

The Importance of Aligning Objectives Prior to the Wealth Transfer

You may have just realized that you want to transfer a portion of your company's wealth to your children or it may have been something that has always been in the back of your mind. Either way, one of the first questions that parents struggle with answering is, "How much wealth should the children have? How much is too much?" If you are struggling with these questions, it is important for you to revisit your original exit objectives, namely, "How much money do you wish to have after the sale of your business?" Once you have answered this question, you then can work with your advisors to design a transfer mechanism that will pass the wealth to your children with minimal tax impact.

To initiate a successful transfer design process, it is important to address the following questions along the way:

1. How much wealth do you want?
2. How much wealth do you want the kids to have?
3. What tools minimize the estate and gift tax consequences of transferring wealth?

To illustrate how one fictional business owner might answer these questions, let's look at the case of George Delveccio, a composite representation of a number of successful business-owning clients.

George opened his meeting with his Exit Planning Advisor almost apologetically. "I knew I'd waited too long to begin gifting part of the company to my kids when I met with my CPA. She told me that the company could be worth as much as \$12 million to a third party. I had no idea! Since I don't need that much, I want to transfer at least half the value—at a lower valuation of course—before any possible sale. My CPA suggested gifting small amounts of stock using my \$12,000 annual exclusion and perhaps part of my lifetime gift exemption. She believes that additional strategies might allow me to increase the amount of my gift without paying gift taxes so she suggested that I meet with an experienced Exit Planning Advisor."

George's Exit Planning Advisor pointed out that the use of the \$12,000 annual gift exclusion and the early use of the \$1 million lifetime gift exemption were sound ideas, but, used alone, could not facilitate the



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transfer of a significant amount of wealth to his children. Even combining George's and his wife's annual exclusion amounts with their full lifetime gift exemptions, the transfer to the kids would be a little more than \$2 million.

The deficiency of this plan was further accentuated when George was asked what he thought the future held for his business. In his words, "The sky's the limit." This was telling given George's occupation—he owned an air freight expeditor business. He strongly believed that the company's cash flow would continue to grow, from its current \$2.5 million, by at least 25 percent per year for the next three years.

"And that's what worries me. Given how much more valuable my business will be in a few years, won't it be even more difficult to transfer wealth to the kids? What I need to know is how I can give my kids as much as possible without paying any taxes."

Believe it or not, this was exactly what George's advisor was hoping to hear. The advisor explained, "The more rapidly your business is growing in value...the more cash it spins off...the easier it is to give wealth away and give it away quickly—with little or no gift tax consequences."

But George, like many owners, was paying too much attention to the wrong issue. The advisor suggested that George focus on the three basic issues that must be resolved for successful wealth preservation planning to occur. These issues include:

1. Fixing your financial objectives before considering a wealth transfer.
2. Determining the amount of wealth to be transferred and identifying how much is too much.
3. Designing a wealth transfer strategy that keeps the IRS from becoming the largest beneficiary of your hard-earned cash.

By focusing on the issues described above, you are well on your way to designing a family wealth transfer strategy that helps meet your exit objectives and minimizes tax consequences.

If you have any questions about transferring wealth to children, please contact us to discuss your particular situation.

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