PROTECTING YOUR BUSINESS AND FAMILY WEALTH

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Avoid Procrastination. Unfortunately, procrastinate is what many successful business owners do instead of effectively planning for the future. Now that they have accumulated sizeable wealth, they become immobilized by seemingly conflicting concerns: how to retain control of their assets as they approach retirement age, retain enough income to live on after retirement, minimize estate taxes, and help provide for their families' security after they die. Mixed into the equation may be a desire to eventually pass on the business to the next generation.

These goals need not be at odds with each other, however, because there are ways to maintain control of the family business or other assets and generate an income stream, while keeping a lid on your estate tax bill. You may want to consider some of the following basic strategies as you map out your future.

Business Gifts. Small business owners can shift ownership to other family members and reduce the size of their taxable estate by transferring to them gifts of stock in the business. The savings on estate taxes can be substantial. When making gifts of shares also consider agreements which prevent shares from being transferred outside the family.

Gifts of stock directly to your children fall within the current $13,000 ($26,000 per couple) annual exclusion rule. You and your spouse can transfer $26,000 of assets each year to each child. For example, a total of $26,000 can be transferred to two children, for a total of $52,000, without paying federal gift taxes or eating into the lifetime exemption. Further, as a closely held business, you may be able to take certain valuation discounts and save on transfer taxes, when making gifts of minority interests into your company. The discount is a recognition that a minority interest may be worth less because of the lack of control and marketability inherent in minority ownership.

So, for instance, you might give away a small stake in your family business to your daughters each year and discount those shares by 30%. That means you could give them a stake with a face value of over $19,000 per year, discount it 30%, and still remain under the $13,000 annual exclusion limit. Remember too, making this gift of stock removes the value of the gift and all of its future appreciation from your estate. Thus, a $13,000 share in the business you give away today might grow to a substantial increase that escapes future estate taxes at your death.

Family Limited Partnership. Estate leveraging, discounting and reduction strategies can also be accomplished with Family Limited Partnerships (FLPs). An FLP is a limited partnership that consists of family members, usually parents and their children or trusts for their benefit. Typically, the parents contribute business and investment assets to the trust. The younger generation is gifted limited partnership interests. The general partners are liable for the partnership's obligations, while limited partners only have their capital contribution at risk and do not participate in the control or management of the partnership.

FLPs allow senior family members to transfer more than a minority interest through gifts of limited partnership interests. For instance, when creating a FLP, you might give away 98% of the business to seven family members, while a general partner holds a 2% interest. The general partner remains involved in the business, while the transfer of the limited partnership interests gets a large portion of your business' value out of your estate that will potentially reduce federal estate taxes. By transferring limited partnership interests in the business to your children over time, you may utilize your annual gift tax exclusion. Gifts of interests in FLPs are also popular because they can utilize discounts for lack of marketability and control. The partnership can be structured so that you can shift income among family members.

Grantor Related Annuity Trust. Another kind of estate planning tool, known as the Grantor Retained Annuity Trust or GRAT, lets you remove assets from your estate without giving up the income they generate. GRATs can be effectively used for the transfer of closely-held business interests. Using this trust, you can potentially remove an asset from your estate with reduced gift tax consequences, as well as enjoy annuity income from the asset transferred to the trust for a predetermined period of time. Family-member GRAT beneficiaries ultimately receive the gifted assets, whether stock, investments, or real estate, at the end of the trust term.

Since they are annuities, GRATs pay you a fixed dollar amount each year. For instance, the trust could pay you $4,000 annually. Be cautious, however, if you take more income from the trust than you can use during your lifetime, you will wind up putting that unspent money back into your taxable estate and possibly paying estate taxes on it. Your gift tax is based on the present value of the remainder interest going to your heirs. Therefore, you will be transferring the assets at a discounted rate. That means a lower gift tax bill for you. Since GRATs are irrevocable, you can't take the assets back later if you decide you need them. So be sure you can afford to lose control of those assets before placing them in the trust.

Used correctly, these various techniques may help you meet your goals of reducing the size of your taxable estate, retaining income, keeping control of your assets, and passing on your business to your heirs when you retire. Contact an estate planning professional to get a better idea of how you can protect your family's assets as they continue to grow.