STEWARDSHIP MINISTRY | TAYLOR UNIVERSITY
236 W Reade Ave, Upland, IN 46989 | taylor.edu
stewardship@taylor.edu

DEFERRED INHERITANCE WITH INSTANT GRATIFICATION

The Scenario:

Bob and Marge Miller are both 67 years old. Bob is the sole owner of a small manufacturing business that has recently been valued at $5 million. He has three adult children that are all active in the business. Bob plans to stay involved in the business as long as he is mentally and physically able. He does, however, want to pass the business on to his children at his death; and the children would like to continue the family business after their dad is gone. Bob and Marge's total net worth is just over $10 million.

The Millers are committed followers of Jesus and are very involved in their local church and a Christian college affiliated with their denomination. They are currently major financial supporters of both. They have come to fully understand their stewardship responsibilities of the wealth that God has so graciously entrusted to them, so being wise stewards of all their wealth is very important to them.

The Challenge:

If Bob tries to pass the business to the children at his death, $4 million of the gift will be subject to Estate Taxes. This transfer will trigger a $1.8 million tax or over one-third of the value of the company. The rest of their net worth, less Marge's $1 million lifetime exclusion, exposes their remaining $5 million of assets to an additional $2.2 million in Estate Taxes, equaling a total of $4 million in Estate Taxes on the $10 million net worth.

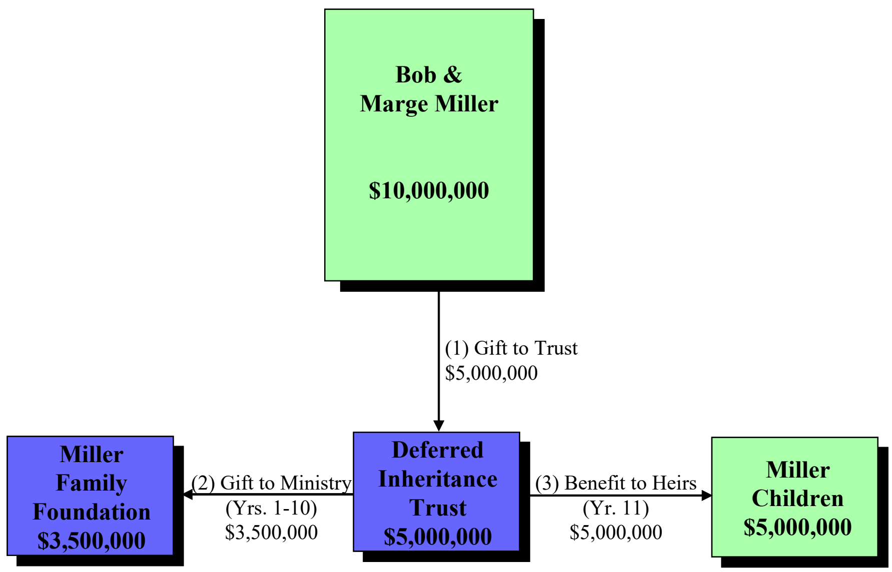
As part of developing an overall Master Stewardship Plan one major challenge was how to transfer the family business to their three children at Bob's death without incurring $1.8 million in unnecessary taxes. Adding to this challenge is the fact that the company is an S-Corporation which, in traditional planning, more difficult to transfer or dispose of in a tax efficient manner.

The Solution (see Figure 1, below):

In order to transfer the business, a testamentary buy-sell agreement was created between Bob's estate and the three children, one-third of the company to each child. By utilizing some creative compression planning, their business can be sold to the three children at a fair market value of only $3.5 million. Because the children did not personally have the cash to buy the business, Bob's estate will sell the stock and take back a ten-year, interest-only, promissory note of $1,167,000 from each child. The note would have a balloon payment at the end of ten years. Because the stock takes a step up in its basis when Bob dies, there will be no Capital Gain Tax owed on the sale of the business to his children. With Bob no longer taking his salary from the business, the children have the additional cash flow from the business to make the interest-only payments on the loans for the next ten years. Consequently, when Bob finally "relocates," his children immediately become the stockholders of the family business.

Next, Bob's Master Stewardship Plan creates a testamentary Deferred Inheritance Trust (DIT) [IRS named a Charitable Lead Annuity Trust]. The three promissory notes from the children are transferred into the trust. The DIT will be a ten year trust paying $350,000 (10%) annually to Bob and Marge's newly created family foundation—an amount equal to the interest payments on the three promissory notes. Over the next ten years, the DIT will contribute $3.5 million to their foundation to support the Christian causes and ministries that they and their children most care about. At the end of the ten years, the DIT will terminate and the three notes will be distributed to Bob and Marge's three children. [The amount of the taxable gift to the children will be just under Bob's $1 million lifetime gift limit (Applicable Exclusion Amount). Thus, there will be no tax owed when the DIT is created and funded.] Now, each of the three children will be holding their own promissory notes to themselves. Through the law known as the Doctrine of Mergers, when the same person is both the lender and the borrower on the same loan, the loan simply ceases to exist. As a result, the final balloon payment need never be paid.

Figure 1



The Result:

The following is a summary of Bob and Marge's original business transfer plan and their new Master Stewardship Plan for transferring their business to the children. The numbers speak for themselves.

Amount to the:	Original Plan	Master Stewardship Plan
IRS	$ 1,800,000	$ -
Children	$ 3,200,000	$ 3,500,000
Kingdom	$ -	$ 3,500,000

For people who have a heart to be good stewards of all the resources that God has entrusted to them, implementing this kind of strategic and creative planning is a given.

Jesus tells us that we are to be as *shrewd as serpents and as innocent as doves*. I interpret this to mean that we are to be both shrewd and honest in how we live; these two behaviors are not mutually exclusive. Shrewdness is not opposed to honesty, and honesty is not opposed to shrewdness. The best stewardship planning utilizes the epitome of shrewdness while honoring both the spirit and the letter of the laws of our land. There will be a time of great satisfaction when we finally stand before our Father as he reviews what we did with what we had, and He says to us, *Well, done…*

ABOUT THE AUTHOR — E. G. "JAY" LINK

Jay Link, Director of Stewardship Planning at Taylor University, spent 35 years counseling Christian families to build customized Master Stewardship Plans. He is an author, a mentor to hundreds of financial advisors and attorneys, and started his career as a pastor. His passion is helping Christian families use all the Lord has entrusted to them for Kingdom-building purposes.