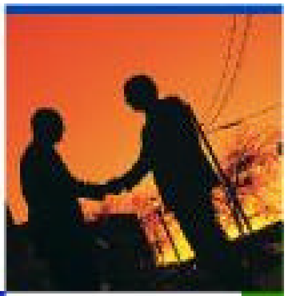
Hale and Dorr LLP

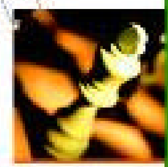
Gifting Strategies

Charitable Gifts

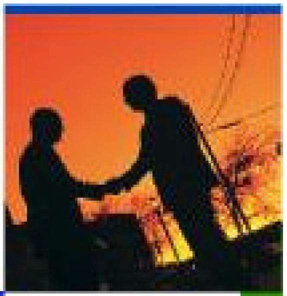
> Advantages

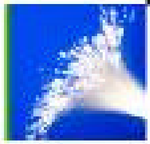
- Income tax deduction
- No gift tax
- Decrease size of estate
- Personal satisfaction

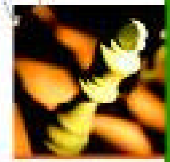




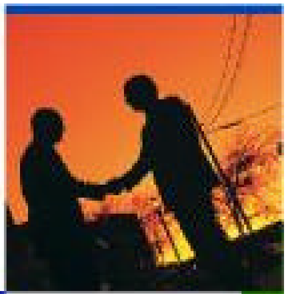
Charitable Gift Opportunities

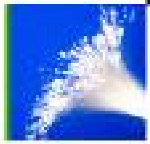


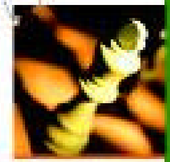




- Significant wealth
- Spike in income
- Appreciated property
- Charitable intent







Timing of Income Tax Deduction

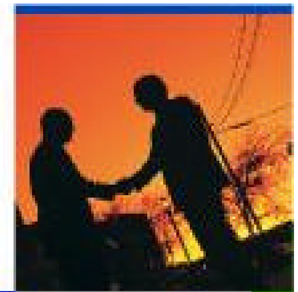
> One may deduct the value of a charitable gift only in the year in which the gift is paid (or, in some cases, in which the gift is irrevocably set aside)

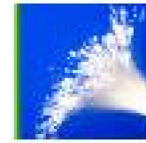
Limitations on Income Tax Deduction

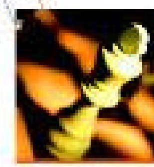
> The amount of the deduction is subject to limitations that relate to the donor's "contribution base"

> The "contribution base" in a given year is, in general, the donor's adjusted gross income

Limitations on Income Tax Deduction



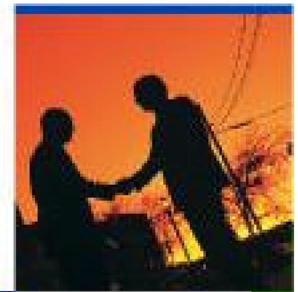


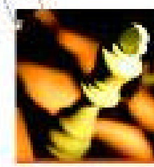


> Limitations are based on:

- Character of charitable donee
- Character of gifted property

Limitations on Income Tax Deduction





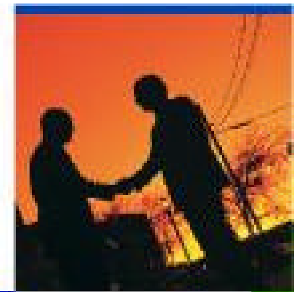
> Gifts to public charities

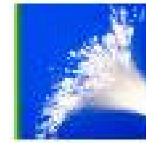
- Deduction for gifts of cash limited to 50% of contribution base
- Deduction for gifts of long-term capital gain securities limited to 30% of contribution base

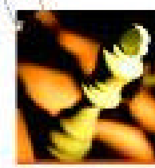
> Gifts to private foundations

- Deduction for gifts of cash limited to 30% of contribution base
- Deduction for gifts of long-term capital gain **publicly traded** securities limited to 20% of contribution base

