Background

Tom is 83 and Jane is 76. They have been married for over 50 years. Their son Tim is single with no children. Their daughter Jeanne is married with 3 children. Both children are well employed and live productive and happy lives.

Tom and Jane are both retired. Tom was an attorney who headed a large patent firm in Washington DC. Jane holds a PhD from Georgetown University in economics and served as an expert in international trade for much of her professional life.

During the latter part of his career, Tom agreed to do work for a start up company that went on to be very successful.

Assets

Today, Tom's share of the company is valued today at $3.2M but generates $1.4M-$1.5M per year in taxable distributions.

The valuation by economic measure should be substantially more, but is controlled by a buy sell agreement among the many partners. The agreement has a call provision (which has been exercised on more than one occasion) that limits the fair market value to $3.2M.

Several years ago, the company spun out one of its divisions and took the new company public. It has seen massive growth; almost no dividends distributed, and has a value today to Tom of approximately $6.4M.

Tom and Jane also have approximately $5.2M in cash, $3.2M in retirement funds, and real estate of $4M for a total net worth of about $22M.

Goals

Their goals are to:

Make sure that they have sufficient funds to live on for the rest of their lives (including provision for long term care)

Maximize what they leave to their children and grandchildren

Increase the amount of charitable giving that they are currently doing

Equalize the financial positions of their son and daughter (gifts to the grandchildren have left the son feeling like he has been short changed a little, and Tom and Jane agree.)

Make a substantial provision for charity in place of estate tax if possible.

Overall Plan Summary

GRAT

Often we look at using a sale to a defective trust in cases like this. But the buy sell agreement provisions would have been triggered by such a move, so we turned to use of a GRAT instead. We worked together with client's attorney to create a plan that involved using a 7 year GRAT funded with the high income producing asset and the spin off. Given the high cash flow, the GRAT should return most of the dividends as well as the stock in the high income producing asset (so that Tom and Jane can continue to enjoy the cash flow after the GRAT is over). With good experience, the spun off company should end up out of the taxable estate at very low or no tax cost.

ILIT

Next we looked at doing an ILIT funded with $2M of insurance to provide a pool of liquidity to take care of the vacation home in perpetuity for the kids and grandkids. As it turns out, Jane's mother and grandmother lived to a ripe old age and internal rate of return did not look so good in the event that Jane lived to 100 (or even longer as her mom and grandmother did.) The insurance decision is still pending.

QPRT

A five year QPRT was designed for the vacation property. At the end of five years, the parents will rent the property back for fair market value. The QPRT will be structured as a grantor trust both during and after the term to minimize income tax issues.

IRA Distributions

Extra money will be distributed out of the IRA, not because it is needed to live on but because the clients can meet their goals of additional charitable giving without having to pay taxes on the distributions since their AGI will be sufficiently high to cover the deduction with room to spare. In addition, the beneficiary of the IRA was amended to provide a new secondary beneficiary (charity) in the event of a disclaimer by the children (primary beneficiaries).

TCLAT

Finally, a disclaimer TCLAT was implemented following the Jackie Onassis pattern. I.e., all to children, but if children disclaim, that portion disclaimed goes to a testamentary charitable lead annuity trust. This technique, if employed at the second death will bring the estate tax to $0 and provide the potential for a significant deferred inheritance for grandchildren.