Aspen Family Business Group, LLC

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Estate Planning Window Closing Rapidly
by Aspen Family Business Group, LLC

We have written in the past about the "The Golden Age" of opportunities that exist for estate planning for family businesses. The $5 million gift exemption ($10 million if you are married) ends after Dec 31, 2012, and reverts to a $1 million exemption on Jan 1, 2013. In addition, valuations for the last 4-5 years have been subdued, and interest rates are at historic lows. Most importantly, discounts often used in family business estate planning are still available for use.

That may be about to change. The unfunded federal deficits we all are aware of will continue for years to come causing Congress and the Administration to review all possible means to raise new tax revenue. Our President's "tax the rich" slogan currently trumpeted has many family businesses square in its sights. Two of these revenue raising maneuvers would put two estate planning techniques at risk. The Administration's "Green Book" contains its revenue raising proposals. The 2010-2012 proposals include the following:

(1)disregarding valuation discounts applicable to certain restrictions or transfers of interest in family-controlled entities and (2) limiting grantor retained trusts to a minimum 10-year term.

In addition, the IRS has maintained that it has the authority to eliminate or limit valuation discounts by regulation. Without going into the detail of the IRS assumption, this means that at any time (even before Jan. 2013) such regulations could be issued effective on the date of the publication, ***without notice or comment***. President Obama has used the "We Can't Wait" doctrine to justify regulatory actions, bypassing the legislative process. Clearly the weight of the executive branch would support such action.

Furthermore, in 2011 the U.S. Supreme Court issued a decision in the Mayo case, a case involving taxation of student income, in which the IRS successfully argued that they had the right to interpret unclear tax law by regulation. Many feel that this case will make it more difficult to challenge the service on such regulatory decisions.

What does that mean for you?

If your advisors have been encouraging you to take advantage of these golden opportunities, they also likely have encouraged you to take advantage of valuation discounts for minority interests transfers. In this way, millions of dollars of value can be transferred to the next generation virtually tax free.

For example, transfers of S-Corp stock in your operating company to children active in the business, LLC interests in real estate to non-active children, and other planning techniques taking advantage of the $5 million gifting exemption would allow an additional $2 million in value to pass to your children tax free. Other techniques, such as a sale to a grantor trust or the aforementioned grantor retained annuity trust, can be leveraged significantly by the use of discounts.

The concern in the planning community is that these valuation discounts could be severely limited at any time by administrative fiat ***without notice*****!** If this happens, it will make the transfer of family businesses more difficult and costly. In addition, many have procrastinated in making the decision to take advantage of the $5 million dollar gift. The interest level is now beginning to rise as the specter of the change on Jan 1, 2013 looms larger. The practical problem is that attorneys and valuation firms are going to be extremely busy in the last 6 months of this year, and the sheer volume of work will preclude some clients from taking advantage of the perfect storm elements.

Let us not forget that as of Jan. 1, 2013, without Congressional action, the estate exemption will drop from $5 million to $1 million, but also the tax rate goes up from 35% to 55%, making it much more difficult in an already challenging environment. Advisors are divided on if and when Congress will take action on the exemption amount and tax rate. Possibly it could return to the 2009 exemption ($3.5million) and rate (45%). The gift exemption could easily return to $1 million.

To take advantage of the "Golden Age" of estate planning opportunities before it is too late, it would be wise to contact your advisors and review your existing estate plan. Have them analyze whether the strategies we have mentioned might facilitate your family business transition objectives in a tax effective manner.

Begin the process of obtaining the necessary valuations so that you know the values you are dealing with. Then create a timetable to implement the chosen strategies before the rush to the door begins in the last half of the year. In future years you will be able to look back and be satisfied that you took advantage of this once in a lifetime estate planning opportunity.