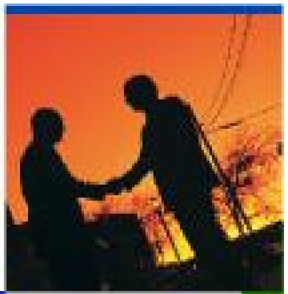
Limitations on Income Tax Deduction

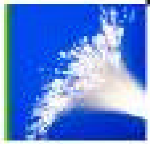


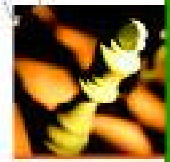




- Charitable gifts that exceed the applicable limitation may be carried forward and deducted for up to 5 years following year of gift







Types of Charitable Gifts

> Outright gifts

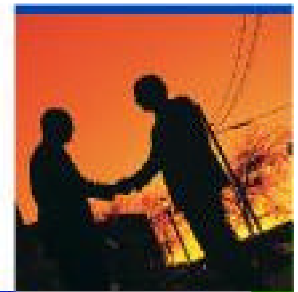
> Gifts (to a public charity) subject to a retained interest

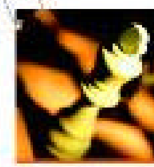
- Gift annuity
- Pooled income fund
- Charitable remainder trust
- Charitable lead trust

> Private foundation

Gifts to Family and Others

- Opportunities to make tax-free gifts
- Decreases size of estate
- Reduces income
- Shifts wealth and income to younger generations



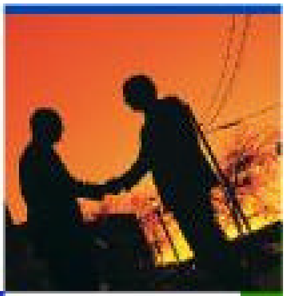


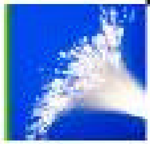
Tax-Free Gifts

> Annual exclusion gifts
  - $11,000 per donee
  - Unlimited number of donees

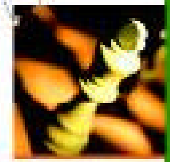
> Gifts of tuition or medical expenses
  - Must make payment directly to school or health care provider
  - Covers tuition only

529 Plans



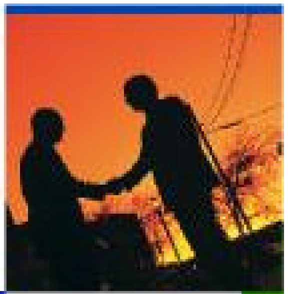


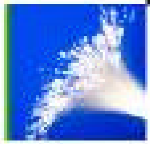
- Contributions to 529 Plans qualify for the gift tax annual exclusion
- Option to front-load 529 Plan with $55,000, free of gift tax

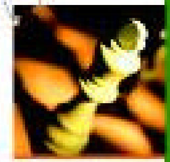


- Income tax deferral
- No income tax on distributions for qualified educational expenses
- No income limitations on donors
- Retention of controls

Taxable Gifts

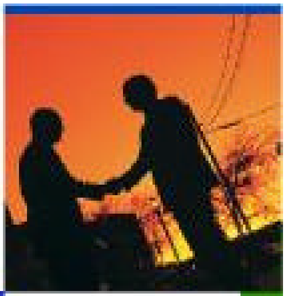


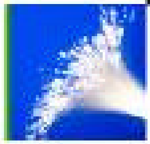


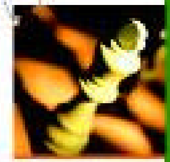


- Gift tax exemption frozen at $1,000,000
- Gift tax exemption utilized during lifetime deducted from estate tax exemption available at death
- Advisable to make taxable gifts of property which are likely to appreciate
- Preferable to pay gift tax rather than estate tax – “Sam Walton” strategy

