





**Don't Let the IRS Plan Your Estate:
Estate and Succession Planning**



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Succession Planning

✓ Family Business Statistics

- Family owned businesses represent more than **90%** of all business enterprises in the United States
- Approximately **30%** of family owned businesses survive into the second generation, **12%** into the third generation, and **3%** into the fourth generation
- Of the 70% of family owned businesses that fail to transition successfully; 60% fail due to problems with communication and trust and 25% fail due to lack of preparation of the next generation
- Of the senior generation; 80% want the business to stay in the family, 25% have not completed estate planning and 20% are not confident in the next generation

• The University of North Carolina at Asheville (June 2008)




3

Succession Planning

- ✓ Farm production by value of all products sold:
 - Large and very large family farms – 63%
 - Non-family farms – 21%
 - Small farms (less than \$250,000 in sales) – 15%
- ✓ Estimated 70% of U.S. farmland will change hands in the next 20 years
- ✓ Most family operations do not have a next generation skilled in or willing to continue farming


• 2007 Ag Census



4

Key Succession Issues


- ✓ Educating and training the next generation
 - What are the expectations of someone returning to the business?
 - Where does the next generation need to focus?
- ✓ Encouraging a greater sense of psychological ownership in the business ("stepping up")
 - Where is the business headed and what role do you intend to play?
 - What is the impact (opportunity) of your return on the business?
 - Ability to make appropriate/relevant decisions
- ✓ Facilitating the financial transition (gift, sale, etc.)
 - Be clear about what the older generation needs and when they need it
 - What value do you intend to use?
 - Brainstorm on ways to fund financial transition
- ✓ Dealing with compensation
 - Determine philosophy and "Put it on the Table"
 - Determine inclusive amount



5

Key Succession Issues (cont.)


- ✓ Balancing long-term employees' loyalty to the current owners while bringing in a new generation of owners
 - What message do you want to send employees?
 - Be up front and explain expectations to both
 - Be consistent in dealing with frustrations, performance or problems
 - Use the long-term employee as a mentor
- ✓ Fairly dealing with the needs of offspring working in the business with those that did not return to the business
 - 3 circle model
 - Ownership (Equity)
 - Management (Performance)
 - Family (Values and Wealth)



6

Key Succession Issues (cont.)

- ✓ Dealing with children who started working in the business at different times
 - Where do gaps appear?
 - It is normal for compensation to be different!
 - Treat ownership in "operations" and "assets" differently
 - Create opportunities for strengths (not ages) to show
 - *Think about equal opportunities, not necessarily equal outcomes*
- ✓ Managing conflict/tension between those leaving the business and those just getting started in the business
 - Identify it – Get it on the Table
 - Determine what it is based on
 - Is it worth resolving?
 - Work to communicate frequently to build trust
 - Lack of communication = lack of trust = dissolution
 - Focus on goals/vision (outcomes) and expectations



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7

Estate Planning


- ✓ What is Estate Planning?
 - Determining what you want to do with your assets during life and death
 - Provide for self, spouse, children
 - Provide for family members with special needs
 - Benefit charities
 - Minimize taxes to pass on more assets
 - Avoid family disputes
 - Protect assets
 - Transfer business assets and management



8

Summary of 2011-2014 Estate Law


- ✓ Reinstatement of estate and GST taxes
- ✓ Portability of estate tax exemption
 - GST exemption is NOT portable



9

Comparison of Estate Law

	2009	2010	2011-12	2013	2014
Gift Tax Exemption	\$1,000,000	\$1,000,000	\$5,000,000- \$5,120,000	\$5,250,000	\$5,340,000
Max Gift Tax Rate	45%	35%	35%	40%	40%
Estate Tax Exemption	\$3,500,000	\$5,000,000	\$5,000,000- \$5,120,000	\$5,250,000	\$5,340,000
Max Estate Tax Rate	45%	35%	35%	40%	40%
GST Exemption	\$3,500,000	\$5,000,000	\$5,000,000- \$5,120,000	\$5,250,000	\$5,340,000
GST Rate	45%	0%	35%	40%	40%




