Planning in a Perfect Storm for Business Owners

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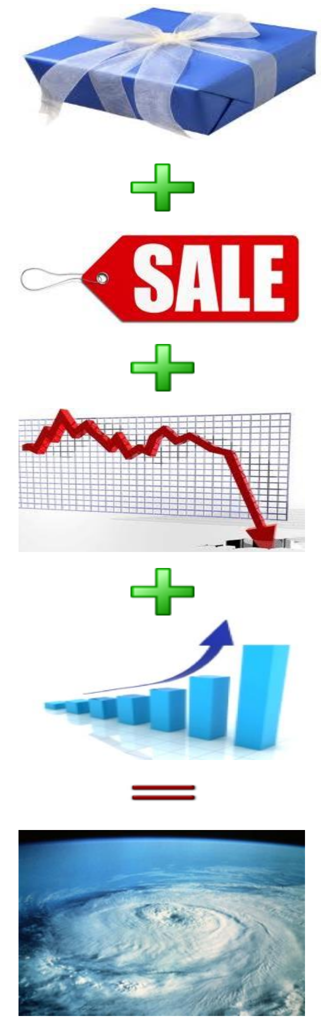
Why is Now the "Perfect Storm" for Planning?

- Doubled Estate Tax Exemption ("Use It or Lose It")
- "Squeeze Planning" with Valuation Discounts (FLP Planning)
- "Freeze" Planning (Gifts and Sales to Grantor Trusts)
- Lock in Interest Rates (Before They Rise More)
- The "Golden Age" Won't Last Forever (Lessons from 2021 Legislative Proposals)



Ideas for Business Owners to Harvest and Leverage $12,920,000 Exemption

1. Outright Gifts to Heirs
2. Gifts to Trusts for Benefit of Heirs
3. Estate Freeze Gifts/ Sales to Defective Grantor Trusts (DGTs)
4. Estate Freeze Gifts/ Sales to Spousal Lifetime Access Trust (SLAT)
5. Estate Freeze Sales to “678 Trust”
6. Gift of Undivided Interest in Real Estate
7. Irrevocable Life Insurance Trust (ILIT)

1. Outright Gifts of Business Interests to Heirs

- Gift $12,920,000 Outright to Descendants
- Drawbacks
  - Assets subject to descendants' creditors and divorces
  - Estate and GST tax exemptions not preserved for future generations ("Generation Skipping"/ Dynasty Planning)
  - Fails to take advantage of leveraging and optimal use of discounts

2. Gifts to Trusts for the Benefit of Heirs

- Traditional, Non-Grantor Trust
- Defective Grantor Trust (DGT)
  - Gift is “supercharged” by grantor’s payment of income tax on trust income
  - Can toggle off grantor trust status later, if desired

3. Estate Freeze Gifts/Sales of Business Interest to DGT

- First explore optimizing valuation discounts (FLP Planning; or non-voting stock)
- Make a “seed gift” to DGT
- Sell assets to DGT in exchange for promissory note (long-term AFR for April is 4.02%)
- Freezes client’s estate at value of the note
- All post-gift/sale appreciation is in the DGT for benefit of beneficiaries

4. Spousal Lifetime Access Trusts (SLATs)

- Husband creates trust for Wife, and Wife creates trust for Husband; trusts must be substantially different and should be created at different times; make gifts/sales of discounted assets to SLATs
- Benefits
  - Uses both spouses' gift tax exemptions ("Use It or Lose It")
  - Assets owned by SLATs not subject to estate or GST taxes for generations
  - Assets owned by SLATs not subject to creditors
  - Spouses continue to have access to assets in SLATs

5. Estate Freeze Sales to "678 Trust"

- Client's parent/sibling/close friend establishes 678 Trust with $5,000 gift; Client <u>sells</u> discounted business interests to 678 Trust in exchange for promissory note (Note will be partially guaranteed)
- Benefits
  - Assets owned by 678 Trust not subject to estate or GST taxes for generations
  - Assets owned by 678 Trust not subject to creditors
  - ***Client continues to have access, control, and flexibility*** over assets in 678 Trust
  - "Cadillac Plan" combines 678 Trust with SLATs (Gifts to SLATs use gift tax exemptions; SLATs sell assets to 678 Trust to freeze SLATs and shift appreciation to 678 Trust)

6. Gift of Undivided Interest in Real Estate

- Example
  - Client owns real estate under business worth $5,000,000
  - Client deeds an undivided 1/16 interest in equal shares to Son and Daughter; the value of each gift is $156,250 minus a 20% discount, which is $125,000
  - When Client dies and the real estate is still worth $5,000,000, Client's 15/16 interest is reduced by a 20% discount ($4,687,500 minus $937,500 equals $3,750,000)
  - That single deed removed $1,250,000 from Client's estate

7. Irrevocable Life Insurance Trust (ILIT)

- Client gifts money to ILIT to use to pay premiums
- Trustee uses money to purchase policy and stay current on premiums
- Upon Client's death, life insurance proceeds are paid to ILIT
- Client saves approximately $400,000 in estate tax for every $1 million of insurance by removing policy from Client's estate

Considerations for Gift-Giving

- Loss of basis step-up when gifting/selling low basis assets (consider “Upstream” gifts/sales to parents)
- Explore ways to qualify for optimal discounts
- Benefits of trusts over outright gifts
- Use Caution with hard-to-value assets
  - Leave a cushion
  - Obtain a qualified appraisal
  - Adequately disclose the gift on gift tax return
  - Use a Wandry formula clause

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