Taxable Gifts – Illustration





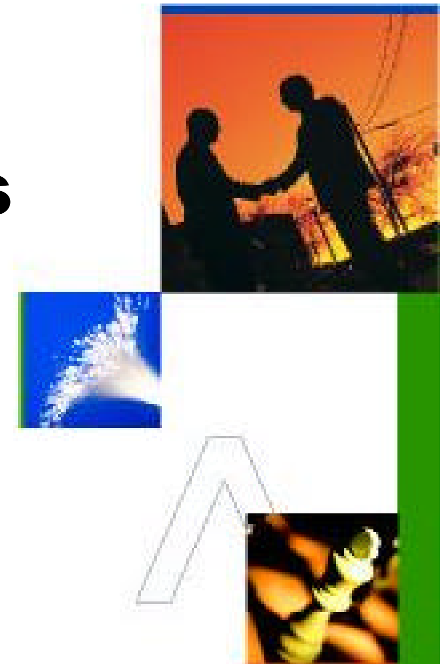


- Assume that individual with net worth of $5,000,000 as of December 1, 2003 owns securities worth $1,000,000
- Assume that securities grow in value to $2,000,000 by December 31, 2006
- Assume that individual dies on December 31, 2006 with a taxable estate of $6,000,000
- Total tax liability: $1,840,000

Taxable Gifts - Illustration

> Assume that individual with net worth of $5,000,000 makes gift of securities worth $1,000,000 on December 1, 2003
> Assume that securities grow in value to $2,000,000 by December 31, 2006
> Assume that individual dies on December 31, 2006 with a taxable estate of $4,000,000
> Total tax liability: $1,034,200
> Tax savings: $805,800

Types of Gifts to Family and Others



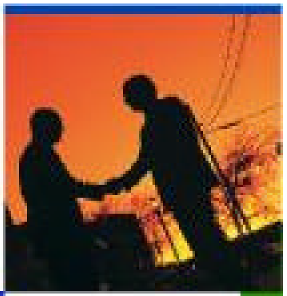
> Outright gifts

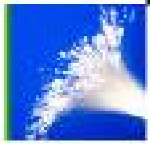
> Gifts to custodian (UTMA)

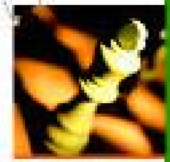
> Gifts in trust

- Flexibility regarding distributions
- Creditors' rights protections
- Potential GST tax advantages

Estate Planning Issues





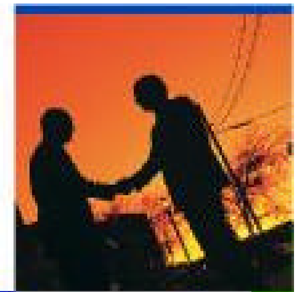


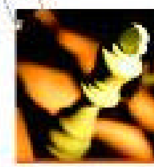
Annual Review of Estate Plan

- > Review goals
- > Review dispositive provisions of plan
- > Review selection of fiduciaries

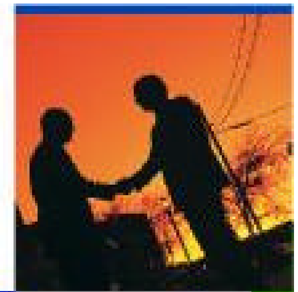
Review of Fiducaries

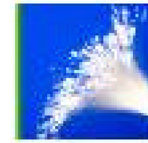
- Guardians
- Executors
- Trustees
- Attorneys-in-fact
- Health care agents

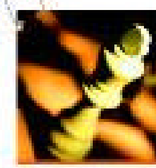




Planning for Disability

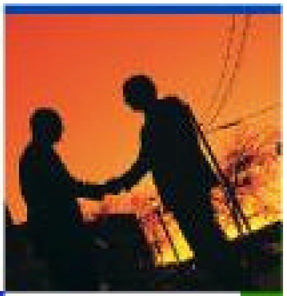


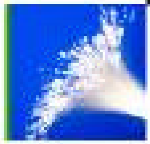




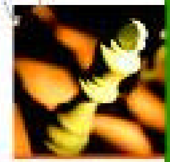
- Durable powers of attorney
- Health care proxies

Annual Review of Life Insurance

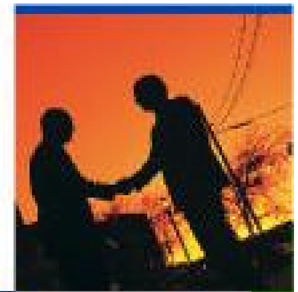


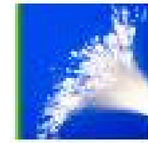


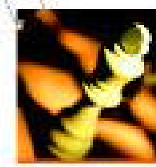
- Determine whether insurance adequate
- Review ownership of policies and beneficiary designations



