

Executing an Integrated Approach to Estate Planning and Wealth Management

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Well-intentioned estate planning often fails to achieve its original goals due to lack of proper administration.

Estate planning vehicles should not only be structured with due regard for a family's wealth transfer objectives, but also should be continuously monitored to determine if they are achieving their intended goals. Executing an integrated approach to estate planning and wealth management requires the collaborative efforts of a team of multi-disciplinary professionals, preferably in a single firm, to avoid the shortcomings of the traditional approach.

THE TRADITIONAL APPROACH

Traditionally, the client would work with an estate planning attorney or law firm, who would develop a basic plan and send the client off with a binder of documents and sometimes a letter of instructions to implement, oversee, and maintain the plan. In this model, the implementation and ongoing maintenance of estate plan might sometimes be picked up by one of the client's other advisors, perhaps the tax accountant or money manager, both of whom tend to have more frequent contact with the client. In many cases implementation and maintenance are neglected.

Sometimes, if some other member of the client's non-integrated group of advisors suggests something new, such as a life insurance trust, a Qualified Personal Residence Trust, a Grantor Retained Annuity Trust or a family limited partnership, the lawyer's services might again be engaged. The client might complete another specific project with the estate planning attorney, but rarely is a fully integrated plan undertaken.

The result is incomplete implementation. Measurement of success, if any, is infrequent and large time gaps pass between checkups.

In the traditional approach, the client must take the initiative to assemble and oversee the team of professionals, if this even happens at all. Pitfalls to achieving success are the client's reluctance to undertake the lead role, procrastination, and the usual anxiety about the high cost of assembling numerous professionals, all billing by the hour.

Advisors grouped in this way may fail to act as a cohesive team because they have not self-selected into this scheme. The various advisors may perceive themselves as being in competition with one another for "top dog" status. Egos prevent effective delegation and teamwork and there can be competition for limited fee income among the advisors.

With this ad hoc "team" approach, there can be a lack of ongoing effective execution because no one member of the group of advisors is responsible for overall oversight. Each team member is usually only concerned about his or her particular field of expertise.

Problems can arise from:

- Failure to follow recommended procedures.
- Failure to maintain proper books and records, such as for family limited partnership entities.
- Failure to make timely payments or distributions from estate planning vehicles such as GRATs or CRTs.
- Failure to prepare and file necessary gift tax returns and income tax returns for estate planning structures.

"Executing an integrated approach to estate planning and wealth management requires the collaborative efforts of a team of multi-disciplinary professionals..."

THE INTEGRATED APPROACH

When a client engages a multi-family office (MFO), the MFO client team should be charged with carrying out the client's estate planning and wealth management objectives in an integrated fashion. The MFO typically has a multi-disciplinary team of professionals covering the disciplines of tax, accounting, investment advisory, estate planning, philanthropy and risk management. An estate planning review should be one of the first projects undertaken by the MFO team for a new client. The review provides the team with a baseline for the client and serves as a refresher for the client of what, if anything, has been accomplished to date. The initial review can also serve as a springboard for recommended improvements to the plan.

Following this approach recognizes that the family's estate planning is not a "one-off" endeavor. Rather, it is an ongoing process of regular reviews, refined over time. Frequent communication between the MFO team and the client allows for continuous measurement of success or failure of the plan and allows for mid-course corrections to achieve estate planning goals.

Let's explore some examples.

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Family Limited Partnerships

Family limited partnerships (FLPs) are a commonly used estate planning tool to transfer wealth in the form of non-marketable limited partnership (LP) interests to junior family members (or trusts for their benefit). The valuation discounts achievable by making gifts of LP interests coupled with the control over the FLP assets retained by the senior generation through retention of general partner interests make FLPs an attractive vehicle for wealth transfers.

FLPs can be created, documented, funded, and maintained on an ongoing basis by the MFO team.

- In conjunction with outside legal counsel, the MFO will propose the FLP, make recommendations as to the terms of the FLP, review drafts and oversee execution of the necessary partnership and transfer documents.
- The investment advisory professionals on the team will help select assets in the client's portfolio best suited for funding the FLP, and once selected will set up the custody accounts for the FLP and help transfer the assets into the FLP custody accounts.
- The tax/accounting professionals on the team will apply for and obtain tax identification numbers for the FLP, and will calendar tax filing dates, estimated tax payment dates and amounts, and coordinate cash flow needs for tax payments with the investment advisory professionals, who can plan for liquidity needs within the FLP investment portfolio.
- The income tax professionals will prepare and file the appropriate annual income tax returns for the FLP, issuing Forms K-1 to the partners, and will prepare individual tax returns for the individual partners.
- If any trusts involved in the planning are partners in the FLP, the tax professionals will, if engaged to do so by the trustees of such trusts, prepare annual trust income tax returns and will coordinate cash flow needs for estimated income tax payments with the investment advisory professionals.

- The estate planning professionals, in consultation with outside estate planning counsel, will oversee engagement of any necessary appraisals and the preparation and filing of appropriate gift tax returns.
- Annual FLP meetings will be held at the instigation of the MFO client service director (often the primary income tax advisor on the team) and will be documented in the files.
- Ongoing review of asset performance in the FLP and opportunities for additional gifting (such as with increased gift tax exemptions) will be considered by frequent review by the team.

“The multi-family office team can be very effective in helping clients implement and administer GRATs.”

