 

Own A Family Business? It's Time To Update Your Estate Plan.

By David M. Frees, III, JD and Douglas L. Kaune, JD |

Would You Like To Able To Keep Your Family Business While You're Alive, Pass It To Your Family Members Under Your Will, And Save Tens To Hundreds Of Thousands Of Dollars In Pennsylvania Inheritance Tax?

If so, then this article will give you the secrets and many of the details of the new law, and how to take advantage of them for you and for your family.

PA ELIMINATES INHERITANCE TAX ON MANY FAMILY BUSINESSES:

If you haven't heard about this new law, you're not alone. Of the few people that know about this important law change, most have not created systems to allow you to understand the new law and to use it in your favor. We have developed these systems and we will share them with you in this article. We also have a full video report on the law and how to use it at http://goo.gl/EHunAm.

The benefits of this law are not automatic. You need to understand this law and then you need to decide if the amazing new benefits are important to you. If they are, then you need to have a process for determining exactly what (if anything) needs to be done to your business structure to make it qualify for inheritance tax free treatment. You will also likely need to revise your will. More on the specifics of that later in this article.

WHAT ARE QFOBS?

First, we will define what we mean (and the state means) by a Qualified Family-Owned Business (QFOB) and who can inherit such businesses without paying inheritance tax - a Qualified Transferee (QT). This law now allows you, as the owner of a QFOB, to transfer that business upon your death to certain qualified family members without any inheritance tax. However, your business transfer will only qualify for inheritance tax exempt status if certain very important conditions are met both before AND after you pass away.

There are some tricky limitations. For example, this new law allows the transfer by will, but not by trusts, of QFOBs only to Qualified Transferees (QTs) and only in certain circumstances. Additionally, after your family member inherits the business they have to follow certain rules or the tax bill comes back to bite them….with interest.

HOW MUCH CAN YOU SAVE?

Current inheritance tax for transfers on death to family members ranges from 4.5% for transfers to children or grandchildren to 12% for transfers to siblings and in some cases even 15% for transfers to nieces and nephews. As an example, if you have a business worth 3 million dollars and you're leaving it to one or more of your children, under the new law you could save $135,000.00 dollars with proper planning. That is a huge tax savings.

Leaving it to a brother or sister? If you do this right, you'll save $360,000.00.
To a niece or nephew? You'd save $450,000.00.

But, there's more to the story. The savings can be even bigger for more valuable businesses. You see, there's a strategy which, when used correctly, can allow a savvy taxpayer to shelter many millions of dollars from tax, much more than you might think when reading the new law on it's face.

WHAT ARE THE REQUIREMENTS?

1) The business has to have fewer than 50 full-time employees; 2) It has to have a net book value of less than 5 million dollars. That the new law values a business by book value rather than fair market value is very important and we'll come back to this later; 3) It has to have been in existence for five years or more prior to the decedent's death; 4) It must be wholly owned by a decedent or by the decedent and members of the decedent's family that are qualified transferees; 5) It has to be engaged in a trade or business, the purpose of which is not the management of investments or income producing assets. This means that many family limited partnerships (FLP) set up for federal state tax purposes might not qualify as a QFOB; 6) It has to be a direct transfer and not IN TRUST to a QT. Again, this may be a disadvantage so more on this later, and finally; 7) Inheritance tax and interest that would be due on the QFOB become liens in favor of the Commonwealth on real and personal property of the qualified transferee (QT) at the time of the transaction.

WHO IS THE QUALIFIED TRANSFEREE?

In other words, who can receive a QFOB without paying Pennsylvania inheritance tax? 1) These interests could be transferred under a will without tax to a husband and wife; 2) To lineal decedents such as children, grandchildren and great grandchildren; 3) To siblings and siblings' lineal decedents - so brothers and sisters and nieces and nephews; and 4) To ancestors and the ancestors' siblings. So it could be given to a parent or grandparent or to an aunt and uncle.

