,083,265	\$ 7,346,640
Year 10	\$ 5,000,000	\$ 7,401,221	\$ 10,794,625
Year 20	\$ 5,000,000	\$ 10,955,616	\$ 23,304,786

Balancing Bet-to-Live and Bet-to-Die Strategies

TAXABLE GIFTS

- To the extent that a taxpayer makes a gift in excess of his/her annual exclusion gift amount and his/her lifetime gift tax exemption amount, he/she will incur a gift tax
- The gift tax due on the taxable gift (in excess of the lifetime gift tax exemption amount) is calculated on a “tax exclusive” basis
 - In this case, the gift tax is calculated only on the value of the amount transferred (i.e. the gift)
 - For estate tax purposes, the estate tax is calculated not only on the value of the amount transferred, but also the tax that is paid on the transfer (i.e. “tax inclusive”)
- The post-gift future appreciation is **not** included in the taxpayer’s gross estate

Balancing Bet-to-Live and Bet-to-Die Strategies

TAXABLE GIFTS

“TAX EXCLUSIVE” NATURE OF GIFT TAX - EXAMPLE

	Estate Tax		Gift Tax	
Total Taxable Estate / Gift	\$	10,000,000	\$	10,000,000
Effective Tax Rate*		40.00%		28.57%
Total Tax	\$	(4,000,000)	\$	(2,857,143)
Savings	\$	-	\$	1,142,857

* Effective Gift Tax Rate = 40%/140%

Balancing Bet-to-Live and Bet-to-Die Strategies

TAXABLE GIFTS

ESTATE INCLUSION ISSUE

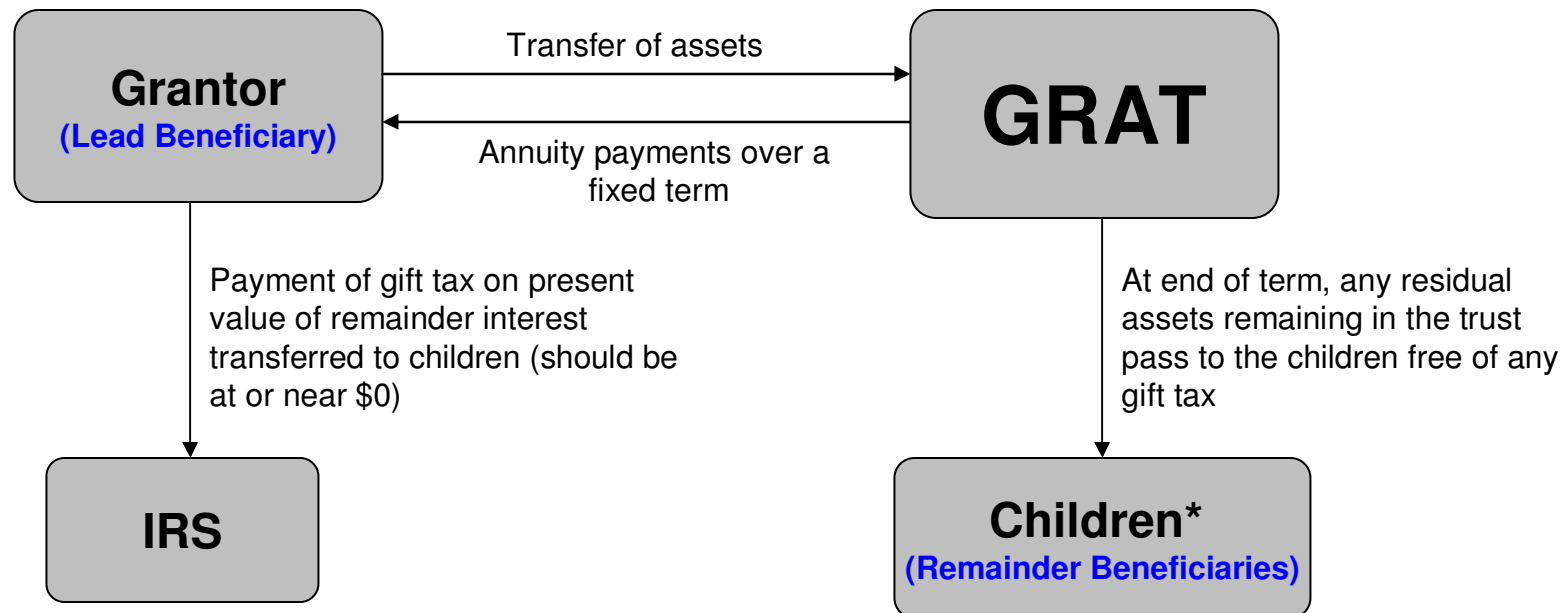
- To the extent that a taxpayer pays gift tax on a taxable gift, his/her gross estate must include the value of the gift tax paid if the taxpayer dies **within 3 years of the gift**
 - The effect is to “gross up” the taxpayer’s gross estate as if the original gift didn’t take place

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST (GRAT)

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST STRATEGY OVERVIEW



* Instead of naming the children as outright remainder beneficiaries of the GRAT, a grantor trust could be used (thus producing a greater estate tax benefit)

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST

GRAT EXAMPLE

Year	Beginning Balance	Taxable Income 10.00%	Annual Payment	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (739,075)	\$ 10,260,925
2	\$ 10,260,925	\$ 1,026,093	\$ (739,075)	\$ 10,547,943
3	\$ 10,547,943	\$ 1,054,794	\$ (739,075)	\$ 10,863,663
4	\$ 10,863,663	\$ 1,086,366	\$ (739,075)	\$ 11,210,954
5	\$ 11,210,954	\$ 1,121,095	\$ (739,075)	\$ 11,592,975
6	\$ 11,592,975	\$ 1,159,298	\$ (739,075)	\$ 12,013,198
7	\$ 12,013,198	\$ 1,201,320	\$ (739,075)	\$ 12,475,443
8	\$ 12,475,443	\$ 1,247,544	\$ (739,075)	\$ 12,983,913
9	\$ 12,983,913	\$ 1,298,391	\$ (739,075)	\$ 13,543,229
10	\$ 13,543,229	\$ 1,354,323	\$ (739,075)	\$ 14,158,477

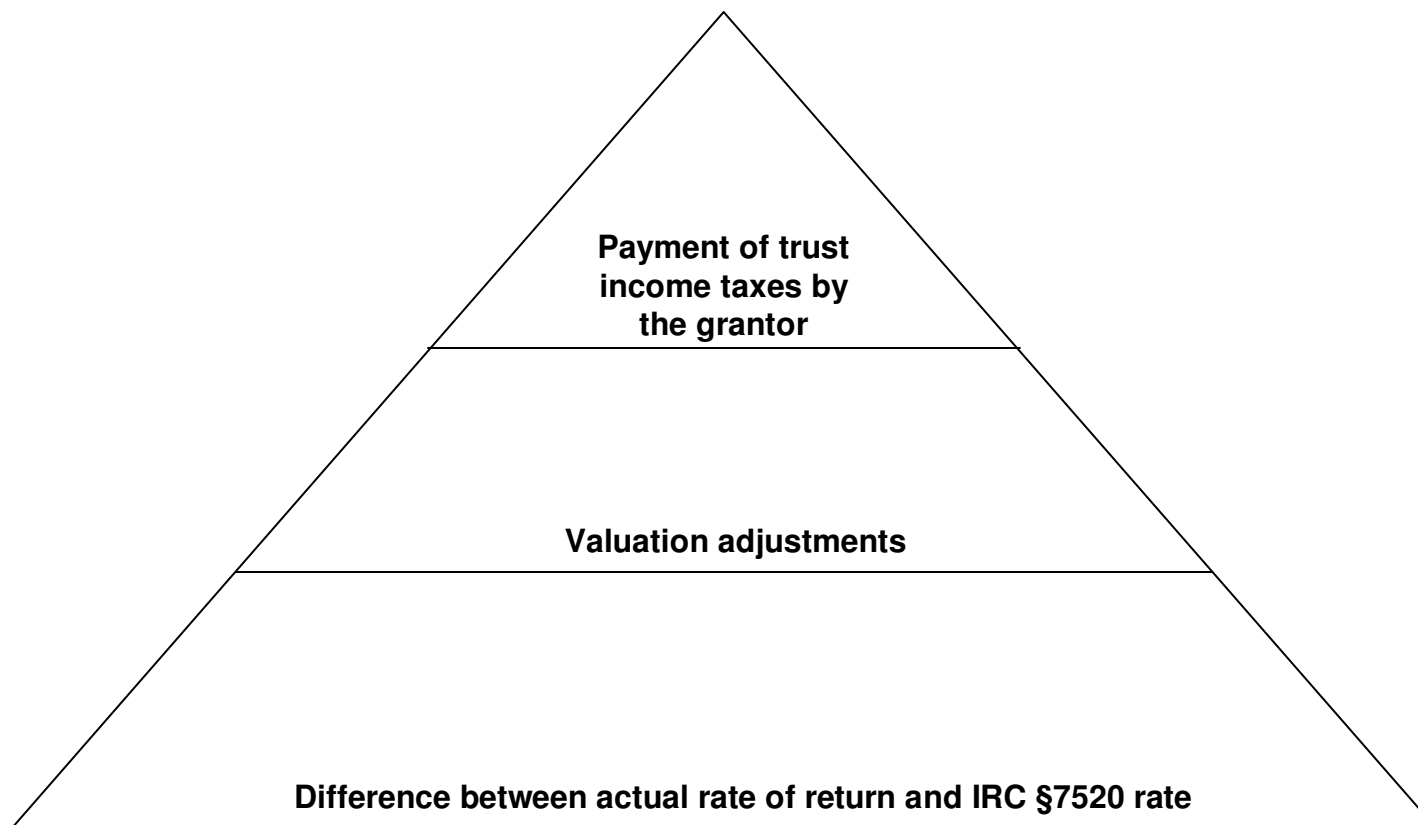
BENEFIT: \$14,158,477 transferred to beneficiaries estate/gift tax-free