State Death Taxes







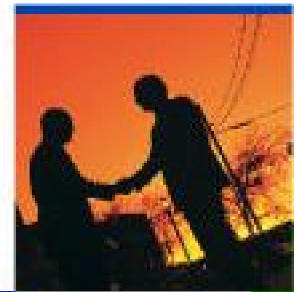
> Before 2001– Most states had “sponge tax” regimes

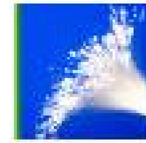
- Death tax equaled the maximum credit for state death taxes payable as an offset against federal estate tax liabilities

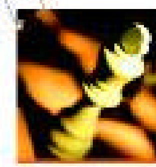
> Economic Growth Tax Revenue & Recovery Act of 2001

- Included phase-out of state death tax credit in stages between 2002-2005
- In 2005, the state death tax credit will be replaced with a federal estate tax deduction for state death taxes paid

State Death Taxes

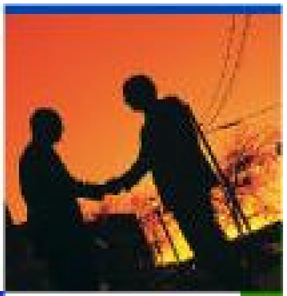


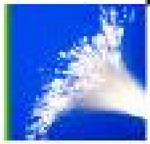


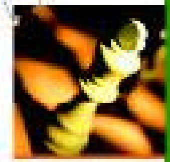


- The phase-out of the state death tax credit effectively phases out state death taxes in “sponge tax” states
- Many former “sponge tax” states, including Massachusetts, have adopted new state death tax schemes to recoup tax revenues

State Death Taxes





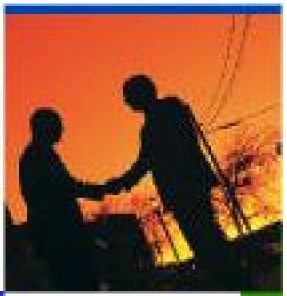


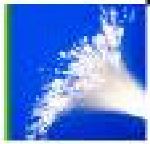
> For married couples who are residents of MA and other states that have new state death tax laws, trust amendment may be required to defer state death taxes until death of survivor.

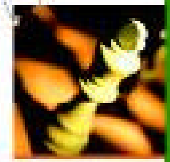
> Otherwise, potential MA estate tax upon death of first spouse to die:

- 2003 – $33,200
- 2004-2005 – $64,400
- 2006-2008 – $99,600
- 2009 – $229,200

State Death Taxes

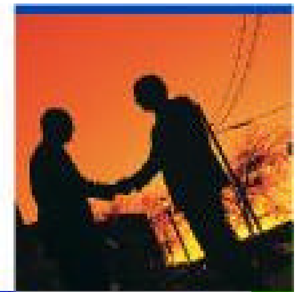


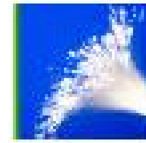


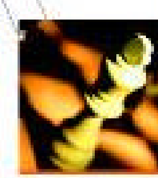


- Some states, including NH and FL, have not modified their “sponge tax” regimes. These states will not collect state death taxes for persons dying on or after January 1, 2005, assuming no state tax law changes are made before then
- In some cases, it may be advantageous to establish domicile in a state that does not collect state death taxes

State Death Taxes – Illustration

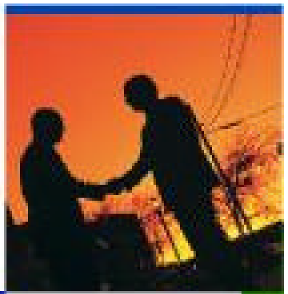


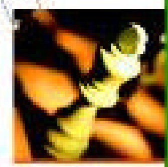




- Assume that an unmarried MA resident dies in 2005 with a taxable estate of $4,100,000
- Under the new MA tax scheme, the amount of MA estate tax will be $290,800
- The federal estate tax, after the deduction for state death taxes paid, will be $1,075,324
- Total estate tax liability: $1,366,124