GRATs

Another frequently used estate planning vehicle is the Grantor Retained Annuity Trust (GRAT). A GRAT is an irrevocable trust designed to transfer future appreciation of an asset free of gift or estate taxes, after the grantor has received all payments of a reserved annuity payable from the GRAT assets for a period of years. If the annuity is structured to have a present value (using the IRS prescribed interest rate) equal to or only slightly less than the value of the assets contributed to the GRAT, the upfront taxable gift on creation of the GRAT is zero or extremely small. If the assets in the GRAT appreciate at a rate higher than the modest interest rate prescribed by the IRS, the excess

appreciation, if any, passes at the end of the annuity period free of gift taxes to the grantor’s intended beneficiaries (or to continuing trusts for their benefit). If the GRAT assets fail to outperform the IRS interest rate, the assets will all come back to the grantor in the form of annuity payments and another GRAT can be attempted, if desired.

The MFO team can be very effective in helping clients implement and administer GRATs. Attention should be paid to initial asset allocation, valuations of GRAT assets and frequent review of asset performance to identify opportunities to lock in GRAT success (or failure, to be followed by another GRAT with the now depressed assets) as asset values fluctuate. How might this play out?

- The MFO team should look for opportunities to recommend GRATs for appropriate clients, often with a series of “rolling GRATs.” A rolling GRAT structure takes the annuity payment received by the grantor from one GRAT and rolls it into a new GRAT. In this way, the process of passing excess appreciation on the asset to the beneficiaries continues.
- The investment advisory professionals will be consulted about selection of appropriate assets for each GRAT.
- The investment advisory professionals will set up custodial accounts for each GRAT and will oversee the funding of each GRAT, with due regard for the requirement that each GRAT only have a single funding.
- Ongoing review of GRAT performance by the team may uncover the opportunities to “lock in” significant gains in a GRAT. With effective coordination among MFO team members, the substitution of stable assets (such as bonds) from the grantor in exchange for appreciated, more volatile GRAT assets in a successful GRAT can be implemented quickly if the investment advisory team overseeing the client’s entire portfolio is able to recommend appropriate assets for an asset swap and efficiently implement the asset swap between custody accounts on behalf of the client.

- The tax advisors on the MFO team will prepare the computations of the gift element upon creation of the GRAT and will prepare and file appropriate gift tax returns to report the gift upon the funding of each GRAT.
- The tax advisors will prepare appropriate grantor trust income tax returns for the GRAT and report the GRAT income on the client's individual tax returns.
- New GRATs can be anticipated, created and funded with assets swapped out of successful or failing GRATs or with annual annuity distributions coming out of each GRAT (again, using so-called "rolling GRATs").
- The team will develop and maintain a calendar tickler system of GRAT annuity payment due dates and will review these deadlines in preparation for each annual annuity payment. Once assets are selected for distribution in satisfaction of a GRAT annuity payment, the estate planning professionals will document the assets to be used and their method of valuation. The investment advisory professionals will prepare and obtain signatures, if necessary, on any needed transfer documents, then will transfer assets between the GRAT custody account and the GRAT grantor's personal account.

"Success in reaching wealth transfer goals can free clients to enjoy their wealth..."

Intra-Family Loans

Wealthy families often make loans among themselves for various purposes. The senior generation might loan funds to children, grandchildren and trusts for the benefit of family members to purchase homes, enter into businesses or simply to make investments. The MFO can assist with loan transactions in the following ways to assure IRS compliance, avoid potential problems and enhance the wealth-shifting effectiveness of such loans.

- Opportunities to shift wealth by structuring low interest rate intra-family loans can be overseen by the team.
- Documenting loans with promissory notes and maintaining tickler files of interest rates, payment due dates and note maturities should be a regular item on the client advisory team's agenda.
- Opportunities to refinance higher rate notes at lower rates should be a regular review item for the MFO team when prevailing minimum intra-family "applicable federal rates" decline.
- Regular reviews among the tax, investment advisory, bookkeeping, accounting and estate planning personnel on the team will assure that interest income is properly paid or accrued and correctly reported on family members' tax returns and that any necessary gift tax returns are prepared and filed, particularly in the case where gifts might be made by the senior generation through debt forgiveness.

CONCLUSION

An integrated approach to estate planning and wealth management, employing a multi-disciplinary group of professionals working as a team, can achieve a greater likelihood of successful wealth transfer and minimization of transfer taxes. Wealthy clients who embrace this approach can hope to realize their wealth transfer goals early enough in their lifetimes to obviate reliance on transfers at death at significant extra transfer tax cost. Success in reaching wealth transfer goals can free clients to enjoy their wealth, to pursue philanthropic goals earlier in life, or to leave a larger charitable legacy at death.



Jim Cody specializes in estate and trust planning and counsels clients on sophisticated tax saving, wealth preservation and wealth transfer strategies. He has more than 25 years of professional experience. Jim earned a bachelor's degree in economics from Yale University, received his MBA from the Graduate School of Business at the University of California, Berkeley and holds a juris doctor from the University of California Hastings College of the Law.

Prior to joining Harris myCFO twelve years ago, Jim practiced law with a San Francisco Bay Area law firm where he chaired its Trusts and Estates practice group. He is a member of the State Bar of California, is certified as a legal specialist in Estate Planning, Trust and Probate Law by the California State Bar Board of Legal Specialization, and a Fellow of the American College of Trust and Estate Counsel (ACTEC).

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