***NOTE:** Assuming a \$7,000,000 (after valuation adjustments) contribution

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST

WHY A GRAT WORKS



Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST

WHY A GRAT WORKS – DIFFERENCE IN RATES OF RETURN

Year	Beginning Balance	Taxable Income 1.00%	Annuity Payment \$ 1,055,821	Ending Balance	Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 1,055,821	Ending Balance
1	\$ 10,000,000	\$ 100,000	\$ (1,055,821)	\$ 9,044,179	1	\$ 10,000,000	\$ 1,000,000	\$ (1,055,821)	\$ 9,944,179
2	\$ 9,044,179	\$ 90,442	\$ (1,055,821)	\$ 8,078,800	2	\$ 9,944,179	\$ 994,418	\$ (1,055,821)	\$ 9,882,776
3	\$ 8,078,800	\$ 80,788	\$ (1,055,821)	\$ 7,103,767	3	\$ 9,882,776	\$ 988,278	\$ (1,055,821)	\$ 9,815,232
4	\$ 7,103,767	\$ 71,038	\$ (1,055,821)	\$ 6,118,983	4	\$ 9,815,232	\$ 981,523	\$ (1,055,821)	\$ 9,740,935
5	\$ 6,118,983	\$ 61,190	\$ (1,055,821)	\$ 5,124,352	5	\$ 9,740,935	\$ 974,093	\$ (1,055,821)	\$ 9,659,207
6	\$ 5,124,352	\$ 51,244	\$ (1,055,821)	\$ 4,119,775	6	\$ 9,659,207	\$ 965,921	\$ (1,055,821)	\$ 9,569,307
7	\$ 4,119,775	\$ 41,198	\$ (1,055,821)	\$ 3,105,152	7	\$ 9,569,307	\$ 956,931	\$ (1,055,821)	\$ 9,470,417
8	\$ 3,105,152	\$ 31,052	\$ (1,055,821)	\$ 2,080,382	8	\$ 9,470,417	\$ 947,042	\$ (1,055,821)	\$ 9,361,637
9	\$ 2,080,382	\$ 20,804	\$ (1,055,821)	\$ 1,045,365	9	\$ 9,361,637	\$ 936,164	\$ (1,055,821)	\$ 9,241,980
10	\$ 1,045,365	\$ 10,454	\$ (1,055,819)	\$ -	10	\$ 9,241,980	\$ 924,198	\$ (1,055,821)	\$ 9,110,357

BENEFIT: \$9,110,357 transferred to beneficiaries estate/gift tax-free (of which \$2,094,955 is due to payment of income taxes by the grantor)

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST

WHY A GRAT WORKS – VALUATION ADJUSTMENTS

Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 1,055,821	Ending Balance	Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 739,075	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (1,055,821)	\$ 9,944,179	1	\$ 10,000,000	\$ 1,000,000	\$ (739,075)	\$ 10,260,925
2	\$ 9,944,179	\$ 994,418	\$ (1,055,821)	\$ 9,882,776	2	\$ 10,260,925	\$ 1,026,093	\$ (739,075)	\$ 10,547,943
3	\$ 9,882,776	\$ 988,278	\$ (1,055,821)	\$ 9,815,232	3	\$ 10,547,943	\$ 1,054,794	\$ (739,075)	\$ 10,863,663
4	\$ 9,815,232	\$ 981,523	\$ (1,055,821)	\$ 9,740,935	4	\$ 10,863,663	\$ 1,086,366	\$ (739,075)	\$ 11,210,954
5	\$ 9,740,935	\$ 974,093	\$ (1,055,821)	\$ 9,659,207	5	\$ 11,210,954	\$ 1,121,095	\$ (739,075)	\$ 11,592,975
6	\$ 9,659,207	\$ 965,921	\$ (1,055,821)	\$ 9,569,307	6	\$ 11,592,975	\$ 1,159,298	\$ (739,075)	\$ 12,013,198
7	\$ 9,569,307	\$ 956,931	\$ (1,055,821)	\$ 9,470,417	7	\$ 12,013,198	\$ 1,201,320	\$ (739,075)	\$ 12,475,443
8	\$ 9,470,417	\$ 947,042	\$ (1,055,821)	\$ 9,361,637	8	\$ 12,475,443	\$ 1,247,544	\$ (739,075)	\$ 12,983,913
9	\$ 9,361,637	\$ 936,164	\$ (1,055,821)	\$ 9,241,980	9	\$ 12,983,913	\$ 1,298,391	\$ (739,075)	\$ 13,543,229
10	\$ 9,241,980	\$ 924,198	\$ (1,055,821)	\$ 9,110,357	10	\$ 13,543,229	\$ 1,354,323	\$ (739,075)	\$ 14,158,477

BENEFIT: \$5,048,120 transferred to beneficiaries estate/gift tax-free

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST

WHY A GRAT WORKS – PAYMENT OF TRUST INCOME TAXES BY GRANTOR

Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 739,075	Less: Taxes @ 40.00%	Ending Balance	Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 739,075	Less: Taxes @ 0.00%	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (739,075)	\$ (104,370)	\$ 10,156,555	1	\$ 10,000,000	\$ 1,000,000	\$ (739,075)	\$ -	\$ 10,260,925
2	\$ 10,156,555	\$ 1,015,656	\$ (739,075)	\$ (110,632)	\$ 10,322,504	2	\$ 10,260,925	\$ 1,026,093	\$ (739,075)	\$ -	\$ 10,547,943
3	\$ 10,322,504	\$ 1,032,250	\$ (739,075)	\$ (117,270)	\$ 10,498,409	3	\$ 10,547,943	\$ 1,054,794	\$ (739,075)	\$ -	\$ 10,863,663
4	\$ 10,498,409	\$ 1,049,841	\$ (739,075)	\$ (124,306)	\$ 10,684,869	4	\$ 10,863,663	\$ 1,086,366	\$ (739,075)	\$ -	\$ 11,210,954
5	\$ 10,684,869	\$ 1,068,487	\$ (739,075)	\$ (131,765)	\$ 10,882,516	5	\$ 11,210,954	\$ 1,121,095	\$ (739,075)	\$ -	\$ 11,592,975
6	\$ 10,882,516	\$ 1,088,252	\$ (739,075)	\$ (139,671)	\$ 11,092,022	6	\$ 11,592,975	\$ 1,159,298	\$ (739,075)	\$ -	\$ 12,013,198
7	\$ 11,092,022	\$ 1,109,202	\$ (739,075)	\$ (148,051)	\$ 11,314,099	7	\$ 12,013,198	\$ 1,201,320	\$ (739,075)	\$ -	\$ 12,475,443
8	\$ 11,314,099	\$ 1,131,410	\$ (739,075)	\$ (156,934)	\$ 11,549,500	8	\$ 12,475,443	\$ 1,247,544	\$ (739,075)	\$ -	\$ 12,983,913
9	\$ 11,549,500	\$ 1,154,950	\$ (739,075)	\$ (166,350)	\$ 11,799,025	9	\$ 12,983,913	\$ 1,298,391	\$ (739,075)	\$ -	\$ 13,543,229
10	\$ 11,799,025	\$ 1,179,903	\$ (739,075)	\$ (176,331)	\$ 12,063,522	10	\$ 13,543,229	\$ 1,354,323	\$ (739,075)	\$ -	\$ 14,158,477

