

Thursday, January 8, 1981

(S.F.78, Ro-9B)(O)7D

Inflation, taxes erode value

Estate planning reaps tax savings

This article on estate planning techniques was prepared by Thomas P. Scholler, a tax partner of Arthur Andersen & Co. in Detroit.

A "silver lining" in our currently depressed economy is that it provides an excellent opportunity to maximize the benefits of estate planning through capital asset freeze techniques.

With business activity down, the underlying value of many closely held businesses is temporarily depressed. The federal gift and estate tax is imposed upon the value of assets being transferred. If transfers can be made during periods of declined value or if the declined value can be locked in for future transfers, estate transfer tax savings can be realized.

Depending on the particular circumstances, substantial future savings may be realized with relatively little or no current cash requirement.

The high rates of inflation have become a primary consideration in family estate planning. Gift and estate tax rates are progressive and as inflation forces up the value of assets, this can result in greater tax liability. Some of

the increases in value may be actual worth because of business expansion or other reasons, but certainly some part of the increase is simply a direct result of inflation.

THE U.S. TRANSFER tax system does not differentiate between increases in estate value due to real appreciation versus increases due to general rise in price levels.

The combination of prolonged high rates of inflation and the steeply progressive estate tax rates can be truly alarming after a period of years.

For example, one dollar in asset value compounded at a conservative eight percent annual rate will increase to \$2 in nine years, \$5 in 20 years and \$7 in 25 years. With inflation running currently above 10 percent, it is conceivable that even relatively modest estates today will be pushed into the 70 percent maximum marginal estate tax bracket in the foreseeable future.

Owners of closely held businesses or family farms or ranches who wish to pass their enterprise to their heirs are particularly vulnerable to estate tax liabilities. If sufficient liquidity has not

been provided for in the estate to cover taxes due to highly appreciated valuations, the business may have to be broken up, sold or burdened with excessive cash outflows over a period of years to pay the tax liability.

A CAPITAL asset freeze is a technique which in general freezes the senior family members' ownership interest in the family business at its current level and passes on future appreciation to the family heirs free of estate tax in the senior members' estates.

A capital asset freeze involves restructuring the ownership interests in a company or property and valuing the underlying interests which have been established.

Both partnership and corporation formats may be used in this technique. The ownership rights in a business are distributed through gift or sale to various family members in accordance with the wishes of the senior family members.

The following example illustrates the potential benefits of an asset freeze. Assume a taxable estate in 1980 dollars of \$1 million and an annual in-

flation rate of 12 percent. For this example there is no appreciation in terms of real dollars.

The \$1 million taxable estate would have a present estate tax liability of about \$300,000. Over 20 years, the value of this estate would increase to more than \$3.5 million, assuming growth at the rate of inflation and no marital deduction adjustment consideration. Without an asset freeze, the transfer tax would increase to about \$5.7 million, leaving only \$3.8 million to the heirs.

STATED ANOTHER way, inflation and the progressive estate tax rates would have reduced the purchasing power of this estate by 30 percent. With proper planning and the use of the asset freeze, the same \$9.5 million taxable estate would retain a tax liability of \$300,000, allowing \$9.2 million rather than \$3.8 million to be passed on to the heirs.

Our current recessionary economy provides an excellent opportunity for the owner of a closely held business to consider a capital freeze in his estate plan. The objective of the freeze is to reorganize the enterprise in such a manner that the senior interests are frozen at the current value while future growth accrues to the heirs.

The closely held business, that is most vulnerable to high estate taxes, typically suffers a significant drop in business during economic downturns. As a result, the current value of the company can be frozen at a relatively low level to reflect current economic conditions although the prospects for future growth of the company remain excellent.

There is a great deal of flexibility in designing the capital freeze, regardless of the methods elected. The most common methods are a corporate recapitalization, a family partnership or a family holding company.

business people

RICHARD HANTON joined Lambrecht Realty Co.'s appraisal and consulting department as an assistant vice president based at the Southfield office. He was assistant vice president and appraisal division head with American Federal Savings and Loan.

ER senior vice president of administration. Fox was executive vice president and continues as chief operating officer. Wanda was vice president of finance and will continue as chief financial officer and corporate treasurer. Kule was vice president of store operations.

CHARLES SHEFFIECK of Lathrop Village has assumed the duties of managing principal/chief executive officer of Bernard, Wells, Loving & Co. He was president of his own consulting firm.

The Northfield Hilton in Troy appointed **STAN ROZMIJEJ** assistant controller, **GREG PARSONS** assistant sales manager, **VALERIE WALLACE** sales representative and **DIANE O'SHEA** of Troy conference center coordinator.

JOHN HOGAN was named marketing manager for the Troy based Budd Co.'s Aftermarket Division. He was president of the Hogan Transportation Equipment Co. in Ohio.

market place

JOEL GARRETT, president of Ladd's Inc. Realtors in Troy, has formed Hometrend of Michigan Inc., the Michigan Regional Agent for Hometrend Inc. of Georgia. Hometrend Inc. is a national real estate franchise company described as "a real estate franchise, developed by Realtors for Realtors with special emphasis placed on service needs, training and recruiting." Officers of the organization are Garrett; Ronald Schebor, vice president and director; and Bonnie Ross, vice president and director.

THE AMERICAN Society of Civil Engineers presented its 1980 Construction Management Award to Rolland Wilkening, president of Barton-Malow Co. and a Bloomfield Hills resident. The award recognizes him for contributions to construction management for 10 years of "on time and on budget" projects. He was cited for his effort to encourage a more professional approach in construction through the management process by co-authoring two books on the subject. He also is a member of the national Associated General Contractors of America board of directors.

E-Z RIZER Chair Co. appointed Thompson Advertising Productions of Farmington Hills as its advertising agency.

THE 1981 Parade of Idea Homes begins Friday and continues through March 22. The annual promotion by the Builders Association of Southeastern Michigan highlights 32 builders featuring 38 new model homes and condominiums in Wayne, Oakland, Macomb, Washtenaw and Livingston counties. A list of models and their locations is available from the association by calling 569-0644.

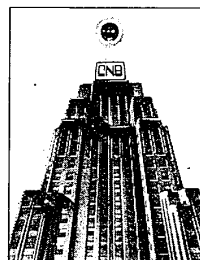
snowplow
Discover the difference!
Try a FISHER snowplow
FONTAINE TRUCK EQUIPMENT CO.
3530 CHERRY AVE.
Livonia
421-3335

BOB POSCH
Friday & Saturday
AT
THE MERIDIAN RESTAURANT
666-3780
6500 Highland
Next to Pontiac Airport Terminal Building



When you're checking on interest, look into CNB's Interest-on-Checking.

NOW...every cent you deposit in the bank can earn interest with a CNB Interest-on-Checking account. For complete information, pick up a brochure at any CNB office. The Talking Bank means business!



City National Bank

Also available at First National Bank of Plymouth, National Bank of Rochester and First Citizens Bank in Troy • Members FDIC