

Special Edition

Successor Planning Part 6

Last week, we discussed the continuing process of transferring the business from one generation to the next, or selling it to a 3rd party. I indicated that it's very important to;

- Select competent advisors.
- Create a Board to assist in the successor transition, and;
- The Board should play an active, not a passive role, in this process.

I further discussed the asset transfer of the business. I stated that there are 3 basic choices in business succession;

1. Keep the business in the family.
2. Create internal management to perpetuate the business or possibly sell the company under an ESOP program, or;
3. Sell the business to an outside interest.

I indicated that as you start the transition, it may seem overwhelming. However, if you have competent advisors that will "walk you through the process" you will be able to get through this emotional transition.

It is very important to get together with your advisors for your estate planning, as well as your accounting firm to make sure that the transfer of your business can be handled minimizing the tax "bite".

This week, I want to discuss the components of capital gains and estate taxes which are part of the process of planning your "exit strategy". The first thing you need to consider when planning your succession is to minimize the tax implications. This is an extremely difficult process.

As I stated previously, selling your business is like planning your own funeral. It's very difficult, emotional and unfortunately, when you get to this stage in your life, a major portion of your life is passing on and none of us like to admit that we're getting old.

With that stated, one of the first things you need to address is what will happen to your business when you die? The IRS will value your company at your death. The full value of your interest in the company will be included in your total taxable estate.

For a successful business, that value could run into the millions of dollars. That's why it's extremely important to have someone that is competent in the transportation industry, value your business as part of your successor planning process.

Normally, estate taxes are due within 9 months of your death. However, if your interest, in a corporate held business exceeds 35% of your total estate; the estate may qualify for a deferral of tax payments. If you own more than one business, your interest in all business, in which you have at least a 20% share, can be added up to reach a 35% level.

MANAGEMENT CONSULTING
OPERATIONAL REVIEWS • MERGERS • ACQUISITIONS • DIVESTITURES

THE AHERN ADVISORY

in this issue

Successor Planning
Part 6



Ahern & Associates, Ltd.

Accredited Member
National Bureau of Certified
Consultants Inc.

July 21, 2009

If you meet these requirements, your estate will owe no taxes until 5 years after your death. Then the estate tax can be paid in 10 equally annual installments, but your heirs will have to pay interest each year.

As we know, capital gains are changing rapidly, so it's extremely important that you have your estate valued on a frequent basis. Estate planners normally suggest putting assets in a trust. There are many types of trust arrangements and each attempt to protect your estate from probate and pass on assets in unique ways. **A trust that is created while you're alive is called a living trust.** Trusts that are either revocable, which can be changed, or irrevocable, which cannot be changed or dissolved.

I don't claim to be an estate tax expert, and obviously anything you do you should discuss with somebody that's very well versed in trust estate issues.

There are well over a dozen types of trusts. Some of the most common types that are likely to come up in your estate planning and successor discussions with advisors and attorneys, I will outline below. **Unlike living or revocable trust, which is not tax shelters,** these trusts have a common strategy; to reduce your estate tax bill.

Bypass or Credit/Shelter Trust

This is an irrevocable trust with your children as beneficiaries that allow up to a specific amount; these amounts keep adjusting each year. In 2006, it was \$1MM for single, and I believe \$2MM for married couples. Although the surviving spouse is not named a beneficiary, he/she can be named as trustee. **Income from the trust goes to the surviving spouse during their lifetime** and the principle can be tapped for emergencies.

Charitable Lead Trust

This trust is a trust funded by you. The trust income is used to make charitable contributions for a specific time. The donations to charity reduce the estate taxes. At the end of its term, the trust assets can pass to your heirs free of estate and gift taxes. **Charitable Lead Trust is a good way to give money to heirs who don't need the income immediately.**

Dynasty trust

This is an irrevocable trust that seeks to provide protection for future generations as it does for you. This trust is geared to families with substantial assets, as these trusts name the children as trustees and grandchildren as successor trustees.

Electing Small Business Trust

This is a relatively new type of trust that allows a more regular trust arrangement to help transfer stock to ownership in a qualifying S corporation without terminating the S corporation election. The down side of ESBT's is that they must pay trust level tax at minimum trust rates and pass through S corporation income.

Generation Skipping Trust

This type of trust is usually an irrevocable trust arrangement that skips a generation of estate tax, leaving your assets to your grand children instead. It can be set up so that the trust income is paid out to your children during their lifetime and the trust principle passes to the grandchildren.

Life Insurance Trust

This is an irrevocable trust that essentially buys and holds the policy on your life; in the process, pushing the proceeds away and out of your taxable estate. The usual strategy is for the trust to apply for the life insurance and then pay premiums with funds you give to the trust.

Q-Tip

A Q-tip is a qualified terminal interest property trust. This is an irrevocable trust. Q-tip trust allows the first spouse that dies to leave assets to children or other beneficiaries while leaving a lifetime income, interest and assets to the surviving spouse. **Assets in a Q-tip are sheltered by the unlimited marital deduction unless they are exempt from estate tax until the surviving spouse dies.** When a spouse dies, the principle of the trust passes to the children or other designated beneficiaries.

Next week, I will discuss how to "shrink the estate".

Quote of the week: **"The biggest problem in the world could have been solved when it was small."**