Gift & Estate Planning

Giving Closely Held Stock

Stewarding the Giver **and** The Gift℠ >>

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GIVING CLOSELY HELD STOCK

Whether you are considering selling your business or working on a future succession plan, charitable giving strategies may help you reduce your tax liabilities and increase your charitable giving opportunities – while still providing for your financial needs and preserving your control over business operations. How can this be?

A charitable gift of non-controlling interests in your company ***before*** a sale or transfer can significantly reduce the tax impact when you do eventually sell or transfer the company. Not only do you receive a charitable deduction for the non-controlling interest you give to charity, the portion gifted to charity generally avoids taxation when the company is later sold or transferred. For this reason, a gift of closely-held stock can be a wise and effective way to steward the financial blessings entrusted to you by God through the success of your business.

How could a gift of closely held stock help you accomplish your charitable giving and business transition goals? Consider the stories of these two Kingdom stewards. . .

Sale of the Family Business

In the early 1980's, Mike and Jenny started a printing company out of their home. Over the years, they have been blessed with profitable connections and contracts, and the company has prospered and expanded. Recently, Mike and Jenny decided that they want to retire from the business. Because their children are grown and not interested in taking over, Mike and Jenny are now investigating how best to sell their company. They believe the company should sell for approximately $4,000,000. Unfortunately, their accountant tells them to expect to pay $1,000,000 in State and Federal capital gains taxes and depreciation recapture. They have the following primary objectives for any future sale transaction:

- To keep control of the company until it is sold;
- To keep approximately 60% of the gross sale proceeds ($2,400,000) for investment to produce a supplemental annual income between $120,000 to $140,000;
- To reduce their tax bill; and
- To maximize the remaining sale proceeds for Kingdom ministries to use to glorify the Lord who has so graciously blessed their business over the years.

In their original thinking (Scenario A), Mike and Jenny planned to sell their stock, keep approximately 60% (or $2,400,000) of the sale proceeds, pay their taxes and give the rest to charity. However, they were amazed at the comparative results of altering their gifting plan to instead give 40% of the stock to charity ***before*** the sale and to keep 60% of the stock for themselves (Scenario B). Here is what they discovered:

Scenario	"Gift" to Government (Taxes*)	Gift to Charity	Income Tax Deduction	Value of deduction to taxpayers*	Combined benefit for family
A. Sell stock then gift after-tax cash	**$1,000,000**	**$600,000**	**$600,000**	**$240,000**	**$ 2,400,000 - 60% sale price +$ 240,000– deduction value $ 2,640,000 – combined benefit**
B. Gift 40% of stock then sell	**$600,000**	**$1,600,000**	**$1,600,000**	**$640,000**	**$ 1,800,000 - net proceeds +$ 640,000– deduction value $ 2,440,000 – combined benefit**

** Assumptions: Taxpayers subject to combined rate of 25% for State and Federal capital gains tax and depreciation recapture; and a combined rate of 40% for State and Federal personal income tax*

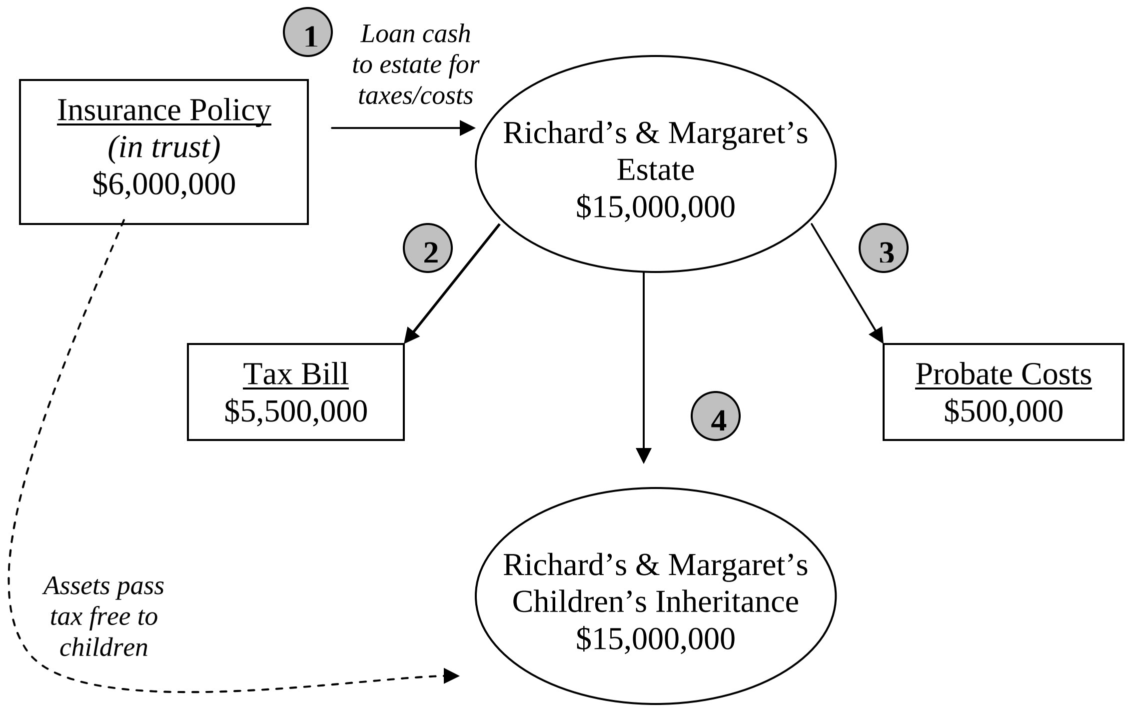
By giving their stock to charity before the sale, Mike and Jenny were able to decrease their taxes by $400,000, increase their Kingdom giving by an additional $1,000,000 and still maintain the desired $2,400,000 of combined benefit for their investment purposes!