10

Estate Value Growth Illustration

- ✓ Estate includes 1,000 acres farmland, worth \$8,500/acre on 1/1/2014
- ✓ Estate value = \$8,500,000


Value Growth	10 Years	20 Years	30 Years
5% Annual Appreciation	\$13,845,604	\$22,553,030	\$36,736,510
10% Annual Appreciation	\$22,046,811	\$57,183,750	\$148,319,919



11

Portability


- ✓ The decedent spouse's unused exemption can be transferred, but will not be indexed for inflation
- ✓ Surviving spouse may receive the unused estate tax exemption from the last deceased spouse
 - The total unused exemption cannot exceed the max exemption for surviving spouse's year of death
- ✓ Election to transfer must be timely; no election allowed on a late-filed return
- ✓ Statute of limitations remains open on decedent spouse until the surviving spouse's statute has run



12

Portability Issues

- ✓ Issues to consider when determining to utilize exemption at first spouse's death vs. transferring to the surviving spouse
 - Size of the combined estate
 - Anticipated growth of survivor's estate
 - Changes in future law
 - Asset protection
 - Additional basis step-up of property in surviving spouse's estate
 - Malpractice risk for advisors



13

Husband and Wife Revocable Trusts


Trust A
Survivor's Trust
Remains Revocable

Survivor Gets

- All Income
- All Principal
- Right to amend
- Unlimited Power to appoint to anyone

Tax on Assets over \$5,340,000

First Spouse Dies



Second Spouse Dies

Trust B
Family Trust
Remains Irrevocable

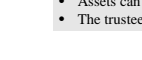
Survivor Can Have

- All Income
- Principal for health, support and maintenance
- Some discretionary distributions with independent trustee

No Tax

Children's Trust

- Assets can be held in this trust while children are growing in maturity
- The trustee manages estate and distributes it to children at specified ages



14

Wealth Transfer Planning


- ✓ 2014 gifts/GST transfers
- ✓ Trusts
 - Spousal Access
 - ILIT
 - Dynasty
 - IDIT
 - GRAT



15

Sale of Appreciating Assets to an IDIT


- ✓ By moving assets out of your estate today (on a discount), there is an extreme amount of leverage in this type of plan
- ✓ The grantor/operator is still in control during their life
- ✓ Discounting can still be accomplished, but has been targeted by Congress and the current administration for termination
- ✓ Cash flow to the trust grantor in the form of note payments from the trust during grantor and spouse's lives; a defined retirement plan
- ✓ Any assets held in the trust at death are not part of grantor's estate
- ✓ If the grantor dies before the note is repaid, only the unpaid balance is included in the estate. The sale "freezes" the value of the grantor's estate by causing future appreciation to escape estate tax on the sold property. The grantor owns a non-appreciating note instead of an appreciating asset.
- ✓ An additional planning opportunity would be the use of a self cancelling note "SCIN", due to historically low interest rates



16

Continued Sale to an IDIT


- ✓ The note payments are very flexible including interest only payments, balloon payments, and accelerated payments
- ✓ The trust is ignored for income tax purposes (so all income is still taxable to the grantor and there is no gain on the sale to the trust), hence the term "defective", but all assets of the trust are outside of the grantor's estate
- ✓ Additional estate depletion opportunity by having the grantor pay the trust's income taxes with no gift tax consequences
- ✓ The provisions of the trust can be customized to meet family needs



17

Continued Sale to an IDIT

- ✓ Trust can be set-up to benefit multiple generations
- ✓ Creates a legacy for heirs or others to benefit from
- ✓ No generation need pay estate tax while assets remain in trust
- ✓ Assets of the trust are protected from creditors of you and your beneficiaries including divorce
- ✓ Assets held in trust avoid the expense and time consuming process of probate
- ✓ Minimal trust administration during grantor's life
- ✓ Peace of mind; knowing your estate plan will accomplish your goals no matter what Congress does in the future



18

Questions

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20