BENEFIT: \$2,094,955 transferred to beneficiaries estate/gift tax-free

Balancing Bet-to-Live and Bet-to-Die Strategies

GRANTOR RETAINED ANNUITY TRUST

WHY A GRAT WORKS – SUMMARY

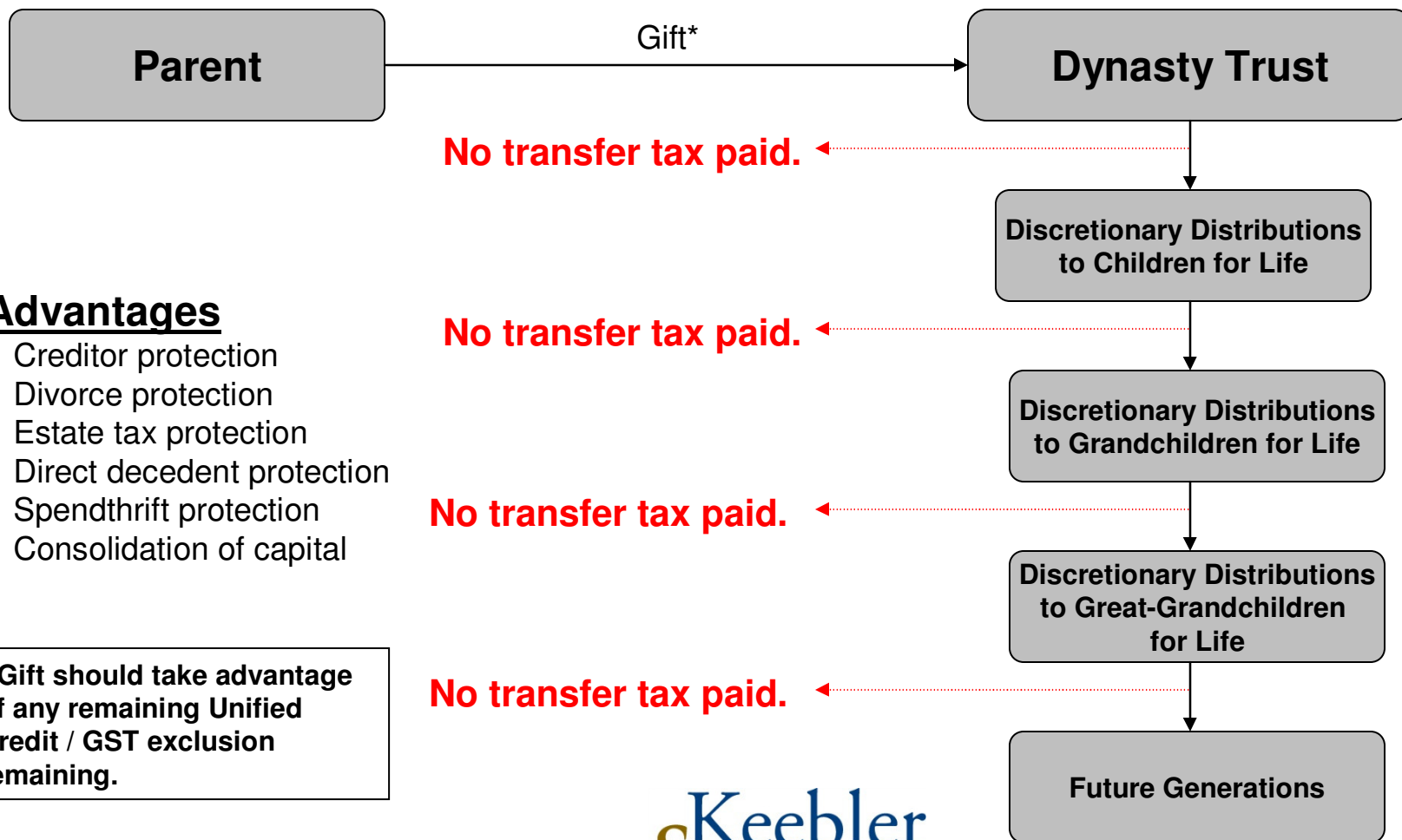
Total Wealth Transferred	\$ 14,158,477
<i>Reasons for Total Wealth Transferred</i>	
Difference in Rates of Return	\$ 7,015,374
Valuation Adjustments	5,048,120
Payment of Trust Income Taxes by Grantor	2,094,955
Rounding Adjustment	28
Total Wealth Transferred	\$ 14,158,477

Balancing Bet-to-Live and Bet-to-Die Strategies

DYNASTY TRUST

Balancing Bet-to-Live and Bet-to-Die Strategies

DYNASTY TRUST STRATEGY OVERVIEW



Balancing Bet-to-Live and Bet-to-Die Strategies

DYNASTY TRUST

TAX SAVINGS FROM AVOIDING ESTATE TAX

	5% Growth		7% Growth		9% Growth	
Value of Trust in 20 years	\$	13,266,489	\$	19,348,422	\$	28,022,054
Estate Tax Savings @ 40%	\$	5,306,595	\$	7,739,369	\$	11,208,822
Value of Trust in 40 years	\$	35,199,944	\$	74,872,289	\$	74,872,289
Estate Tax Savings @ 40%	\$	14,079,977	\$	29,948,916	\$	29,948,916
Value of Trust in 60 years	\$	93,395,929	\$	289,732,134	\$	880,156,460
Estate Tax Savings @ 40%	\$	37,358,372	\$	115,892,854	\$	352,062,584
Value of Trust in 80 years	\$	247,807,205	\$	1,121,171,938	\$	4,932,758,341
Estate Tax Savings @ 40%	\$	99,122,882	\$	448,468,775	\$	1,973,103,336

Initial investment of \$5,000,000

Balancing Bet-to-Live and Bet-to-Die Strategies

DYNASTY TRUST

ADVANTAGES

- Takes maximum advantage of the \$5,250,000 lifetime gift tax exemption
- Takes maximum advantage of the \$5,250,000 GST tax exemption
- Appreciation of assets will be free from estate tax
- Provides a layer of asset protection from the beneficiaries' creditors
- No estate/gift/GST tax will be paid at the death of the grantor's descendants
- Future trustees can be given the discretion to make distributions as appropriate, given the circumstances that exist at the time the distributions are made
- Grantor can use the trust to positively affect future behavior

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN INTENTIONALLY DEFECTIVE GRANTOR TRUST (IDGT)

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

INTENTIONALLY DEFECTIVE GRANTOR TRUST (IDGT)

An IDGT is a type of dynasty trust where all income earned by the trust is taxed to the grantor because the trust is “defective” for income tax purposes, thus allowing for a tax-free gift to the trust’s beneficiaries.

