PROFESSIONAL FINANCIAL SERVICES, INC.
THE PRACTICE OF INSURANCE AND FINANCIAL SERVICES
*A REGISTERED INVESTMENT ADVISOR*

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ROBERT E. TUCKER
PRESIDENT

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Ms. Faye Messer
10913 Lawyers Road
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Dear Faye:

I have (necessarily) written to you a number of times over the last few months (twice in October alone) regarding the economy. **With all of the focus on the economy, it is easy to overlook other topics that are also important.** So, in this letter I shall mention a few that may be of interest to you, as well as update you on some information regarding Professional Financial Services, Inc. Here goes.

**<u>Annual Gift Tax Exclusion</u>**

**On January 1, 2009, the annual gift tax exclusion increases to $13,000 per person per year.** You can make annual gifts up to and including $13,000/year to as many people as you wish. The gift(s) you make is not deductible to you, but it's also <u>not</u> taxable to the recipient. It's completely tax free.

Gifts of stock/securities are valued at the time the gift is completed <u>and</u> your cost basis transfers "as is." For example, suppose several years ago you bought 260 shares of IBM stock for $20/share and it's now valued at $50/share, you can gift the stock (260 shares x $50/share = $13,000) value to someone, and they receive the stock tax free. However, their cost basis is the same as yours; i.e. 260 shares x $20 = $5,200. So, if they sell the stock the next day, they would owe tax on $7,800 which is the difference between the value ($13,000) and the cost basis ($5,200).

Cash, of course, is cash. The cost basis = the value. There are no tax implications for gifts of cash.

**<u>Unified Credit (Exemption Equivalent) for Federal Estate Taxes</u>**

Each of us can convey (1) **an unlimited amount to our spouses free of any Federal estate tax and (2) up to $2,000,000 ($1,000,000 during life) in aggregate to non-spouses, e.g. children, grandchildren or others.**

Suppose a husband owns $4,000,000 of assets (not jointly). A common planning technique is to have $2,000,000 go into a Family Trust and the other $2,000,000 pass outright to their spouse. So, when the spouse dies, the surviving spouse receives $2,000,000 and the other $2,000,000 goes to the Family Trust <u>from</u> which the <u>surviving spouse</u> gets 100% of the income earned by the $2,000,000 in trust, limited rights to principal, and at the discretion of the trustee, the surviving spouse <u>could</u> receive any or all of the trust assets.

However, whatever remains in the Family Trust at the time the surviving spouse dies is not included in the surviving spouse's estate.

So, assuming the surviving spouse has $2,000,000 and the trust has $2,000,000, only the surviving spouse's $2,000,000 is in his/her taxable estate, **<u>but</u> the surviving spouse also has an exemption of $2,000,000. Therefore there's <u>no</u> tax at the death of either spouse and the entire $4,000,000 ultimately passes tax free to the heirs.**

It looks like this:

**Husband's assets = $4,000,000**

**<u>Husband Dies</u>**

| <u>To Spouse</u> | | <u>To Family Trust</u> | |
|---|---|---|---|
| **Outright to Spouse** | **$2,000,000** | To Family Trust | $2,000,000 |
| Less Marital Deduction | - $2,000,000 | Less Exemption | - $2,000,000 |
| Federal Tax Due | 0 | Federal Tax Due | 0 |

**<u>Wife Dies Subsequently</u>**

| | | | |
|---|---|---|---|
| **Wife's Assets** | **$2,000,000** | Amount in Family Trust | $2,000,000 |
| Wife's Exemption | - $2,000,000 | | N/A |
| Tax Due | 0 | | N/A |

Wife's Assets $2,000,000 + Trust = $2,000,000

**$4,000,000 Tax Free to Heirs**

**<u>What's the point</u>? On January 1, 2009, the exemption goes to <u>$3,500,000</u> per person. The problem (if one exists) may lie in the drafting of the legal documents.** In the methodology described above, it is common for the legal documents to say (essentially) **when the first spouse dies the amount needed <u>to take advantage fully of the exemption automatically</u> goes to the Family Trust and <u>the balance</u> goes outright to the spouse.**

If you have that type of language in your legal documents, the result can be that as of January 1, 2009, the spouse will receive $500,000 outright with $3,500,000 going to the Family Trust. **The federal estate tax <u>will still be zero at both deaths</u>, but the surviving spouse may be more than a little surprised (not to mention displeased) at what will happen at the husband's death.**

Here's how:

**Husband's assets = $4,000,000**

**Husband Dies**

| To Spouse | | To Family Trust | |
|---|---|---|---|
| **Outright to Spouse** | **$500,000** | **To Family Trust** | **$3,500,000** |
| Less Marital Deduction | - $500,000 | Less Exemption | - $3,500,000 |
| Federal Tax Due | 0 | Federal Tax Due | 0 |

**Wife Dies**

| | | | |
|---|---|---|---|
| **Wife's Assets** | **$ 500,000** | Amount in Family Trust | $3,500,000 |
| Wife's Exemption | $3,500,000 | | N/A |
| Tax Due | 0 | | N/A |

**Wife's Assets** $\underbrace{\textbf{\$500,000} + \text{Family Trust \$3,000,000}}$

**$4,000,000 Tax Free to Heirs = Same Result to Heirs**

So, again, the result to the heirs is the same. **The result FOR THE SPOUSE during remaining lifetime is definitely NOT THE SAME.**

**Can this "undesirable result" happen without you doing anything? <u>Absolutely possible</u>. Can it be fixed? You bet – provided <u>you take action</u>!**

What's required is to review (1) your current assets and titling, (2) your current life insurance coverage amounts, ownership and beneficiary arrangements, and (3) your current legal documents.

I fully expect that a more in-depth explanation may be necessary to help you understand any implications that may apply to you. **In my opinion, if your total assets (husband and wife) total <u>more than $2,000,000</u> (<u>including</u> life insurance) you should have us review your planning. Don't be seduced by the notion that an estate of $3,500,000 or less has no problem. It isn't necessarily so.**

**<u>Please call to schedule an appointment so that we can discuss this issue</u>.**

**Registered Investment Advisor**

Every year Professional Financial Services, Inc. renews its registration with the Securities Departments of Virginia, Maryland and the District of Columbia as a Registered Investment Advisor (RIA). The registration document (ADV) and the Client Advisory Agreement are available upon request and I will be happy to send one to you or whomever you might designate. Just let us know.

**Dayna Dragoi**

In August, a valued client referred me to Dayna Dragoi as a potential candidate for an opening in our office. A college graduate with a degree in marketing from Virginia Tech, I was instantly impressed with her skills and professionalism. So impressed that she has become the newest member of Professional Financial Services, Inc. Dayna joins Faye Messer and Susie Ragan in rounding out the in-office staff and she is a perfect fit.

**Conclusion**

Well, that's all for now. It has been and continues to be an eventful year. Perhaps now that the Presidential and Congressional elections are over, we can begin to see some POSITIVE momentum going forward.

Happiest of Holidays to you and your family and thank you for the continued opportunity to be of service.

Best regards,

Robert E. Tucker, CLU
Chartered Financial Consultant

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