



Hinman, Howard & Kattell, LLP

ESTATE TAX PLANNING

- What is the estate tax?
 - One-time separate, non-income tax based on the fair market value of assets owned at the time of death in excess of the exemption amount
- Estate tax planning options that are designed to:
 - Reduce the tax
 - Provide a source of funds to pay the tax







ASSETS INCLUDED IN GROSS ESTATE

- Real Estate
- Investments
- Retirement benefits (including 401(k) and IRA)
- Life insurance if policy owned by the decedent
- Closely held businesses LLC created for oil and gas purposes

HH&K



Hinman, Howard & Kattell, LLP



HOW IS THE ESTATE TAX CALCULATED?

Hinman, Howard & Kattell, LLP

No estate tax if the value of assets are less than the current exemption amount.

- Take an inventory of all property interests owned by the decedent.
- Fair market value as of date of death not what the decedent paid for it.
- There is both a Federal Estate Tax and State Estate Tax

HH&K 9



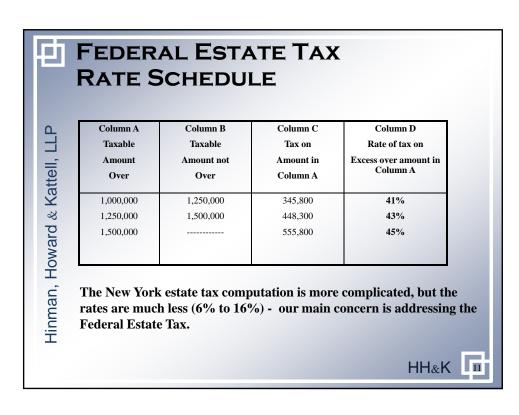


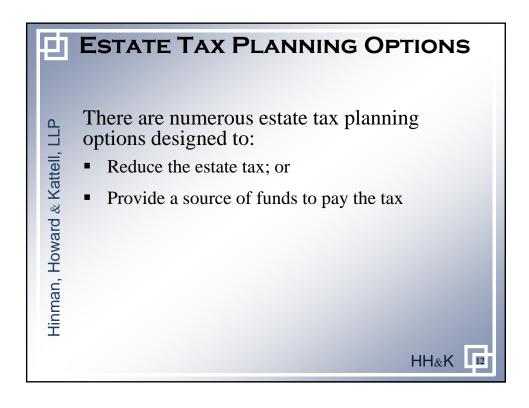
The size of the Federal Estate Tax Exemption Amount depends upon the decedent's year of death.

Hinman, Howard & Kattell, LLP

Year of Death	Federal Exemption Amount
2001	\$675,000
2002-2003	\$1,000,000
2004-2005	\$1,500,000
2006-2008	\$2,000,000
2009	\$3,500,000
2010	TAX REPEALED
2011	\$1,000,000

The size of the New York Estate Tax Exemption amount is \$1,000,000. Pennsylvania ranges from 0 to 15% but typically 4.5% after deductions. Waiting for Congress to Act? HH&K







ESTATE TAX PLANNING OPTIONS

Hinman, Howard & Kattell, LLP

- \$13,000 annual gift tax exclusion
- Credit shelter trust/QTIP trust
- There is no estate tax when the first spouse dies – it is taxes upon the death of the second spouse.
- Life insurance
- Charitable giving
- Estate Freeze / Discounting Techniques





How Does the Annual GIFT TAX EXCLUSION WORK?

Hinman, Howard & Kattell, LLP

- A person (the donor) can make gifts of up to \$13,000 gift per donee (the person receiving a gift) per year with no gift or estate tax implications. If the donor is married, the donor could make gifts up to \$26,000 per donee per year.
- Applies to anyone: children, grand-children, their spouses, friends.

HH&K





How Does the Annual Gift TAX EXCLUSION WORK?

Hinman, Howard & Kattell, LLP

Can use a trust – restrict use of qualified funds for specific purpose, such as college education.

- Estate Tax Benefit: Reduces size of estate by removing gifted asset and future growth on asset; therefore reduces estate tax.
- Donee does not pay income tax on gift.
- Donor may have to file Federal gift tax return (IRS Form 709).







ESTATE TAX PLANNING OPTIONS

Hinman, Howard & Kattell, LLP

Credit Shelter Trust

- Unlimited marital deduction allowed for all property passing to surviving spouse upon death of decedent.
- Why not simply leave everything to spouse to avoid estate tax?