Balancing Bet-to-Live and Bet-to-Die Strategies

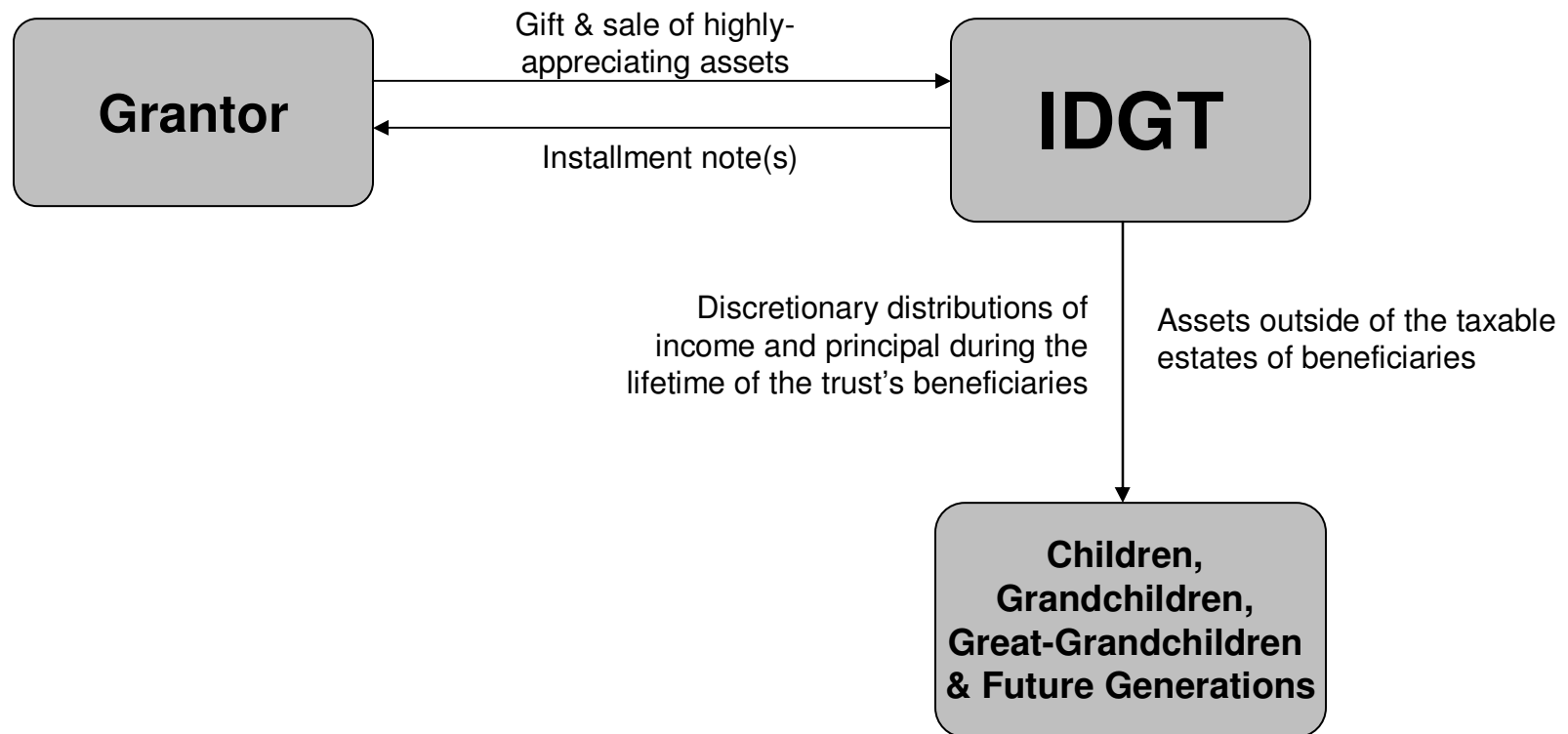
SALE TO AN IDGT

SUMMARY OF STRATEGY

- A type of transaction whereby a grantor sells a highly-appreciating asset to an IDGT in exchange for an installment note.
 - However, the grantor should make an initial gift (at least 10% of the total transfer value) to the trust so that it has sufficient capital to make its payments to the grantor.
- To the extent that the growth rate on the assets sold to the IDGT is greater than the interest rate on the installment note taken back by the grantor, the “excess” is passed on to the trust beneficiaries free of any gift, estate and/or GST tax.
- No capital gains tax is due on the installment sale to the trust because the trust is “defective” for income tax purposes.
- Interest income on installment note is not taxable to the grantor because the trust is “defective” for income tax purposes.

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT STRATEGY OVERVIEW



Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

CURRENT APPLICABLE FEDERAL RATES (AFRs) – 1/2013

Short-Term AFR (3 years or less)	.21%
Mid-Term AFR (over 3 years, up to 9 Years)	.87%
Long-Term AFR (over 9 years)	2.31%

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

SALE TO AN IDGT EXAMPLE

Year	Beginning Balance	Taxable Income 10.00%	Annual Payment	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (161,700)	\$ 10,838,300
2	\$ 10,838,300	\$ 1,083,830	\$ (161,700)	\$ 11,760,430
3	\$ 11,760,430	\$ 1,176,043	\$ (161,700)	\$ 12,774,773
4	\$ 12,774,773	\$ 1,277,477	\$ (161,700)	\$ 13,890,550
5	\$ 13,890,550	\$ 1,389,055	\$ (161,700)	\$ 15,117,905
6	\$ 15,117,905	\$ 1,511,791	\$ (161,700)	\$ 16,467,996
7	\$ 16,467,996	\$ 1,646,800	\$ (161,700)	\$ 17,953,095
8	\$ 17,953,095	\$ 1,795,310	\$ (161,700)	\$ 19,586,705
9	\$ 19,586,705	\$ 1,958,670	\$ (161,700)	\$ 21,383,675
10	\$ 21,383,675	\$ 2,138,368	\$ (7,161,700)	\$ 16,360,343

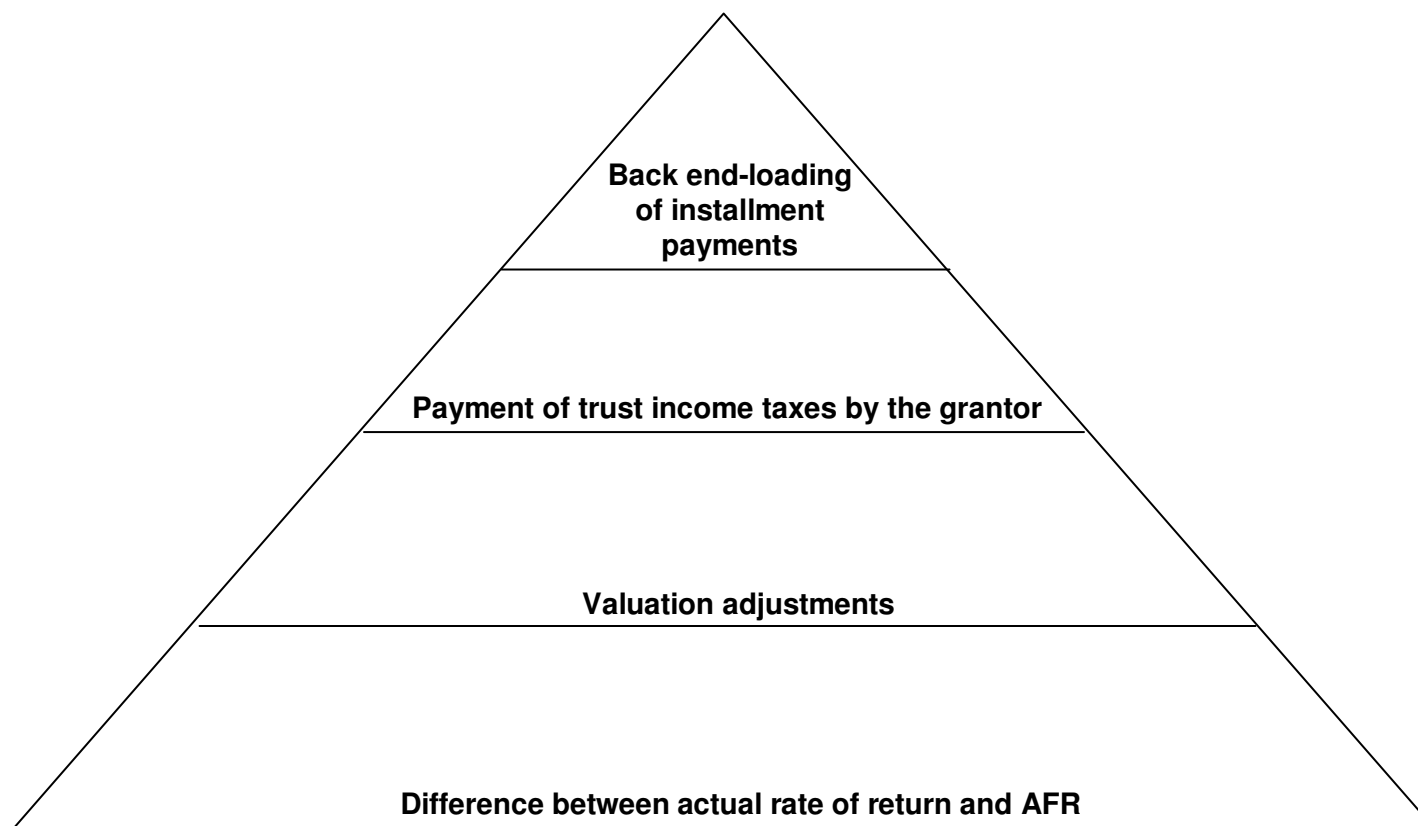
BENEFIT: \$16,360,343 transferred to beneficiaries estate/gift tax-free

***NOTE:** Assuming a \$7,000,000 (after valuation adjustments) interest only, balloon payment feature installment note with a 2.31% annual interest rate (long-term AFR)

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

WHY AN IDGT SALE WORKS



Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

WHY AN IDGT SALE WORKS – DIFFERENCE IN RATES OF RETURN

Year	Beginning Balance	Taxable Income 2.31%	Installment Payment \$ 231,000	Ending Balance	Year	Beginning Balance	Taxable Income 10.00%	Installment Payment \$ 231,000	Ending Balance
1	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	1	\$ 10,000,000	\$ 1,000,000	\$ (231,000)	\$ 10,769,000
2	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	2	\$ 10,769,000	\$ 1,076,900	\$ (231,000)	\$ 11,614,900
3	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	3	\$ 11,614,900	\$ 1,161,490	\$ (231,000)	\$ 12,545,390
4	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	4	\$ 12,545,390	\$ 1,254,539	\$ (231,000)	\$ 13,568,929
5	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	5	\$ 13,568,929	\$ 1,356,893	\$ (231,000)	\$ 14,694,822
6	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	6	\$ 14,694,822	\$ 1,469,482	\$ (231,000)	\$ 15,933,304
7	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	7	\$ 15,933,304	\$ 1,593,330	\$ (231,000)	\$ 17,295,634
8	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	8	\$ 17,295,634	\$ 1,729,563	\$ (231,000)	\$ 18,794,198
9	\$ 10,000,000	\$ 231,000	\$ (231,000)	\$ 10,000,000	9	\$ 18,794,198	\$ 1,879,420	\$ (231,000)	\$ 20,442,618
10	\$ 10,000,000	\$ 231,000	\$ (10,231,000)	\$ -	10	\$ 20,442,618	\$ 2,044,262	\$ (10,231,000)	\$ 12,255,880

BENEFIT: \$12,255,880 transferred to beneficiaries estate/gift tax-free (of which \$6,730,667 is due to payment of income taxes by the grantor)

