

Sensible Estate Planning for Business Owners

The uncertainty over the future estate-tax law has put many business owners—not to mention their advisers—in a tizzy. Yet one of the worst things to do is to completely ignore the situation. This is especially true if a business owner is contemplating retirement or a sale of the business, or both, in the upcoming years.

Conversely, a comprehensive plan emphasizing flexibility can minimize potential estate-tax liability, regardless of any changes in the estate-tax law that may be enacted. Moreover, an estate plan may avoid a “distress sale” of a business interest while preserving assets for the owner’s heirs.

The initial step is to identify the objectives of the estate plan. Determine the benefits to be derived, the risk assumptions and the amount needed to sustain a comfortable retirement. Once these goals have been established, professional advisers can help formulate the best way to achieve them.

Next, provide the advisers with an inventory of assets. This can be accomplished simply by listing all the assets owned in addition to the business interest (e.g., real estate, stocks, bonds, bank accounts, life insurance, etc.). The advisers can make a reasonable projection of the future net worth of these assets.

The plan may also utilize a buy–sell agreement providing a blueprint for the future sale. Such an agreement may facilitate a transfer of power to the younger generation or a sale to outsiders.

Seeking to minimize potential estate taxes is more problematic in the current environment. At the crux of the matter is the scheduled repeal of the federal estate tax for 2010. This is to be followed by a restoration of the tax in 2011 with a less favorable exemption and revision of the “carryover basis” rules for inheritances. However, even during this period of uncertainty, business owners may benefit from the use of the unlimited marital deduction and astute trust arrangements for family members.

Furthermore, the size of a business owner’s estate may continue to be reduced through lifetime gifts. For 2010, the annual gift-tax exclusion covers gifts of up to \$13,000 per recipient, before any portion of the \$1 million lifetime gift-tax exemption is used. Also, special estate-tax breaks for business interests may be available. For instance, the federal estate tax due on a large business interest may be spread out over a 14-year period if certain conditions are met.

Finally, consider life insurance as part of the plan. In particular, business owners may rely on life insurance for its liquidity. If the policy is structured carefully, the proceeds can be received free of both estate and income taxes.

Of course, this general overview does not take any extenuating circumstances into account. Consult with knowledgeable advisers to arrange a plan designed to fit the specific needs of the situation.