State Death Taxes – Illustration



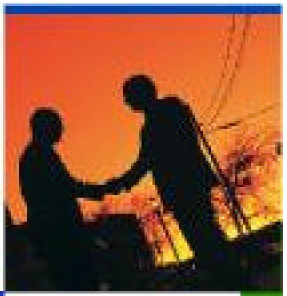


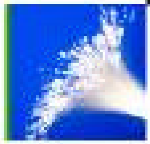
- Assume that an unmarried FL resident dies in 2005 with a taxable estate of $4,100,000
- Assume that no change in the FL Constitution to modify the existing state death tax scheme
- The amount of FL tax will be $0
- The amount of federal estate tax will be $1,212,000
- Total estate tax liability: $1,212,000
- Tax savings: $154,124

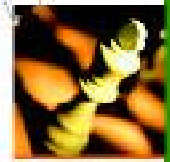
State Death Taxes – Domicile

> Suggestions to demonstrate change in domicile:

- Sale of real estate in former domicile
- Purchase of real estate in new domicile
- Transfer of bank accounts, brokerage accounts and other financial arrangements to new domicile
- Driver's license and voter registration in new domicile
- Participation in community groups in new domicile

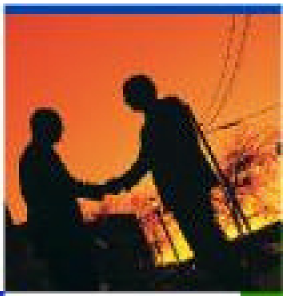


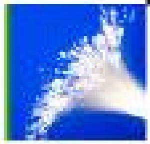


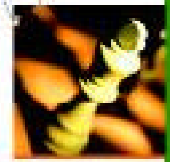


Reap the Full Benefits of the 2003 Federal Income Tax Cut

Highlights of the 2003 Federal Income Tax Cut



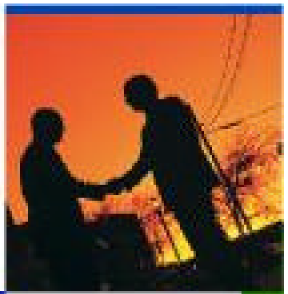


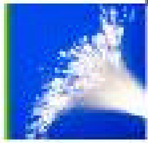


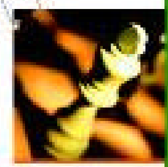
> 2001 federal income tax cuts are accelerated

- The 2001 tax cut set out a schedule whereby, over time, tax rates on ordinary income would decrease
- The 2003 tax cut fully accelerates the 2001 tax cuts on ordinary income
- Although the 2003 tax cut was passed in May, its ordinary income tax rate reduction provisions apply retroactively to January 1, 2003

Highlights of the 2003 Federal Income Tax Cut



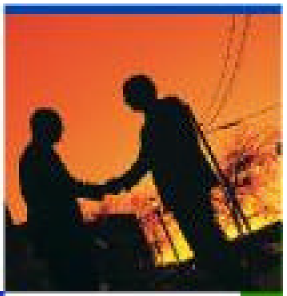


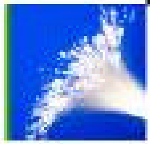


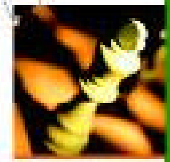
2003 Federal Income Tax Rate Changes

	2003 Rate Without Cut		2003 Rate With Cut
Highest Bracket	38.6%	→	35%
2nd-Highest Bracket	35%	→	33%
3rd-Highest Bracket	30%	→	28%
4th-Highest Bracket	27%	→	25%
5th-Highest Bracket	15%	→	15%
Lowest Bracket	10%	→	10%

Highlights of the 2003 Federal Income Tax Cut



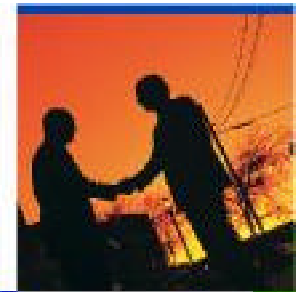


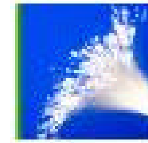


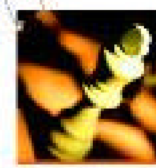
> Capital gains and dividend tax rates are lowered