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

WHY AN IDGT SALE WORKS – VALUATION ADJUSTMENTS

Year	Beginning Balance	Taxable Income 10.00%	Installment Payment \$ 231,000	Ending Balance	Year	Beginning Balance	Taxable Income 10.00%	Installment Payment \$ 161,700	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (231,000)	\$ 10,769,000	1	\$ 10,000,000	\$ 1,000,000	\$ (161,700)	\$ 10,838,300
2	\$ 10,769,000	\$ 1,076,900	\$ (231,000)	\$ 11,614,900	2	\$ 10,838,300	\$ 1,083,830	\$ (161,700)	\$ 11,760,430
3	\$ 11,614,900	\$ 1,161,490	\$ (231,000)	\$ 12,545,390	3	\$ 11,760,430	\$ 1,176,043	\$ (161,700)	\$ 12,774,773
4	\$ 12,545,390	\$ 1,254,539	\$ (231,000)	\$ 13,568,929	4	\$ 12,774,773	\$ 1,277,477	\$ (161,700)	\$ 13,890,550
5	\$ 13,568,929	\$ 1,356,893	\$ (231,000)	\$ 14,694,822	5	\$ 13,890,550	\$ 1,389,055	\$ (161,700)	\$ 15,117,905
6	\$ 14,694,822	\$ 1,469,482	\$ (231,000)	\$ 15,933,304	6	\$ 15,117,905	\$ 1,511,791	\$ (161,700)	\$ 16,467,996
7	\$ 15,933,304	\$ 1,593,330	\$ (231,000)	\$ 17,295,634	7	\$ 16,467,996	\$ 1,646,800	\$ (161,700)	\$ 17,953,095
8	\$ 17,295,634	\$ 1,729,563	\$ (231,000)	\$ 18,794,198	8	\$ 17,953,095	\$ 1,795,310	\$ (161,700)	\$ 19,586,705
9	\$ 18,794,198	\$ 1,879,420	\$ (231,000)	\$ 20,442,618	9	\$ 19,586,705	\$ 1,958,670	\$ (161,700)	\$ 21,383,675
10	\$ 20,442,618	\$ 2,044,262	\$ (10,231,000)	\$ 12,255,880	10	\$ 21,383,675	\$ 2,138,368	\$ (7,161,700)	\$ 16,360,343

BENEFIT: \$4,104,463 transferred to beneficiaries estate/gift tax-free

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

WHY AN IDGT SALE WORKS – PAYMENT OF TRUST INCOME TAXES BY GRANTOR

Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 161,700	Less: Taxes @ 40.00%	Ending Balance	Year	Beginning Balance	Taxable Income 10.00%	Annuity Payment \$ 161,700	Less: Taxes @ 0.00%	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (161,700)	\$ (335,320)	\$ 10,502,980	1	\$ 10,000,000	\$ 1,000,000	\$ (161,700)	\$ -	\$ 10,838,300
2	\$ 10,502,980	\$ 1,050,298	\$ (161,700)	\$ (355,439)	\$ 11,036,139	2	\$ 10,838,300	\$ 1,083,830	\$ (161,700)	\$ -	\$ 11,760,430
3	\$ 11,036,139	\$ 1,103,614	\$ (161,700)	\$ (376,766)	\$ 11,601,287	3	\$ 11,760,430	\$ 1,176,043	\$ (161,700)	\$ -	\$ 12,774,773
4	\$ 11,601,287	\$ 1,160,129	\$ (161,700)	\$ (399,371)	\$ 12,200,344	4	\$ 12,774,773	\$ 1,277,477	\$ (161,700)	\$ -	\$ 13,890,550
5	\$ 12,200,344	\$ 1,220,034	\$ (161,700)	\$ (423,334)	\$ 12,835,345	5	\$ 13,890,550	\$ 1,389,055	\$ (161,700)	\$ -	\$ 15,117,905
6	\$ 12,835,345	\$ 1,283,535	\$ (161,700)	\$ (448,734)	\$ 13,508,446	6	\$ 15,117,905	\$ 1,511,791	\$ (161,700)	\$ -	\$ 16,467,996
7	\$ 13,508,446	\$ 1,350,845	\$ (161,700)	\$ (475,658)	\$ 14,221,932	7	\$ 16,467,996	\$ 1,646,800	\$ (161,700)	\$ -	\$ 17,953,095
8	\$ 14,221,932	\$ 1,422,193	\$ (161,700)	\$ (504,197)	\$ 14,978,228	8	\$ 17,953,095	\$ 1,795,310	\$ (161,700)	\$ -	\$ 19,586,705
9	\$ 14,978,228	\$ 1,497,823	\$ (161,700)	\$ (534,449)	\$ 15,779,902	9	\$ 19,586,705	\$ 1,958,670	\$ (161,700)	\$ -	\$ 21,383,675
10	\$ 15,779,902	\$ 1,577,990	\$ (7,161,700)	\$ (566,516)	\$ 9,629,676	10	\$ 21,383,675	\$ 2,138,368	\$ (7,161,700)	\$ -	\$ 16,360,343

BENEFIT: \$6,730,667 transferred to beneficiaries estate/gift tax-free

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

WHY AN IDGT SALE WORKS – SUMMARY

Total Wealth Transferred	\$ 16,360,343
<i>Reasons for Total Wealth Transferred</i>	
Difference in Rates of Return	\$ 5,525,213
Valuation Adjustments	4,104,463
Payment of Trust Income Taxes by Grantor	6,730,667
Total Wealth Transferred	\$ 16,360,343

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

ADVANTAGES

- Freezes value of appreciation on assets sold in the grantor's taxable estate at the low interest rate on the installment note payable
- No capital gains tax due on installment sale
- Interest income on installment note is not taxable to the grantor
- Grantor pays income tax on trust income, leaving more assets in the IDGT for remainder beneficiaries
- Valuation adjustments increase effectiveness of sale for estate tax purposes

Balancing Bet-to-Live and Bet-to-Die Strategies

SALE TO AN IDGT

DISADVANTAGES

- Estate inclusion of note if grantor dies during term of installment note
- No step-up in basis at grantor's death
- Trust income taxable to grantor during his/her life could cause a cash flow problem if there is not sufficient income earned by the grantor
- Possible gift and estate tax exposure if insufficient assets are used to fund the trust
- Possible taxable gift for amount of loan
- Possible taxable estate inclusion under *Karmazin* (retained life estate)

Balancing Bet-to-Live and Bet-to-Die Strategies

SELF-CANCELING INSTALLMENT NOTE (SCIN) SALE TO AN IDGT

Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

SELF-CANCELING INSTALLMENT NOTE (SCIN)

- Transaction similar to an ordinary installment sale to an IDGT
- Cancellation-at-death feature added to note
- Premium must be paid, either in the form of additional principal or increased interest rate to compensate for the cancellation-at-death feature

OBJECTIVE: Reduction of estate tax if premature death occurs

Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

TYPES OF SCINS

- **Hedge SCIN** – A SCIN designed to hedge against the possibility of death during a bet-to-live strategy (taxable gifts, GRAT, etc...)
- **Mortality SCIN** – A SCIN designed for those who have a high likelihood of dying within a short period of time

Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

SAMPLE OF SCIN INTEREST RATE RISK PREMIUMS

SINGLE LIFE				JOINT LIFE				
Age	SCIN Risk		Total Interest Rate	Age 1	Age 2	SCIN Risk		Total Interest Rate
	Premium	AFR				Premium	AFR	
53	0.870%	2.310%	3.180%	53	53	0.067%	2.310%	2.377%
58	1.346%	2.310%	3.656%	58	58	0.153%	2.310%	2.463%
63	2.042%	2.310%	4.352%	63	63	0.332%	2.310%	2.642%
68	3.183%	2.310%	5.493%	68	68	0.742%	2.310%	3.052%
73	5.115%	2.310%	7.425%	73	73	1.675%	2.310%	3.985%
78	8.211%	2.310%	10.521%	78	78	3.554%	2.310%	5.864%

***Assumptions**

Term of Note	10
AFR	2.31%
Payment Frequency	Annually
Type of Note	Interest Only with Balloon Payment

Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

SCIN SALE TO AN IDGT EXAMPLE

Year	Beginning Balance	Taxable Income 10.00%	Annual Payment	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (736,470)	\$ 10,263,530
2	\$ 10,263,530	\$ 1,026,353	\$ (736,470)	\$ 10,553,413
3	\$ 10,553,413	\$ 1,055,341	\$ (736,470)	\$ 10,872,284
4	\$ 10,872,284	\$ 1,087,228	\$ (736,470)	\$ 11,223,043
5	\$ 11,223,043	\$ 1,122,304	\$ (736,470)	\$ 11,608,877
6	\$ 11,608,877	\$ 1,160,888	\$ (736,470)	\$ 12,033,295
7	\$ 12,033,295	\$ 1,203,329	\$ (736,470)	\$ 12,500,154
8	\$ 12,500,154	\$ 1,250,015	\$ (736,470)	\$ 13,013,700
9	\$ 13,013,700	\$ 1,301,370	\$ (736,470)	\$ 13,578,600
10	\$ 13,578,600	\$ 1,357,860	\$ (7,736,470)	\$ 7,199,990