HH&K





TWO MAJOR PROBLEMS WITH GIVING EVERYTHING TO SPOUSE

Hinman, Howard & Kattell, LLP

- Estate tax payable on combined estates when surviving spouse dies. Only able to use one unified credit exemption amount upon death of surviving spouse.
- Testator may want to leave assets to someone other than spouse.







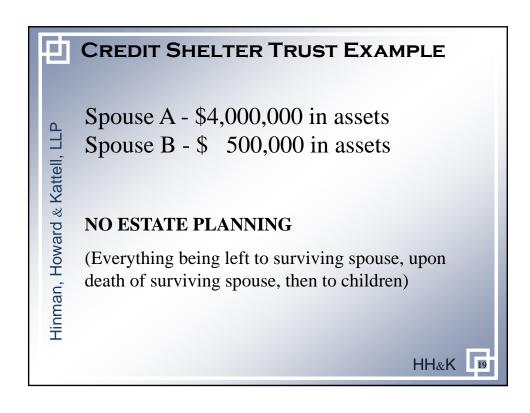
BETTER APPROACH

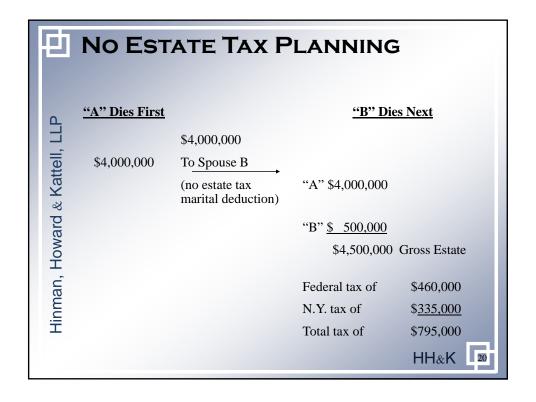
Hinman, Howard & Kattell, LLP

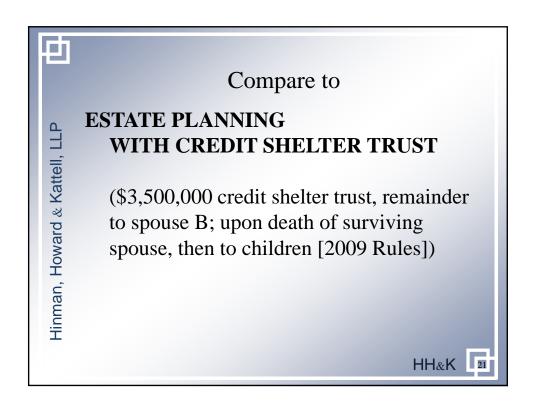
- Try to utilize unified credit exemption amount available to both spouses.
- Not \$3,500,000 per couple it is \$7,000,000 per couple [2009 Rules]
- One way to fully utilize both exemption amounts is through the use of credit shelter trusts in both spouse's wills.

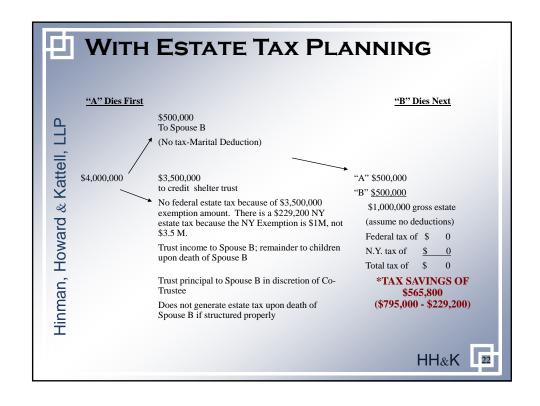
HH&K













FOR CREDIT SHELTER TRUST TO WORK, Two Steps Must Be Followed:

Hinman, Howard & Kattell, LLP

- Each spouse's will must be drafted with credit shelter trust provisions in it.
- Each spouse should have a certain amount of assets in his or her name alone. Joint assets don't help. Assets with designated beneficiaries (life insurance, IRAs) don't help, unless beneficiary designation is changed to the trust.