- The 2003 federal income tax cut lowers the maximum capital gains rate to 15%
- For lower income individuals (i.e., those in the 10% and 15% wage brackets), the maximum capital gains rate is 5%
- The lower capital gains rates apply to capital assets sold after May 5, 2003
- Dividends are now taxed at capital gains tax rates
- The May 5th transition date does not apply to dividends, which are taxable at the lower rates for all of 2003

Effects of the Lower Capital Gains/Dividend Rates





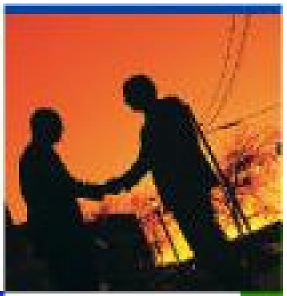


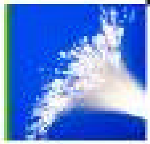
- The 15% rate on dividends makes dividend-paying investments more attractive
- Similarly, the 15% maximum capital gains rate makes the next few years a good time to sell appreciated capital assets
  - Note that capital gains attributable to collectibles are still taxed at a 28% rate

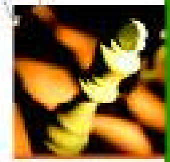
Choice of Entity Considerations

> By lowering the tax rate on dividends, the 2003 tax cut has removed some of the effects of the double taxation of corporations and their shareholders and has made C corporations more attractive

- Investors in S corporations or partnerships should consider whether a C corporation now would be more suitable to their needs





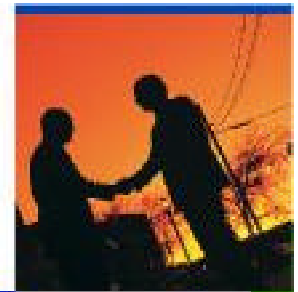


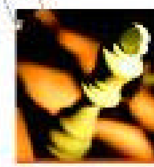
“Reasonable Compensation” Considerations

> The new 15% rate on dividends may also have an effect on compensation to shareholder-employees

- Unreasonably high compensation paid to a shareholder-employee was often automatically reclassified by the IRS as a dividend
- With the 15% rate on dividends, such a reclassification actually might be a benefit to the shareholder-employee
- The 15% rate on dividends may completely alter the way the IRS looks at “reasonable compensation” issues and, in many cases, may cause the IRS not to question compensation arrangements in closely-held companies

Other Incentives in the 2003 Federal Income Tax Cut

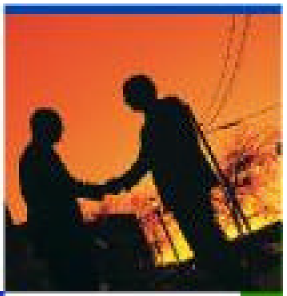


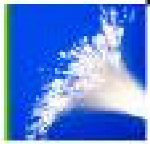


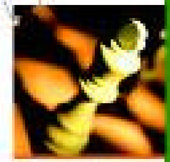
> Section 179 deduction is increased

- The Section 179 deduction allows taxpayers to expense certain qualified property in the year of purchase instead of capitalizing and depreciating it
- The maximum Section 179 deduction increases from $25,000 to $100,000 and is effective for tax years 2003 through 2005
  - the deduction, however, is limited based upon the amount of qualified property placed into service and the taxpayer's income received from a trade or business, including wage and salary income

Other Incentives in the 2003 Federal Income Tax Cut



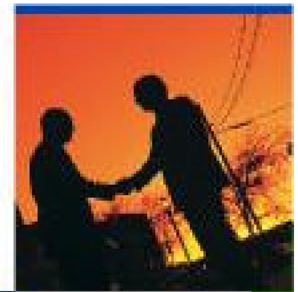


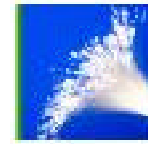


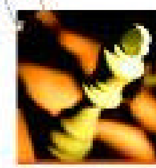
> "Bonus depreciation" is increased from 30% to 50%

- The 2003 federal income tax cut increases a bonus depreciation allowance that was originally passed in 2002
- This new benefit generally is available for qualified property placed in service after May 5, 2003 and before January 1, 2005
- The bonus depreciation is in addition to the regular first-year depreciation that would be taken on the asset and is equal to 50% of the adjusted basis of the qualified property