SOME ADDITIONAL FEATURES

The new statute had several other important requirements:

1) The interest must be continuously owned by a Qualified Transferee (QT) for seven years after the decedent's death. That means if the QT actually transfers or sells the business interest, they are going to owe not only the original inheritance tax, but the interest that would be paid on it. It is very, very important to understand this.;

2) The interest also must be reported on a timely filed Pennsylvania inheritance tax return so you have to make sure that your executor is savvy and will hire counsel to properly file that return;

3) There's another requirement, that a certificate must be filed annually by each Qualified Transferee for the seven-year period and failure to do this will result in loss of the exemption;

4) Furthermore, if the QFOB is transferred to a trust, the transfer will not qualify even if the trust beneficiary would otherwise be a QT.

SO YOU HAVE A CHOICE – PAY TAXES OR PROTECT THE ASSET

In many cases, it will be important to consider whether it's better to save the inheritance tax or if it's better for the family member to have the creditor, divorce and lawsuit protection that can be created only by transferring the business to a trust.

Clients must realize there are some ongoing negative implications associated with garnering this tax savings, but in most cases these implications should be easily outweighed by the benefits of a massive tax savings. (We've created a system to help you to maximize the savings and to revise the estate planning to qualify for the new treatment).

Through this system, we help you to figure out if this planning will work for you; help to insure your business will be treated as a QFOB, and we will create special wills that allow you to give the asset to the Qualified Transferee in a way that allows them to decide whether to avoid paying the tax or to transfer it into an asset-protection trust if they are facing a divorce, lawsuit or they are concerned about those issues arising in the future.

FIND OUT IF IT'S RIGHT FOR YOU

We call this process the QFOB (Qualified Family Owner Business) Protection Process™. We will publish more about this process in the next newsletter. But, if you have a family owned business and you want to know more right now, you can see our full video report at http://goo.gl/EHunAm. If you already know you're interested, call Lisa at 1-888-808-5464 and ask for one of our Tax Free Family Business Audit calls. This is a quick call with David Frees or Douglas Kaune to determine if the business planning geared to take advantage of the new law is right for you and if your business will qualify for these massive Pennsylvania inheritance tax savings.

Part Two: Will This New Law Impact Your Estate Planning?

By David M. Frees, III, JD and Douglas L. Kaune, JD |

In part one of this article we announced a new Pennsylvania law that allows certain family businesses to pass by will (and not by trust) and without paying Pennsylvania Inheritance Tax.

We reviewed the new law, what it required, and how it might be used. However, there are some important strategies that can make this law much more valuable to family business owners and can result in death tax savings of hundreds of thousands of dollars…or even more by using this exemption from tax. We have created a system to adapt and update your wills to take advantage of it.

Strategy #1 – In Trust or Not In Trust. Since the law does not allow transfers of business interests IN TRUST, to qualify, most lawyers will tell you that you have to decide right now whether to get the tax saving OR to get the asset and divorce protection of a trust. But by using our system and approach, you can allow your heirs to decide at the time of your death which is more important: 1) the tax savings or 2) the creditor protection of a trust.

But, that planning must be done in advance, so that they can have this choice. And, it allows them to do that after your death when they can best assess the situation. Furthermore, if one of your heirs values asset protection and protection from divorce and another prefers the tax savings, they can each choose a different path.

So, with our QFOB Protection Process™ you can do a will or trust now and leave that decision to each recipient later.

Strategy #2 Create Qualified Businesses So now that we know a couple of these important aspects of the new law, let's look at some of the strategies for really using this and leveraging this to the max. First of all, one of the most important things that leaps out is there is that there are no limits on how many qualified business interests you might have. Thus, if you have a business worth more than 5 million dollars it can be, and in many cases should be divided into separate businesses so you could create multiple 5 million dollar exemptions.

This requires some advanced planning. Therefore, if you have a single family business entity that owns a piece of real estate or a family business that could be divided you should absolutely discuss with us whether or not that should happen.

Strategy #3 Book Value Not FMV Next, and this is vitally important, this law provides that the valuation of the 5 million dollar threshold is done based on book value and not fair market value.

