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## **FAMILY BUSINESS FORUM**

### **Estate Taxes Are Voluntary**

**By Donald Levitt**

“We consider the federal estate tax to be a voluntary tax,” says Chris Steiner, an attorney with Bayer, Papay and Steiner in Maumee, Ohio.

Now that got my attention – and it should get the attention of any family business owners who want to keep their assets – and their business – in the family.

Steiner and his partner Debbie Papay offer regular workshops on reducing or eliminating federal estate taxes. Here is how they explain estate planning in their workshops.

#### **Basic Planning**

Steiner uses the supermarket check-out line as a metaphor. “Let’s say your husband passes away. The tax commissioner looks at all of your assets on the conveyor belt – your house, savings accounts, stocks, and the value of your family business.”

“In your purse you have a ‘coupon’ the government gave you to help pay the bill. In 2005 this ‘coupon’ – the federal estate tax exemption – is worth \$1.5 million. If your husband’s estate is less than this amount, you pay no estate taxes on your husband’s estate, and the entire value of his estate goes into a ‘family trust.’ You can receive income from the family trust and can access the principal for reasonable living expenses.”

What happens when you die? “Now your children are at the ‘check-out line’ and the tax commissioner is assessing the value of your estate. The assets which are already in the family trust are not considered part of your estate. If your estate is worth less than the value of the ‘coupon’ at that time (the federal estate tax exemption amount currently increases to \$3.5 million by 2009, and is then repealed in 2010 and reverts to \$1 million in 2011), then your estate pays no taxes.”

But what if your husband’s estate or your estate is worth more than the “coupon?” “When you are ‘checking-out’ your husband’s estate, \$1.5 million is covered by the ‘coupon’ and goes into the family trust, and the remainder goes untaxed into a marital trust (to which you have unrestricted access.) When your children are then ‘checking-out’ your estate years later, they use the ‘coupon’ to reduce the estate tax by the current

exemption amount; the money in the family trust is untaxed; and the estate then pays taxes on the marital trust and the remainder of your estate.”

The above steps are pretty straightforward. While it is possible to accomplish these steps using wills, it is ultimately quicker, easier, less expensive, and not open to public scrutiny if trusts are used rather than wills.

### **Advanced Planning**

If you project that your estate will exceed the value of the “coupons”, how can you further reduce estate taxes?

“The simplest approach is to use the \$11,000 annual gift tax exclusion. This does not in any way affect your ‘coupons’. While you and your husband are both still alive, you can each give \$11,000 to each child, each child’s spouse, each grandchild, etc. Assuming you have two married children and four grandchildren, you can give away up to \$176,000 a year. If you start early enough, this gifting, along with the ‘coupons’ should cover most estates.”

“If you need to shelter even more money, you can put these gifts into a family limited partnership. The parents are the general partners and retain full control. The children are limited partners. Because the children have no control over the assets, the gifts are ‘discounted’ – meaning you can give more than the \$11,000 gift tax exclusion – up to about 40% more. And these gifts can be in property – not just in liquid assets.”

And if that shelter is *still* not enough? “You can create an irrevocable life insurance trust (ILIT). You pay the premium on the life insurance and put the policy into an irrevocable trust. When the policy is paid after your death, it is not considered part of your assets, and is not taxed.

### **The Tip**

Federal estate taxes are “voluntary” – but only if you set up the proper estate planning structures – and start this well before you pass on to your own eternal (non-monetary) rewards.

***Donald Levitt, president of Levitt Consulting, helps family businesses to succeed as both a business and a family. More information about this month’s topic, and other family business issues, can be found at [LevittConsulting.com](http://LevittConsulting.com).***