Bonus Depreciation Example







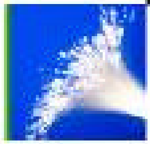
> On October 31, 2003, the Red Sox acquire and put into service new computer equipment costing $200,000

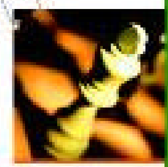
> In 2003, the Red Sox can claim $120,000 in depreciation, consisting of:

- $100,000 in bonus depreciation ($200,000 x 50%) +
- $ 20,000 in regular first-year depreciation ([$200,000 – $100,000] x 20%)

Avail Yourself of “Tried and True” Income Tax Planning

Basic Year-End Planning





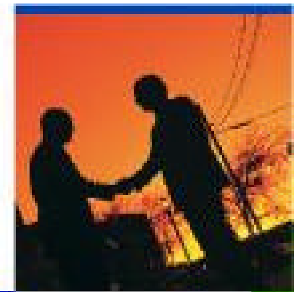
> $3,000 of capital loss can be used each year to offset ordinary income

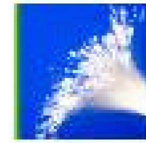
- If you have no capital losses, consider generating a loss to take advantage of the $3,000 offset

> Try to maximize itemized deductions

- Plan your charitable giving
- Consider pre-paying any state or local tax due in 2004 in 2003
  - because state and local taxes are items of tax preference for the alternative minimum tax (AMT), care should be taken when pre-paying state or local taxes if you are subject to the AMT

Alternative Minimum Tax Planning





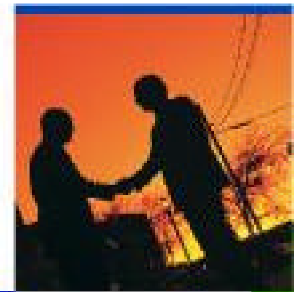
> The AMT is a parallel tax to the regular tax that takes into account items of “tax preference” and makes certain adjustments for a separate minimum tax calculation

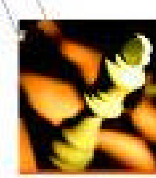
> If AMT liability exceeds regular income tax liability, then you pay the AMT

> One strategy to avoid the AMT is to move preference items and adjustments into future years. Some examples include:

- Miscellaneous itemized deductions
- Taxes
- Interest
- Qualified small business stock (QSB Stock) sales (discussed later)

Alternative Minimum Tax Planning



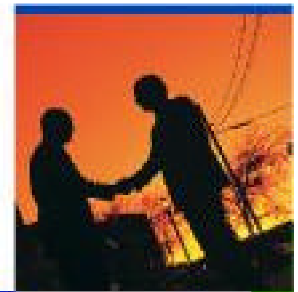


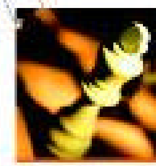
> Because income recognized on the exercise of an incentive stock option (ISO) is taxable for AMT purposes, an exercise of an ISO that is "in the money" may cause a significant AMT liability

> One strategy to avoid the AMT generated under an ISO is to sell the stock purchased upon the exercise of an ISO in the same year as the exercise

- AMT is not due if an ISO is exercised and the acquired stock is sold in the same year
- Although this may cause a "disqualifying disposition", if the stock has depreciated in value since the exercise, the favorable treatment in avoiding the AMT may outweigh the negative aspects of the disqualifying disposition

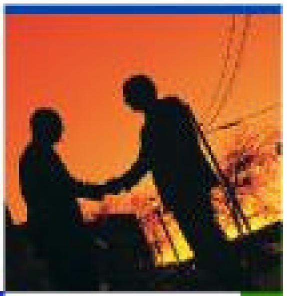
Qualified Small Business Stock

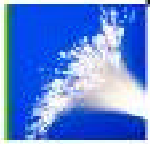


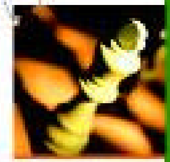


- If a company meets certain requirements, its stock will be considered QSB Stock and will be accorded beneficial tax treatment upon sale
- Before the 2003 tax cut, the effective 14% tax rate on the sale of QSB Stock made it an attractive investment option, especially when compared to the 20% long-term capital gains rate on the sale of stock generally
- By reducing the capital gains rate to 15%, the 2003 tax cut reduced some of the lure of QSB Stock
- However, one of the main benefits of QSB Stock, the ability to perform a tax-free rollover of the proceeds from the sale of QSB Stock to the purchase of other QSB Stock, still remains and makes QSB Stock an attractive investment alternative