Transition of the Family Business

Richard and Margaret have invested a majority of their lifetimes into building a successful manufacturing company. They are blessed to have three adult children who work in the company and are capable of taking over once Richard and Margaret pass away. Richard and Margaret's top objective is to leave the company to their children upon their death. In addition to that main goal, they would like to minimize their taxes and leave a generous charitable legacy as part of their estate plan.

Unfortunately, their accountant tells them that with their business (worth approximately $12,000,000) and their other asset holdings, they can expect a combined Federal and State estate tax bill of $5,500,000. For that reason, their accountant and financial professional advised them to obtain a life insurance policy with a death benefit of $6,000,000 to cover the expected estate tax burden and probate costs when the survivor of them passes away.

In general, their estate plan currently looks like this:



However, Richard and Margaret were intrigued when they heard they could restructure their estate plan to reduce (and even eliminate) their estate tax burden. Rather than letting the government use their God-given resources through the taxes they anticipated paying, Richard and Margaret were excited to learn they could instead direct those resources into the hands of ministries they trust to carry out charitable work they support.

The strategy for eliminating their estate taxes and increasing their Kingdom giving involved taking the following steps:

- First, they recapitalized the company into 6 voting shares and 94 non-voting shares;

- Upon their death, they directed in their estate plan that the children are to receive:

  - The 6 voting shares, plus

  - As many of the non-voting shares as they could receive estate tax free (which in their situation resulted in approximately 40% of the non-voting shares after discounting the shares' pro rata value of the underlying company's worth by 30% due to their non-controlling and non-marketable nature)

- The remaining non-voting shares (approximately 60%) are to be distributed to Richard and Margaret's designated charity.

- Because the charity has no interest in being a shareholder in the family business, the charity would reasonably be interested in offering its non-voting shares back to the children for a bona fide redemption transaction. The children could then use the proceeds from the life insurance policy (intended previously to pay taxes) to redeem the non-voting shares back from the charity.

- The end result of this arrangement is that the children receive the business; estate taxes are completely eliminated and the charities Richard and Margaret wish to support receive a generous legacy to continue their charitable work.

Is it advisable to already have a buyer arranged before giving my closely-held stock to charity?

Entering into negotiations with a potential buyer prior to making your gift to charity can result in negative tax outcomes. If you have already negotiated a sales arrangement with a potential buyer prior to giving the stock to charity and the charity then sells the stock to this buyer, there is a risk that the sale transaction will be treated as a prearranged sale by the IRS. Should that happen, you would be taxed on the entire gain resulting from the sale based upon the IRS's declaration that the charity was a mere conduit for carrying out your prearranged sale. For your protection, the charity should enter into independent negotiations with the buyer subsequent to your gift to the charity. The degree of risk for the IRS declaring the stock sale to be a prearranged sale varies from situation to situation. For this reason, your attorney needs to advise you how best to protect your tax position if any discussions have occurred with a potential buyer prior to making a gift of your stock to charity.

Will I need to get an appraisal?

Yes. For any gift of non-publicly traded stock exceeding $5000 in value, you will need to get a qualified appraisal to substantiate your charitable deduction. A "qualified appraisal" is defined in the United States Treasury Regulations. Full details regarding the qualified appraisal requirements should be discussed with your tax professional.

However, in general, a qualified appraisal must:

- Be prepared by a qualified appraiser;
- Describe the appraiser's background, education and experience;
- Disclose the fee arrangement for the appraisal services;
- State the gift date;
- Provide the fair market value of the stock on the gift date; and
- Be obtained no earlier than 60 days before the date of the gift and no later than the day before the due date of the income tax return on which you are reporting the gift.

In addition to obtaining a qualified appraisal, you will need to file an "appraisal summary" on IRS Form 8283 with your federal income tax return in order to claim your charitable deduction.

Can you help me better understand how a gift of my closely held stock could help me accomplish my charitable giving and tax planning objectives?

To receive a personalized analysis of how a gift of your closely held stock may help you wisely accomplish your giving objectives, please contact us at (800) 782-8227. We welcome the opportunity to talk with you, and we will gladly send you a personal proposal for you to discuss with your professional tax advisor and legal advisor.