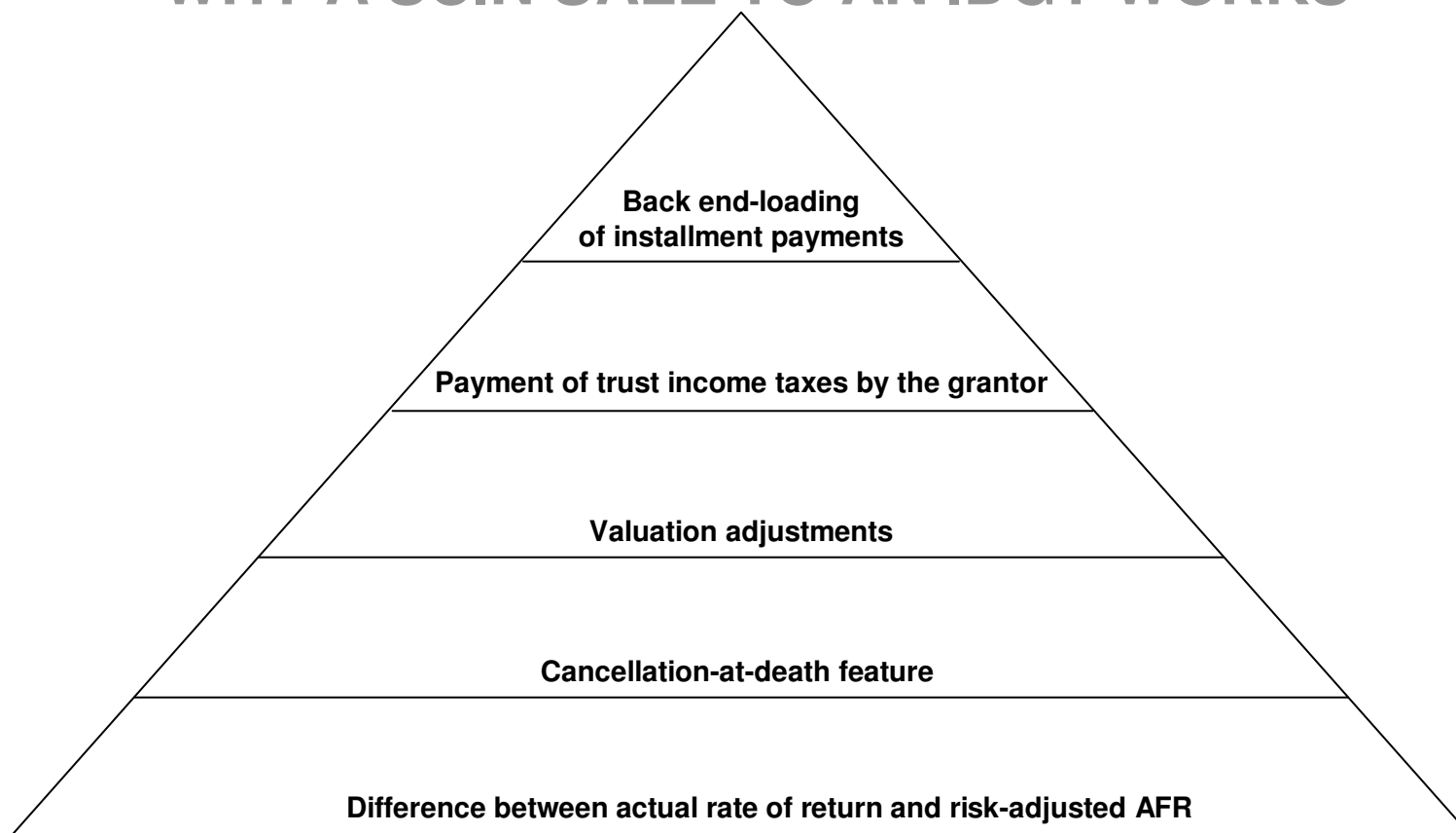
BENEFIT: \$7,199,990 transferred to beneficiaries estate/gift tax-free

***NOTE:** Assuming a 78-year-old seller and a \$7,000,000 (after valuation adjustments) interest only, balloon payment feature installment note with a 10.521% annual interest rate (2.31% long-term AFR + 8.211% mortality risk premium)

Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

WHY A SCIN SALE TO AN IDGT WORKS



Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

ADVANTAGES

- Future appreciation above the note interest rate, including the risk premium, is removed from the grantor's estate
- Asset not included in grantor's estate in case of premature death during SCIN term
- Value of assets transferred out greatly exceeds value of payments coming back into the estate of the grantor if he/she passes away prematurely
- No gain or loss on sale
- Trust income taxable to grantor allows for greater appreciation to inure to future generations, thereby creating an additional tax-free gift
- Valuation adjustments increase effectiveness of sale for estate tax purposes

Balancing Bet-to-Live and Bet-to-Die Strategies

SCIN SALE TO AN IDGT

DISADVANTAGES

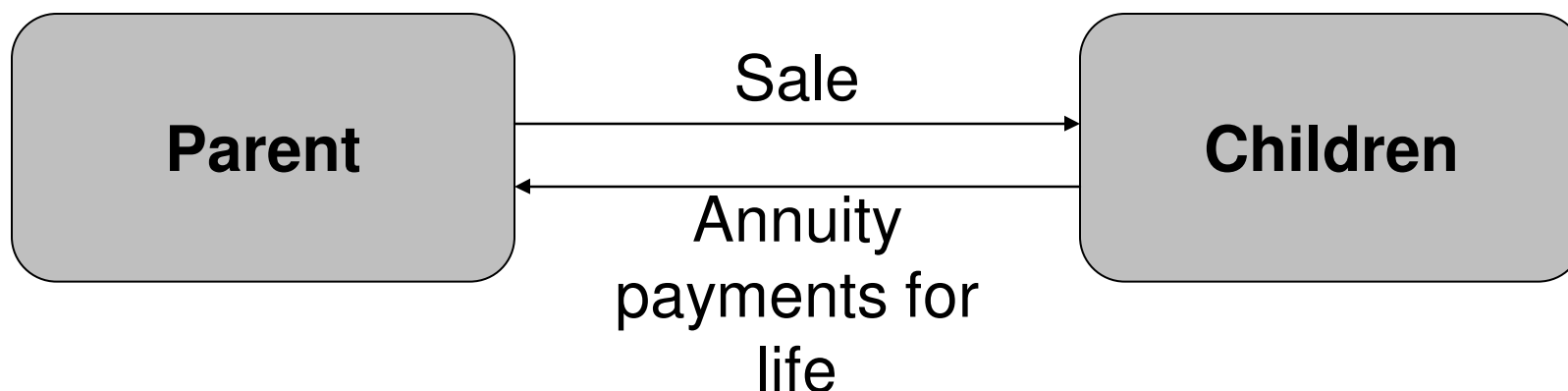
- Complex calculation of risk premium
- Possible gift tax exposure if SCIN risk premium is inadequate
- Possible gift tax exposure if trust is insufficiently funded
- Possible taxable estate inclusion under *Karmazin* (retained life estate)
- No step-up in basis at grantor's death
- Possible acceleration of capital gain at grantor's death
- Trust income taxable to grantor during his/her life could cause a cash flow problem if there is not sufficient income earned by the grantor
- Possible upstream transfer if the grantor survives the term of note (or lives a significant portion of the term and/or is relatively old)

Balancing Bet-to-Live and Bet-to-Die Strategies

PRIVATE ANNUITY

Balancing Bet-to-Live and Bet-to-Die Strategies

PRIVATE ANNUITY



The seller's age and the current IRC §7520 rate are used for purposes of determining the amount of the annuity.

Provided that the annuity is calculated correctly, the future value of the assets sold less the future value of the payment stream retained by the seller inures to the buyer (beneficiaries) free of transfer taxes, thus effectively freezing the growth of assets at the IRC §7520 rate.

The IRC §7520 rate for January 2013 is 1.0%.