Tax Planning for and with Children







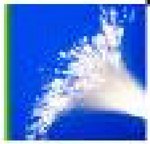
> Consider shifting income-producing assets to children, who will be taxed at a lower rate

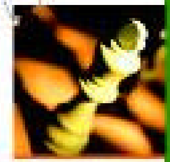
> Careful planning is necessary due to the “kiddie tax”

> The following generally explains how the “kiddie tax” works

- The “kiddie tax” applies to tax on the unearned income received by children under the age of 14
- Unearned income up to $750 is not taxed
- Unearned income between $750 and $1,500 is taxed at 10%
- Unearned income in excess of $1,500 is taxed at the parents’ highest rate

Tax Planning for and with Children





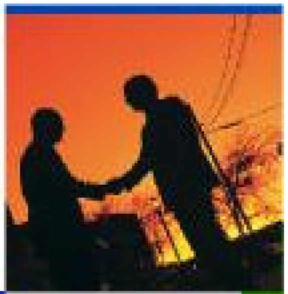
> Hiring children as employees

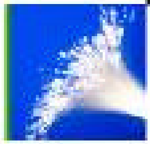
- By hiring children, assets can be passed to them in the form of wages
- Also, a business expense deduction may be available for wages paid

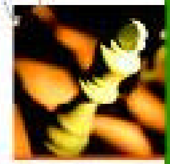
> If your child has wages from a job, consider starting a traditional or Roth IRA

Prepare Yourself for Changes in the Tax Laws

Rates are Scheduled to Change in 2008, 2009, and 2011



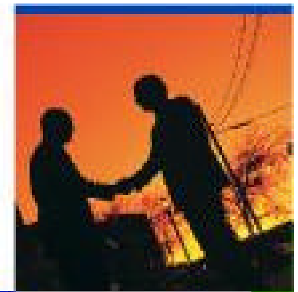


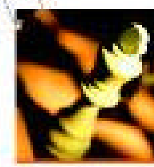


Future Schedule of Changes to Tax Rates

	2003-2007	2008	2009-10	2011
Highest Bracket	35%	35%	35%	39.6%
2nd-Highest Bracket	33%	33%	33%	36%
3rd-Highest Bracket	28%	28%	28%	31%
4th-Highest Bracket	25%	25%	25%	28%
5th-Highest Bracket	15%	15%	15%	15%
Lowest Bracket	10%	10%	10%	N/A
Capital Gains	15%	15%	20%	20%
Capital Gains (10% & 15% Brackets)	5%	0%	10%	10%
Dividends	15%	15%	Ordinary Income Tax Rate	Ordinary Income Tax Rate
Dividends (10% & 15% Brackets)	5%	0%	Ordinary Income Tax Rate	Ordinary Income Tax Rate

Planning for Tax Rate Changes





> Planning with the new capital gains/dividend tax rates

- The lower rates are only effective for 2003 through 2008
  - if you have control over the payment of dividends, it may be a good idea to declare them, as there is no certainty as to how long the lower rate on dividends will last
  - also, because the rate cut on dividends is potentially temporary, care should be taken before selecting or switching the form of a business entity

> Planning with income tax rates

- Deferring income potentially might not be the best option, as rates may rise in the future

Did You Know…

> Massachusetts is now requiring taxpayers who did not file a separate use tax return to report their use tax liability on their Massachusetts income tax returns

- The use tax is a back-up for and complement to the sales tax
- If you purchase, for use in Massachusetts, an item that is or would be subject to the Massachusetts sales tax, but the tax is not collected, you owe use tax on that item—even if you purchased the item in another state, a foreign country, or on the Internet
  - Note: Massachusetts has a relationship with US Customs, and has been assessing use tax on high-ticket-price items that Massachusetts residents bought overseas and declared to Customs

Hale and Dorr LLP