This gives you massive business leverage.

For example, if you own a piece of real estate that's currently worth 8 million dollars but it's been depreciated and your business has a very low book value you might be able to transfer an asset worth 8 million dollars by separating it into two assets or businesses worth 4 million dollars each to qualified transferees with no Pennsylvania inheritance tax even though it is worth much, much more than the 5 million dollars. Furthermore, by dividing family-owned businesses into multiple interests each of which meet these qualifications you might be able to leverage this over and over again to shelter businesses which are each worth less than 5 million dollars.

When you divide businesses into separate entities you might also get some litigation and law suit protection during your lifetime as well. How? Well, if all of your business activities are under one umbrella, then a law suit against that company or entity could get at all of your assets. But if your business activities are under separate entities, each is protected from the liability against the other.

So how do you go about doing this and what are the pros and cons? Well the pros are obvious. You could save 4.5% to 15% percent of the fair market value of the business depending on whether or not it is being transferred to children, or more distant relatives.

The cons are that this doesn't work for trust transfers, there are significant costs to doing it (although the savings should be much much larger than the costs) and there are some restrictions – so this is not for everyone.

SO WHAT'S THE BOTTOM LINE? You need to determine:

1) Do you have a family business that qualifies or could be made to qualify?

2) If you don't have a family business, are you engaged in activities that could be converted into a qualified family business that would qualify?

3) You need to decide if an existing family business or a reconstituted family business should be divided into multiple businesses so you could transfer multiple businesses each of which has a book value of less than 5 million dollars. This would be important if the book value of your business exceeds 5 million dollars.

SO WHO IS THIS FOR? It's for families that:

- own real estate (commercial or residential) and which have high market value but low book value
- own businesses of any type that you're not planning to sell but to pass on to heirs
- <u>want to pass these assets only to other family members</u>
- are tired of being told that they have to give away all of their assets prior to death to save taxes
- want to keep their options open to protect assets from a divorce or law suit OR to trigger these large tax savings.

WHO IS THIS NOT FOR? It's NOT for you if:

- you're planning only on selling the business to people who don't qualify as QTs (non family members)
- you're leaving it to a son in law or daughter in law
- you have overriding reasons to leave the business to your heirs IN TRUST rather than outright since that's not permitted under the new law

SO WHAT'S THE NEXT STEP?

How can you go from complicated to easy? Generally, this is not something you'll do on your own. It can be simple and sometimes only requires a change to your will. But, the law is complicated and you should seek the advice of a lawyer with experience in both business and trust and estate planning so that you maximize the savings and so that it can be customized to YOUR PARTICULAR CIRCUMSTANCES.

In some cases, where your business' book value is below 5 million dollars this can be as simple as doing a new will with our QFOB Protection Plan™.

In other cases, where the saving can be massive, you'll probably also want a business lawyer who will coordinate with your accountant as there are many lifetime income tax issues related to some of the planning techniques here. You may also want us to consult or to coordinate with your insurance adviser since some of this planning can involve changes that might mean small changes to your insurance coverage. So whether you're looking at saving tens of thousands, or hundreds of thousands of inheritance taxes, we have a process that can help you to find out if this is for you.

Please call 1-888-808-5464 if you are ready to schedule a Family Business Estate Planning Consult.

While there is no charge or obligation to proceed after the call, the fees for the process can range from as little as $2,700 dollars up to $10,000. But, you'll never spend that money unless this planning makes sense FOR YOU. For those clients and business owners who ARE planning to leave a business to a child or other family member, this could be a huge return on investment of your time and the costs involved. If you decide to proceed with the planning following our call, you'll be set up with an appointment to finish the planning and an appointment to execute any documents that are required to make your new plan a reality.

Thank you for taking the time to read this article and to learn more about this astonishing new opportunity.

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Offices of UTBF Attorney David M. Frees, III, Douglas L. Kaune, and Whitney O'Reilly
Please call 888-605-6482 and mention you read the "UTBF NEWSLETTER", we are happy to assist you with any questions concerning your estate planning.