

TRYING CASES

Eight moves top attorneys are urging their clients to consider.

BY DALE BUSS



TODAY'S ECONOMIC TUMULT is upsetting the sturdiest of investment strategies and testing the best-planned legacies. So your lawyer is more critical than ever when it comes to advising and executing your family financial decisions.

"Just as time will show there are some investment opportunities at the moment, there are some planning opportunities at the moment," says William Lowell, partner in Choate Hall & Stewart in Boston. "The challenge is getting clients to focus on them."

Here are some of the moves that Lowell and his peers are suggesting:

GROW GRATS: If your primary goal remains transferring as much wealth as possible to your heirs at minimal levels of taxation, this period is tailor-made for your strategy. With greatly deflated current values for all kinds of giftable assets, you can pass more on to your children, who could benefit handsomely if the assets recover.

"Individuals who have stamina and can think about this clearly—but also have gumption—are seeing unprecedented opportunities to gift value to the next generation with little or no transfer costs," says Anita Rosenbloom, partner in Stroock & Stroock & Lavan in New York.

She and other attorneys strongly advise creating a Grantor Retained Annuity Trust. A GRAT allows you to transfer assets to a trust while retaining the right to receive a fixed annuity for a specified term, often two years.

"GRATs are perfect because you know you can get your principal back," Lowell explains. "If you're a bit on the fence about making a large transfer right now, this is a nice way to do it without making yourself so nervous that you don't do anything."

At the end of the term, remaining trust assets pass to the ultimate beneficiaries of the GRAT—usually your children or a trust for them—free of any estate or gift tax. The

assets you select are likely to appreciate during the GRAT term more than the monthly IRS "hurdle rate" (which, in October, was at a low 3.8 percent). Typically, the GRAT is "zeroed-out," meaning it's structured to produce no taxable gift.

DIG INTO IDGTS: Another ideal instrument for current market conditions is an Intentionally Defective Grantor Trust (IDGT), which gives you two separate planning opportunities. You pay the tax on the income generated by the trust—including capital-gains taxes—which allows the trust to grow for the next generation unencumbered by income tax, while reducing your estate. And individuals can transact with an IDGT without tax consequences.

Of course, such benefits come with strings attached. If you're going to sell stock in a family business to an IDGT, for example, the sale must be at arm's length so the IRS doesn't claim it's a disguised gift. And to accomplish the proper form, you must ensure that the trust has other assets—so you must "seed gift" the IDGT.

RECONSIDER LIFE INSURANCE: If you're relying on substantial real estate wealth to pay your estate taxes, you may want to take your first look in a long time at that homeliest form of investment: a life-insurance policy.

Most well-to-do clients "hate paying for life insurance," admits Jill Dodd, a partner in San Francisco-based Manatt, Phelps & Phillips. "But you can't assume that your real estate investments will be any less heavily leveraged in the future than they are now."

PLANT CDARS: Are your bank deposits arranged for maximum FDIC protection? "I've gotten dozens of questions about this since the turmoil began, says Stuart Morris, managing partner of Morris Law Group in Boca Raton, Fla.

The federal government's financial-rescue package hiked FDIC coverage to \$250,000 per account. But you might still consider signing up for CDARS, the Certificate of Deposit Account Registry Service. Up to a limit of \$50 million, CDARS allows one bank to spread your cash around to correspondent banks so you're completely covered by the FDIC—and you only get one bank statement to boot.

BECOME A MORTGAGE BANK: “If your children are trying to buy houses and having trouble getting a mortgage, or ARM rates are too high, parents could loan the money and get a few percent,” says Deborah Cochran, partner in Cochran & Owen, in Vienna, Va. “In today's market, 3 percent isn't such a bad return.”

KEEP IT IN THE FAMILY: Today's environment also favors other kinds of intra-family loans. Each month, the IRS publishes tables that specify the lowest rate that can be used for such loans without producing a taxable gift. (In November, the short-term rate for loans of up to three years was 1.63 percent.) Funds that you loan to children or to a trust for their benefit will grow in your estate at this extremely low interest rate. And your offspring can put those funds to use in a manner that, with any kind of economic growth at all in the next three years, will beat the IRS rate.