Hinman, Howard & Kattell, LLP

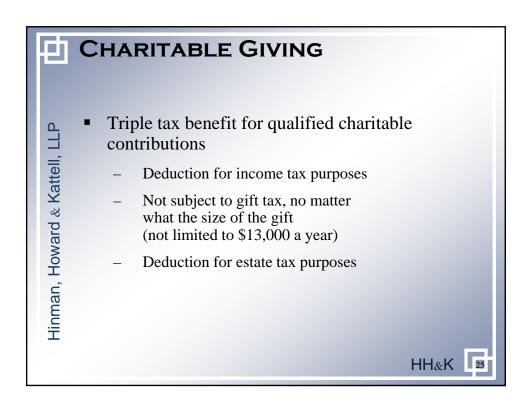
LIFE INSURANCE AND ESTATE TAX PLANNING

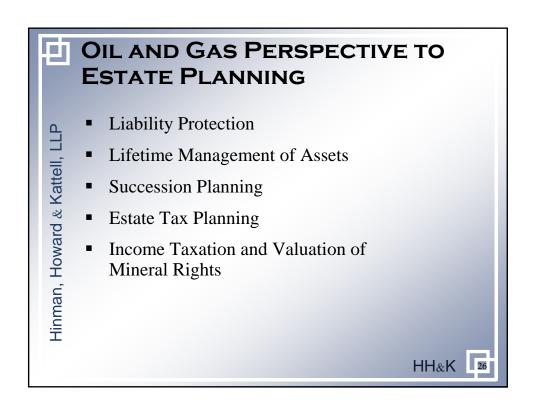
Life insurance is subject to estate tax if the policy was owned by the decedent. However, if the policy is owned by someone other than decedent, then the insurance is not subject to estate tax.

- Have life insurance policy owned by an irrevocable life insurance trust or someone other than the insured (such as insured's children)
- Make sure you have an adequate level of insurance
 - Liquidity for need of beneficiaries
 - Liquidity for payment of taxes, both estate and income
 - Liquidity to fund buy-sell agreements

HH&K 24









LIABILITY PROTECTION

Hinman, Howard & Kattell, LLP

Hinman, Howard & Kattell, LLP

- Are you Protected from personal liability if something goes very wrong?
- Who is going to be named in a lawsuit?
- Look at the indemnification clause in your lease.
- Look at your homeowner insurance policy and talk to you agent.







- Separate Legal Entity
 - Also corporations family limited partnership
 - (PA) Capital Stock Tax (for now)
 - Starting a Business to Manage this Asset
- No double taxation, income flows to the members of the LLC
- Asset must be transferred to LLC

HH&K 28



14



THE LIMITED LIABILITY **COMPANY "LLC"**

Hinman, Howard & Kattell, LLP

Generally, managed by the members (similar to shareholders in a corporation)

- Operating Agreement to provide for orderly management of business and rules between members
- If done correctly LLC will limit your personal liability.







Hinman, Howard & Kattell, LLP

LIFETIME MANAGEMENT **OF ASSETS**

- Who owns the Property now?
- Husband and Wife vs. Single Person
 - **Determines Control**
 - Income Distribution
- Initially the current owners will be Members of LLC
 - **Operating Agreement**
 - Determine How Decisions are made
 - Member Managed vs. Manager
 - What will happen in the future

HH&K



Hinman, Howard & Kattell, LLP



- Do you want to include children?
 - Would have an ownership interest
 - Could share in decision making (Manager Managed)
 - Would share in income distribution of royalties based upon percent of ownership
 - Gift Membership interest over time





Why Transfer Membership Now?

- Can over time remove an asset with a very high future value from your estate and potentially avoid or lesson estate tax burden.
- Maximizing use of lifetime Unified Credit / Annual Exclusion Gifting at Lower value of property vs. after bonus / royalties paid.
- Can annually gift membership interest to each child with a value of up to \$13,000/\$26,000 spilt without effecting the Unified Credit.

HH&K



Hinman, Howard & Kattell, LLP



ESTATE FREEZE/DISCOUNTS

Hinman, Howard & Kattell, LLP

- Freeze values of assets at today's values so that all future appreciation occurs outside of a person's estate
- Transfer of assets by Donor to LLC in return for LLC interests
- Transfer of LLC Interests by Donor to Donor's children or trust created for the benefit of Donor's children







ESTATE TAX BENEFIT OF CREATING LLC

Hinman, Howard & Kattell, LLP

- The first level of discounting occurs when the donor's property is transferred into the LLC. This discount is for equity in a "private illiquid company"
- The LLC interests that are transferred to the donor's children (or a trust) are discounted for "lack of marketability" and "minority interest". Total discount could range from 20% to 40%