Balancing Bet-to-Live and Bet-to-Die Strategies

PRIVATE ANNUITY

SAMPLE OF PRIVATE ANNUITY AMOUNTS*

Age	Private Annuity Amount
53	\$ 300,262
58	\$ 347,508
63	\$ 409,992
68	\$ 495,526
73	\$ 617,900
78	\$ 794,588

***Assumptions**

Value of Assets Sold
IRC §7520 Rate
Payment Frequency
Timing of Payment

\$7,000,000
1.00%
Annually
End of Period

Balancing Bet-to-Live and Bet-to-Die Strategies

PRIVATE ANNUITY

PRIVATE ANNUITY EXAMPLE

Year	Beginning Balance	Growth 10.00%	Annual Payment	Ending Balance
1	\$ 10,000,000	\$ 1,000,000	\$ (794,588)	\$ 10,205,412
2	\$ 10,205,412	\$ 1,020,541	\$ (794,588)	\$ 10,431,365
3	\$ 10,431,365	\$ 1,043,137	\$ (794,588)	\$ 10,679,914
4	\$ 10,679,914	\$ 1,067,991	\$ (794,588)	\$ 10,953,317
5	\$ 10,953,317	\$ 1,095,332	\$ (794,588)	\$ 11,254,061
6	\$ 11,254,061	\$ 1,125,406	\$ (794,588)	\$ 11,584,879
7	\$ 11,584,879	\$ 1,158,488	\$ (794,588)	\$ 11,948,779
8	\$ 11,948,779	\$ 1,194,878	\$ (794,588)	\$ 12,349,069
9	\$ 12,349,069	\$ 1,234,907	\$ (794,588)	\$ 12,789,388
10	\$ 12,789,388	\$ 1,278,939	\$ (794,588)	\$ 13,273,738

Benefit: \$13,273,738 Transferred to Beneficiaries Tax-Free

* Assuming a 78-year-old seller and a \$7,000,000 (after valuation adjustments) sale price

Balancing Bet-to-Live and Bet-to-Die Strategies

PRIVATE ANNUITY

ADVANTAGES

- Provides an income stream to the seller for life
- Asset not included in seller/grantor's estate in case of premature death during the annuity term
- Value of assets transferred out of the seller's estate greatly exceeds value of payments coming back if he/she passes away prematurely
- Valuation adjustments increase effectiveness of sale for estate tax purposes

Balancing Bet-to-Live and Bet-to-Die Strategies

PRIVATE ANNUITY

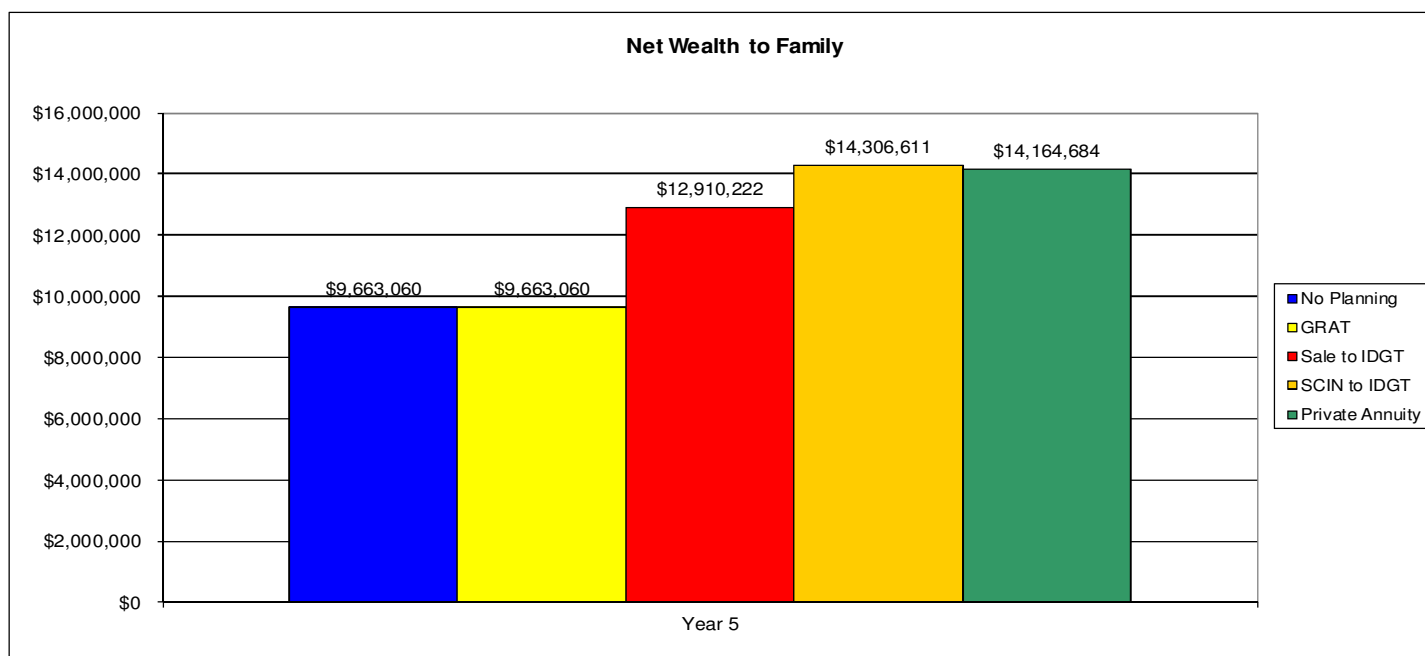
DISADVANTAGES

- Under the Proposed Treasury Regulations, an immediate gain would be recognized by the seller
- The buyer's payments are not deductible as "interest", thus causing more ordinary income to be recognized (double taxation)
- Potential upstream transfer if seller lives for a long period of time (especially if the seller lives longer than his/her life expectancy)
- If assets are sold to a trust, possible gift tax exposure could occur if the trust has inadequate assets to support the payments

Balancing Bet-to-Live and Bet-to-Die Strategies

COMPARISON OF STRATEGIES

GRANTOR DIES MIDWAY THROUGH TERM



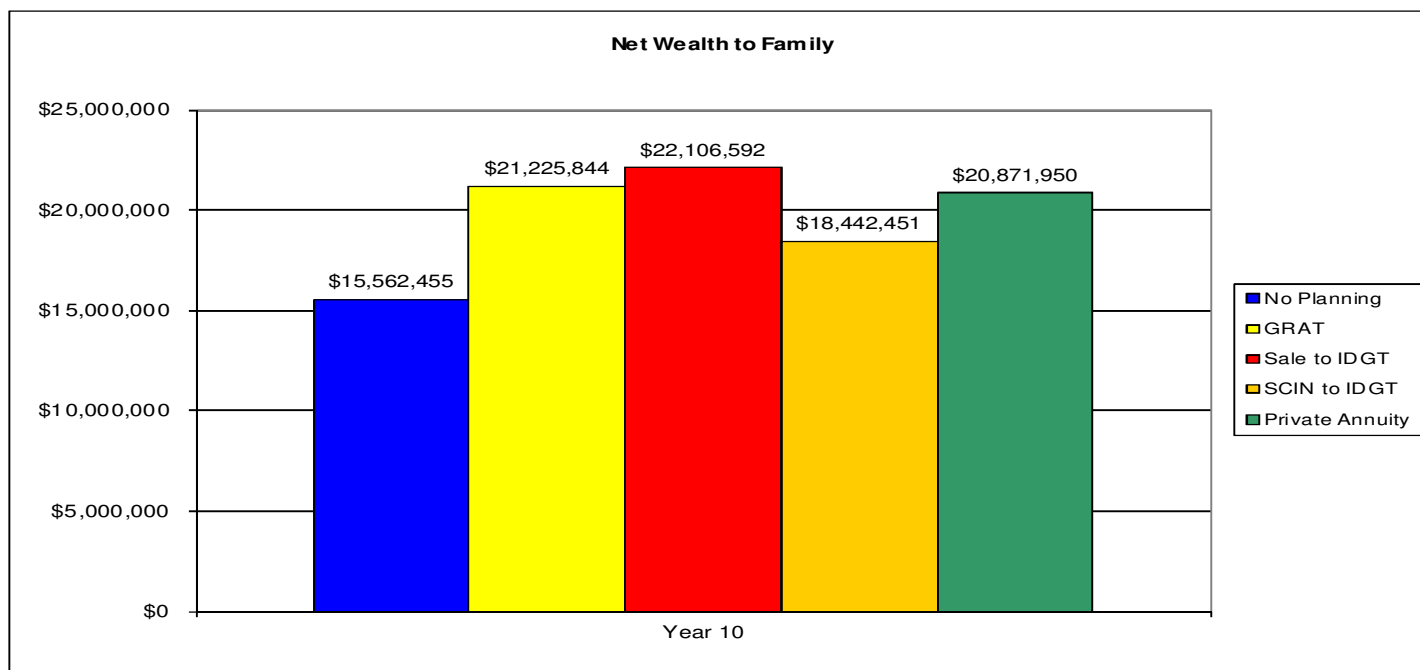
Assumptions

Gross Value of Assets Transferred	\$10,000,000
Net Value of Assets Transferred	\$7,000,000
IRC §7520 Rate	1.00%
AFR	2.31%
Term / Life Expectancy	10 Years
Payment Frequency	Annually
Type of Payment (Installment Note/SCIN)	Interest Only with Balloon Payment
Age of Seller / Annuitant	78
Estate Tax Rate	40%

Balancing Bet-to-Live and Bet-to-Die Strategies

COMPARISON OF STRATEGIES

GRANTOR SURVIVES ENTIRE TERM



Assumptions

Gross Value of Assets Transferred	\$10,000,000
Net Value of Assets Transferred	\$7,000,000
IRC §7520 Rate	1.00%
AFR	2.31%
Term / Life Expectancy	10 Years
Payment Frequency	Annually
Type of Payment (Installment Note/SCIN)	Interest Only with Balloon Payment
Age of Seller / Annuitant	78
Estate Tax Rate	40%



Balancing Bet-to-Live and Bet-to-Die Strategies

“TAX BURN” SELF- CANCELLING INSTALLMENT NOTE (SCIN)

Balancing Bet-to-Live and Bet-to-Die Strategies

“TAX BURN” STRATEGY

SUMMARY OF STRATEGY

The “tax burn” strategy basically involves an installment sale (or other transfer) to a grantor trust. The purpose of this strategy is to reduce the grantor’s gross estate by having him/her pay the annual income tax liability on behalf of the trust. In turn, the grantor’s payment of income tax on the trust’s behalf is a tax-free gift to the trust (see Rev. Rul. 2004-64).