CHECK YOUR PHILANTHROPY: Many philanthropists are now establishing tighter controls over their giving in an attempt to guarantee higher satisfaction with the results.

“Even clients who are making grants to public organizations are asking for more accountability and public involvement in a program, versus just writing a check and getting an annual report at the end of the year,” says John Vryhof, partner in Snell & Wilmer in Phoenix.

You also might want to reconsider creation of the Charitable Remainder Trusts that, during times of market appreciation, allow you to escape capital-gains taxes on a designated investment as long as the underlying asset goes to a charity upon your death. “With no appreciation these days, you don't have as much incentive to create these trusts—unless you're just charitably inclined,” Cochran says.

RECALIBRATE DIVORCE: Rotten market conditions can serve as a catalyst to divorce “as money that was used to paper over a bad marriage starts to disappear,” says Steve Eisman, senior partner in Abrams, Fensterman, in New York.

And terrible times can prompt unusual tactics. For example, an individual suing for divorce from a faltering provider might want to make sure to file before the end of 2008 so that this “bad year” doesn't figure into the five-year average that courts typically use to evaluate income and assets. Conversely, the more moneyed spouse may want to try to forestall a divorce filing until 2009, when this year's massive depreciation will become part of the formula. ■

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Questions for Your Attorney

- 1. HOW SHOULD I PRIORITIZE LEGACY PLANNING?** First, make sure you've got enough assets to give away what you want without keeping yourself awake at night. And don't let the planning tail wag the returns dog: If you can make a good deal and sell an asset before you can couch it in an estate-tax-saving gambit, do it.
- 2. HOW DO I KNOW YOU'RE TURNING OVER ALL THE ROCKS?** Like everything having to do with your money these days, legal strategies should be covering unprecedented territory, looking for unseen opportunities—and avoiding new perils.
- 3. WHAT'S GOING TO HAPPEN TO ESTATE TAXES?** The exemption is scheduled to rise from \$2 million today to \$3.5 million in 2009. In 2010, estate taxes are supposed to disappear altogether before returning to 2002 levels in 2011.
- 4. WILL THE NEW CREW IN WASHINGTON AFFECT THAT?** Undoubtedly.
- 5. CAN I DELAY PAYMENT OF ESTATE TAXES IF IT'S NECESSARY?** Under certain conditions, yes.
- 6. WHAT ARE SOME OTHER WAYS THAT I CAN PASS WEALTH ON IN MY FAMILY?** You can, without tax effects, pay tuition and medical bills for grandchildren. After January 1, you can give away up to \$13,000 a year (up from \$12,000 in 2008) to any individual without gift taxes. And over your lifetime, you can give away up to an additional \$1 million tax-free to whomever you wish (although that amount, dollar for dollar, reduces what you can shield from estate taxes when you die).
- 7. WHAT MUST I DO TO PROTECT MY ASSETS IN A DOWNTURN?** Consider self-settled trusts and other instruments that can shield assets from future claims by creditors.
- 8. IS THERE ANYTHING I CAN DO TO SHIELD MYSELF AGAINST EXISTING CLAIMS BY CREDITORS?** Not really.
- 9. WHAT'S YOUR PHILOSOPHY ABOUT ASSET DIVISION AMONG HEIRS?** Most savvy attorneys will urge you to divide what you bequeath equally among your children, assuming you enjoy good relationships with all of them. Similarly, you should avoid designating specific assets—which now may seem to have roughly equal worth—for specific survivors, because of how asset values can fluctuate.
- 10. WHAT IF I SCREW UP AND NEED SOME OF MY ASSETS BACK FROM MY HEIRS?** If you have got close and trusting relationships with them, you can set up trusts that allow you to receive back assets as gifts. Or your kids could always take pity on you.