HH&K 34



Hinman, Howard & Kattell, LLP

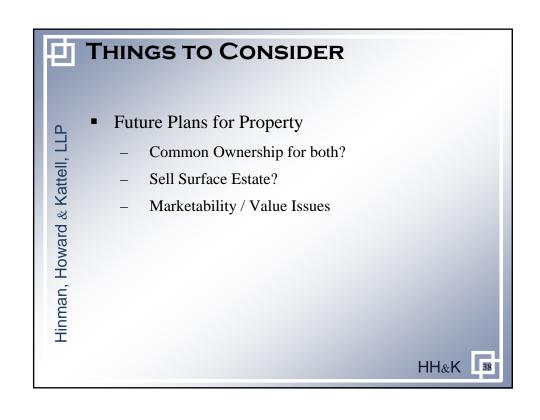


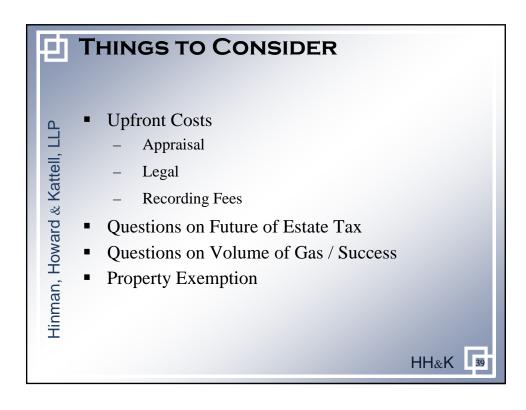
- Value of gifted LLC interest are fixed as of the date of transfer at the discounted value
- All future appreciation of the gifted LLC interest will be attributed to the gifted interest and thus will not be included in the Donor's estate
- Donor still has some control over the LLC as the LLC Manager

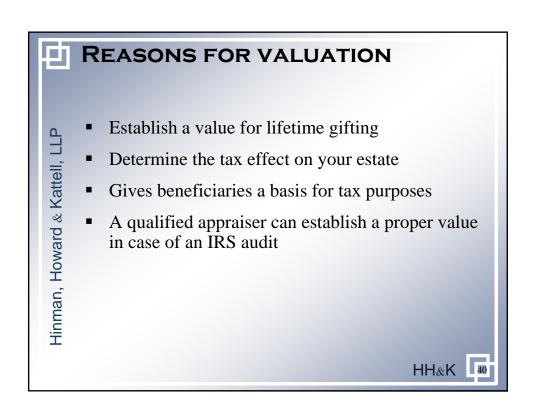
HH&K 35

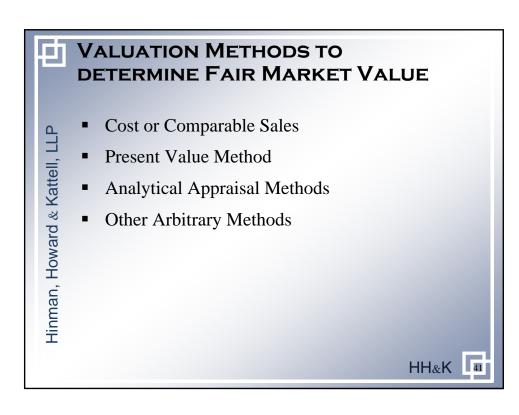
■ Business Partners - Determine how business managed / transfer to others ■ Single Person - Need an Estate Plan - Change in Status in future - Charitable Gifts HH&K















VALUATION OF MINERAL RIGHTS WITH A LEASE IN PLACE BUT NO GAS PRODUCTION

Hinman, Howard & Kattell, LLP

- Comparable Sales or Present Value method can be used
- Mineral Rights must be considered
- Discounts due to drilling and production speculation allowed
- Middle of the road valuation of mineral rights







Hinman, Howard & Kattell, LLP

VALUATION OF MINERAL RIGHTS WITH ACTIVE WELLS IN PRODUCTION

Comparable Sales or Present Value method can be used

- Mineral Rights must be considered
- Only discount is for future production risk
- Highest valuation of mineral rights

HH&K 44



22



INCOME TAX CONSEQUENCES

Hinman, Howard & Kattell, LLP

- Gas Lease Bonus Payments are considered normal income
- Income tax may be due on the entire bonus amount the year the lease is signed even if bonus is paid out in annual installments
- Royalty payments are considered normal income
- Sale of mineral rights will be considered capital gain







- Hinman, Howard & Kattell, LLP
- Overall Estate Plan
 - Will, Trust, LLCs, Gifting
- Pass on Wealth, Limit Estate, Tax Expense
- Team Approach
- Not One Plan Fits All
- Don't do it Yourself
- Don't put it off

HH&K 46