Balancing Bet-to-Live and Bet-to-Die Strategies

“TAX BURN” SCIN™

SUMMARY OF STRATEGY

Grantor sells highly-appreciating assets to a grantor trust (such as an IDGT) in exchange for a Self-Canceling Installment Note (SCIN)



Balancing Bet-to-Live and Bet-to-Die Strategies

“TAX BURN” SCIN™

USING A SCIN TO OFFSET “TAX BURN”

- If grantor dies during term of SCIN, the note and assets sold to the IDGT are out of the grantor’s estate
- If the grantor survives the term of the SCIN, then the “Tax Burn” will have eroded the grantor’s estate to the point where the repayment of the note will not increase the grantor’s taxable estate

Year	Income Tax on IGDT Income*	Installment Payment Received From IGDT**	"Tax Burn"	Cumulative "Tax Burn"	SCIN Balance	Assets Included in Grantor's Estate
1	\$ (400,000)	\$ 378,000	\$ (22,000)	\$ (22,000)	\$ 6,300,000	\$ -
5	\$ (585,640)	\$ 378,000	\$ (207,640)	\$ (552,040)	\$ 6,300,000	\$ -
10	\$ (943,179)	\$ 378,000	\$ (565,179)	\$ (2,594,970)	\$ 6,300,000	\$ -
15	\$ (1,518,999)	\$ 378,000	\$ (1,140,999)	\$ (7,038,993)	\$ 6,300,000	\$ -
						\$ -

* \$10,000,000 FMV of assets held in IGDT x 10% return x 40% tax rate (compounded by 10% per year)

** \$6,300,000 SCIN principal (discounted) x 6% interest rate (AFR + mortality risk premium)

Cumulative effect of "tax burn" eliminates value of SCIN coming back into grantor's estate upon repayment

Asset not included in grantor's estate during note term

Balancing Bet-to-Live and Bet-to-Die Strategies

“TAX BURN” SCIN™

“TAX BURN” SCIN™ DEFINITIONS

- Initial Burn Point (a.k.a “Tax Burn”) – The point at which the income tax liability paid by the grantor becomes greater than the installment payments received from the trust.
- Full Burn Point – The point at which any cumulative reinvested “positive transfers” (i.e. installment payment received > tax liability) by the grantor and the SCIN are eliminated by the cumulative effect of the “tax burn.”

Year	Income Tax on IGDT Income*	Installment Payment Received From IGDT**	"Tax Burn"	Cumulative "Tax Burn"	SCIN Balance	Assets Included in Grantor's Estate
1	\$ (400,000)	\$ 378,000	\$ (22,000)	\$ (22,000)	\$ 6,300,000	\$ -
5	\$ (585,640)	\$ 378,000	\$ (207,640)	\$ (552,040)	\$ 6,300,000	\$ -
10	\$ (943,179)	\$ 378,000	\$ (565,179)	\$ (2,594,970)	\$ 6,300,000	\$ -
15	\$ (1,518,999)	\$ 378,000	\$ (1,140,999)	\$ (7,038,993)	\$ 6,300,000	\$ -
						\$ -

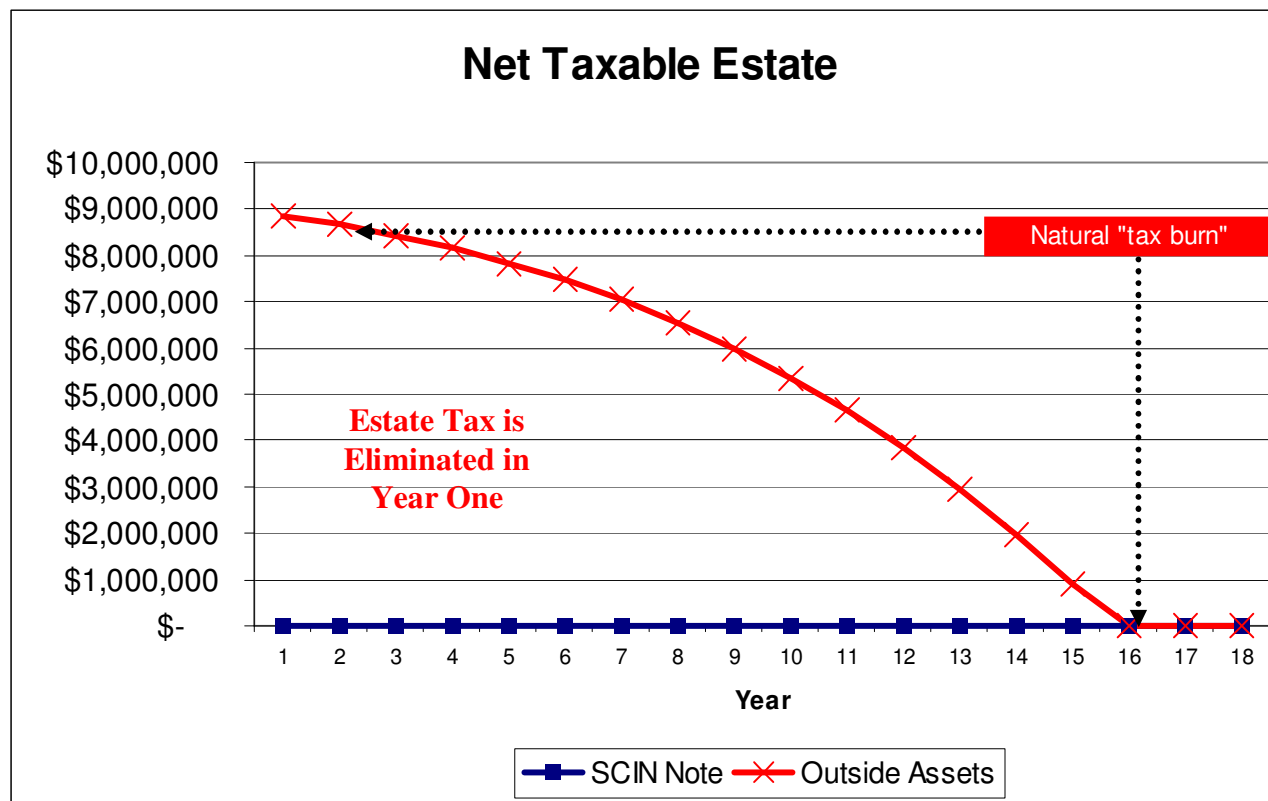
* \$10,000,000 FMV of assets held in IGDT x 10% return x 40% tax rate (compounded by 10% per year)
 ** \$6,300,000 SCIN principal (discounted) x 6% interest rate (AFR + mortality risk premium)

Initial Burn Point → (between Year 10 and 15)
 Full Burn Point → (between Year 10 and 15)

Balancing Bet-to-Live and Bet-to-Die Strategies

“TAX BURN” SCIN™

“TAX BURN” SCIN™ EXAMPLE



Required Disclosure Under Circular 230

Pursuant to the rules of professional conduct set forth in Circular 230, as promulgated by the United States Department of the Treasury, nothing contained in this communication was intended or written to be used by any taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer by the Internal Revenue Service, and it cannot be used by any taxpayer for such purpose. No one, without our express prior written permission, may use or refer to any tax advice in this communication in promoting, marketing, or recommending a partnership or other entity, investment plan or arrangement to any other party.

For discussion purposes only. This work is intended to provide general information about the tax and other laws applicable to retirement benefits. The author, his firm or anyone forwarding or reproducing this work shall have neither liability nor responsibility to any person or entity with respect to any loss or damage caused, or alleged to be caused, directly or indirectly by the information contained in this work. This work does not represent tax, accounting, or legal advice. The individual taxpayer is advised to and should rely on their own advisors.



For information on upcoming seminars and webinars, please visit our website:

www.keeblerrandassociates.com

To be added to our newsletter, please email

emily.rosenberg@keeblerrandassociates.com