

Case Study – Ferris and Beatrice

Client Background

Ferris and Beatrice Bueller are 60 and 58 respectively. They own and are active in two distinct closely-held businesses that have proven to be recession-proof. They live a comfortable lifestyle, spending about \$600,000 a year after taxes, and their annual income exceeds their spending. Currently, they pay just under \$1M a year in income tax. Ferris and Beatrice have assets worth approximately \$50M and therefore have a substantial estate tax exposure.

Their daughters, Jenny and Megan, are very involved as managers in the day-to-day operation of the business, and one of the primary planning goals includes the successful transfer of these two businesses to the daughters in a tax-efficient manner.

Jenny's husband, Mark, is also involved in the business. Although Ferris and Beatrice are very fond of Mark, and would like for him to remain a key person in the family and the businesses, they do not

want any of the business ownership to pass to him.

The two businesses represent about 75% of the \$50M estate and generate over \$2M per year in taxable income. While many companies have struggled in the recent recession, these businesses have continued to thrive and are expected to grow significantly.

Although the businesses generate significant cash, the Buellers do not have much in the way of liquid assets because they have elected to accelerate the pay-down of business debt. And though they currently own life insurance with an \$8M death benefit, they know that their daughters would have great difficulty covering estate tax liabilities should something happen to Ferris and Beatrice. They don't want the daughters to have to liquidate one or both of the businesses to pay the estate taxes.

Client Goals and Concerns

The primary planning goals are to:

- Ensure that they have sufficient income to live on for the rest of their lives (approx. \$600,000/yr. after taxes and gifts)
- Maximize what they leave to their children and grandchildren
- Increase their current involvement in charitable giving
- Reduce or eliminate their business debt
- Provide a smooth transfer and transition of both businesses to the daughters
- Reduce current income taxes
- Reduce or eliminate estate taxes

The Solutions

As with all our clients, integrated planning solutions vary from client to client. This situation used six different planning strategies, which were designed to meet all the client's goals and mitigate as much risk as possible.

We will look at two of the strategies used in this client's plan.

GDOT

With such significant value and taxable income from the businesses, a sale to a grantor deemed owner trust (GDOT) was the ideal solution. Using a recapitalization of the S corporation stock, we split the stock into voting and non-voting shares. This created some valuation leverage (lowering the value of the non-voting stock) when it was sold to the GDOT.

This sale also enabled us to freeze the value of the stock so that all future appreciation and growth of the business interests would accumulate in an asset-protected and estate tax free vehicle while keeping the estate value constant.

The terms of the GDOT allow Ferris and Beatrice to pay the income tax liability of the trust, which amounts to additional tax-free transfers from the estate. This is sometimes called "tax burn." Because of personal cash flow concerns, this income tax burn will need to be monitored.

GDOT Insurance

Even with the estate freeze and income tax strategies in place, there still remained a liquidity problem, especially in the early years of the plan. To help counter this, we recommended a \$30M survivorship policy inside of the GDOT, using income and distributions from the companies to pay the premiums. This enabled us to pay premiums on the policy while having the policy owned in an asset-protected and tax-efficient trust.

Annual Meetings and Maintenance

Our annual maintenance program helps Ferris and Beatrice to stay on track with monitoring their cash flow and lifestyle needs as well as the choices they made in the planning process.