The Renaissance Report

Providing customized financial, estate and investment management solutions.

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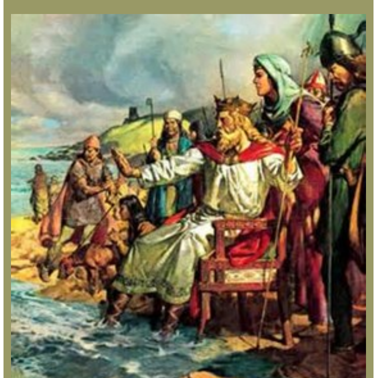

History can be a great teacher. So often the experiences of the past are forgotten or ignored often to the detriment of the present. The investment community appears to have a particularly short memory at times usually accompanied by the mantra "it is different this time". Politicians too are prone to lapses in memory or maybe they just believe they really can make things different this time. The result is inevitable. Stock markets conform to a fairly similar cycle based on economic fundamentals although time frames may differ. When politicians believe they can control these cycles, they are usually doomed to disappointment. In our newsletter for this quarter, we examine two such issues today in relation to Greece and China and we look at the implications for U.S. investors. Tom has written about some of the changes to tax legislation and the implications this may have for lifetime giving programs as part of estate planning. I hope you will find both articles interesting, informative and tinged with a degree of entertainment as you relax, enjoying the welcome summer weather.

Trevor

…or 'folie de grandeur'

submitted by: Trevor Forbes

King Canute, or Cnut the Great, was one of the first Europeans reigning over a region known as the Anglo Scandinavian Empire. Unlike many of today's leaders, King Canute seems to have been aware of his own fallibilities. Since then we have had over a thousand years to ponder his experiences. On ascending the English throne in 1018 he sought to demonstrate to his fawning courtiers that the Monarch was not omnipotent. Sitting by the sea and commanding the waves to retreat, he demonstrated his failings by getting his feet wet.

Sadly, many of today's leaders believe they are not only able to command the waves but push them back over seeming insurmountable rocks. (continued on Page 2)

New Look at Lifetime Giving

submitted by: Tom Malinowski

One of the most popular estate-tax saving strategies I have recommended over the past 30 years has been the implementation of a lifetime giving program to the younger generation, children or grandchildren. This approach was particularly appropriate for assets with the greatest potential for appreciation. The purpose was to reduce the value of an individual's estate as much as possible and thus avoid or reduce estate taxes upon death. Because combined estate tax rates often exceeded 50%, this device proved very valuable.

The drawback to this approach, from a tax perspective, was that the recipient child or grandchild (or trust on their behalf) received the individual donor's tax basis, or cost.

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'…grandeur' (continued from Page 1)

The intractable approach of the Greek government shows this in their response to the inevitable. The leaders of the Eurozone show this in the ill thought out construct of the monetary union that uses the euro as their currency. Each in their own way appears to regard history with disdain.

The Chinese leadership, however, have now moved one stage closer to the sea. The local 'A' shares market has fallen by 40% since it reached its giddy apex in early June. The stunning rise of 300% since last July to its peak was fueled by easy money and a lack of growth in the economy, prompting expectations of 'guaranteed' riskless returns. This was as foolish a notion as the government's response to these excesses. True, margin borrowing has become much more costly and initial public offerings (IPO's) have been banned. At the same time, the ruling policymakers have reduced interest rates on commercial lending in an effort to prop up an economy that seems to be ailing much more than the official data suggest.

This in turn, has caused a significant withdrawal from the stock market by local investors. Investor sentiment seems to have developed the characteristics of a tidal wave, to which the government has reacted by buying large-capitalization stocks in a vain attempt to stem this inexorable pressure of selling. Other tools have been used such as closing trading periodically in up to a half of the companies quoted on the market. The response, so far, is that the selling continues and may be accelerating. In other words, to complete, the historical analogy, China's government is getting its feet wet.

Why is this happening to an economy that is supposed to be as robust as China's? Well, some statistics lie but probably not all of them. Consider the regime's claim that the growth in economic activity is progressing at nearly 6% ahead of this time last year.

The Chinese economy is reported (by the government) to be ***growing*** at its slowest for twenty six years, but does this stand up to scrutiny? Probably not!

The latest trade statistics are very revealing. Imports have fallen by nearly 20% over the last twelve months:

Exports have been more volatile but appear to be falling by 3% over the same period. Among the major developed country trading partners, only the U.S. and the UK are registering gains over this time last year. Elsewhere in Europe and Asia the picture appears very gloomy. Looking at some of China's emerging market trading partners the picture is even worse.

This decline in activity is affecting a wide range of commodities, particularly the base metals and is probably also weighing on the oil price.

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"…some statistics lie but probably not all of them."

… Lifetime Giving (continued from Page 1)

Alternatively, if that child or grandchild received the same asset at the death of the individual, the tax basis would have been the fair market value of the property on the date of death.

In light of changes in our tax structure, this device may no longer be attractive in most circumstances.

Example:

Milton Wright gives during his lifetime $10,000 worth of TWA stock to his son Wilber for which he paid $9,000. At the time of Milton's death, the stock is worth $15,000. Milton would have excluded $5,000 ($15,000 less $10,000) from his estate and potentially saved $2,500 in estate taxes ($5,000 x 50%). Wilber's tax basis in his shares of TWA would be $9,000. If Wilber decides to sell the shares upon Milton's death, he would incur a capital gains tax of $1,200 ($6,000 x 20% (combined federal and estate tax rate)). Thus, Wilber would realize an overall savings of $1,300 ($2,500 less $1,200) with a lifetime gift from his father.

The New World

Under today's new tax structure, the result would be quite different. Most notable is the jump in the estate tax exemption amount to $5,430,000. As a result, estate taxes will be an issue for far fewer individuals going forward. In addition, for individuals with high income, the combined federal and state capital gains tax rate could be 28%.

Example:

Now, assuming similar facts but under today's tax structure, Milton Wright gives during his lifetime $10,000 worth of TWA stock to his son Orville for which he paid $9,000. At the time of Milton's death, the stock is worth $15,000. Assuming Milton's total estate does not exceed $5,430,000, there would not be any estate tax savings. Orville's tax basis in his shares of TWA would be $9,000. If Orville decides to sell the shares upon Milton's death, he would incur a capital gains tax of $1,680 ($6,000 x 28%). Thus, Orville would realize an overall cost of $1,680. If Milton did not gift the shares during his lifetime, Orville would be able to sell the shares and incur no tax at all.

There exist other tax and non-tax reasons for not making lifetime gifts:

Depreciating Assets – If an asset depreciates following a lifetime gift, a greater portion of the donor's applicable exclusion would have been utilized than if the asset was retained until death. This would be relevant in those situations where an estate tax is possible.

Loss of Income – In most instances, assets given away during life may result in a loss of income for the donor. These assets would no longer be available to meet the donor's cash flow needs should a financial uncertainty arise.

Loss of Control - The donor typically relinquishes control over an asset once it is given away. Some degree of control may be retained if certain more complex structures are utilized.

Making lifetime gifts may continue to be appropriate in certain circumstances and should be considered after a thorough investigation. However, in this current tax environment, many instances in which a lifetime giving strategy was advantageous may no longer be appropriate today. Should the tax structure change, lifetime giving may once again be beneficial to all. *§§*

> ***"...in this current tax environment, many instances in which a lifetime giving strategy was advantageous may no longer be appropriate today."***

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