



*Starting Soon....*

# 18<sup>th</sup> ANNUAL INTERGENERATIONAL ESTATE PLANNING CONFERENCE

November 8, 2023



# Welcome! Housekeeping:

**Conference Materials** can be found at: [www.pierrolaw.com/events](http://www.pierrolaw.com/events)

Click on this Intergen program.

**Accountants:** fill out the application for four free CPEs. Thanks to **MMB + CO** for sponsoring these credits!

**Fill Out the Survey** in your materials or online after the program – we value your feedback.

# ► Thank You To Our Sponsors



BUSINESS  
ADVISORS  
AND CPAS

INTERGEN

# Featured Speakers



**Louis Pierro**  
Pierro, Connor & Strauss, LLC



**Dan Nolan**  
Graypoint, LLC



**Sean Leonard**  
Graypoint, LLC



**John Sobieski**  
MMB + CO



**Nathan Schroeder**  
Empire Valuation Consultants



**Frank Melia**  
Contour Mortgage



**Gary Sancilio**  
The Affinity Group



**Theresa Skaine**  
Pierro, Connor & Strauss



**Jacob Verchereau**  
Pierro, Connor & Strauss



# Meet Kai and Jade

- ▶ Kai, 78, Successful Businessman, Founder: Cloud Dragon
- ▶ Jade, 67, Community Volunteer and Philanthropist
- ▶ **Both:** New York Residents, 2<sup>nd</sup> generation Asian American



# Kai's Health Concerns

- ▶ Kai has been diagnosed with Alzheimer's and is considered incapacitated
- ▶ Kai's company is now in limbo
- ▶ Family is concerned about the business, taxes and estate planning
- ▶ Kai's long-term care is putting a strain on finances with out-of-pocket costs at \$305K/yr.



# Previous Planning

- ▶ Prior to the illness, Kai was “too busy” to do estate planning
  - ▶ Currently has a simple will and power of attorney naming Jade without gifting powers
- ▶ Kai and Jade have not used their lifetime gift tax exemptions





# Kai and Jade's Income

## Kai

- \$900,000 per year

## Jade

- \$100,000 per year



# Kai and Jade's Assets

## Jointly Held

- ▶ Niskayuna Home \$450K
- ▶ Commercial building with tenants \$1.2M
- ▶ Liquid Assets (Investments, Cash) \$14M
- ▶ Retirement Accounts
  - ▶ Kai's Cloud Dragon 401(k) \$5M
  - ▶ Jade's Cloud Dragon 401(k) \$750K



# Kai and Jade's Insurance

## Kai

- ▶ 10-yr. term insurance purchased at age 70;
  - ▶ \$5M death benefit
  - ▶ Conversion option expires in 2 years
- ▶ Universal Life policy for \$5M – underfunded and at risk of lapsing

## Jade

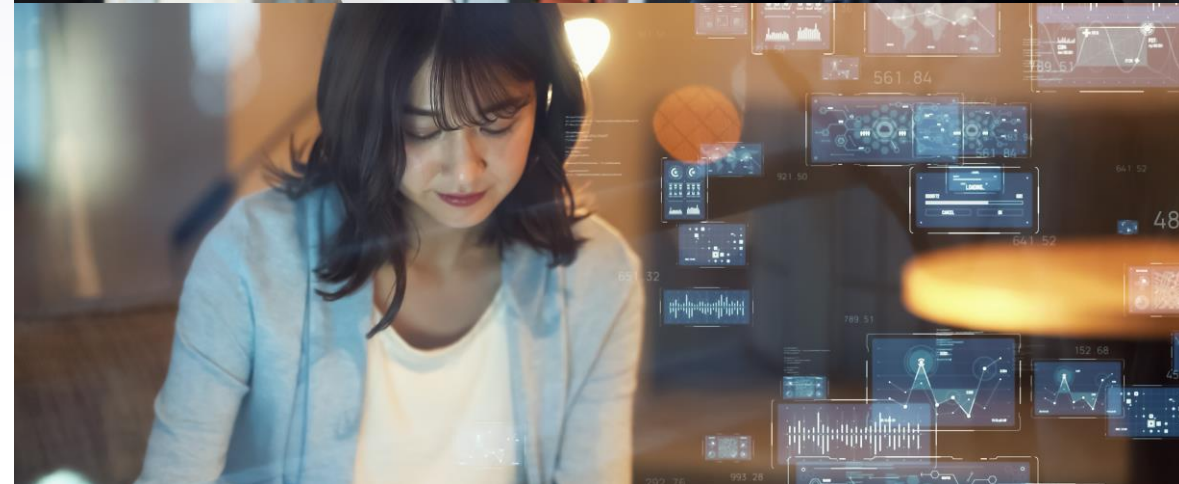
- ▶ No insurance





# The Kids

- ▶ **Melvin, 43** - married with one child - works in the business
  - ▶ Spouse, Jane, 43 and Son, Mike, age 8
- ▶ **Maria, 41** - has a significant other - works in the business
  - ▶ Significant Other, John Smith, age 41 and Daughter, Lydia, age 6
- ▶ **Michael, 38** - snowboarder, single, not in business
  - ▶ concerned that his interests are protected; brings a lawyer to the table to ensure estate equalization.

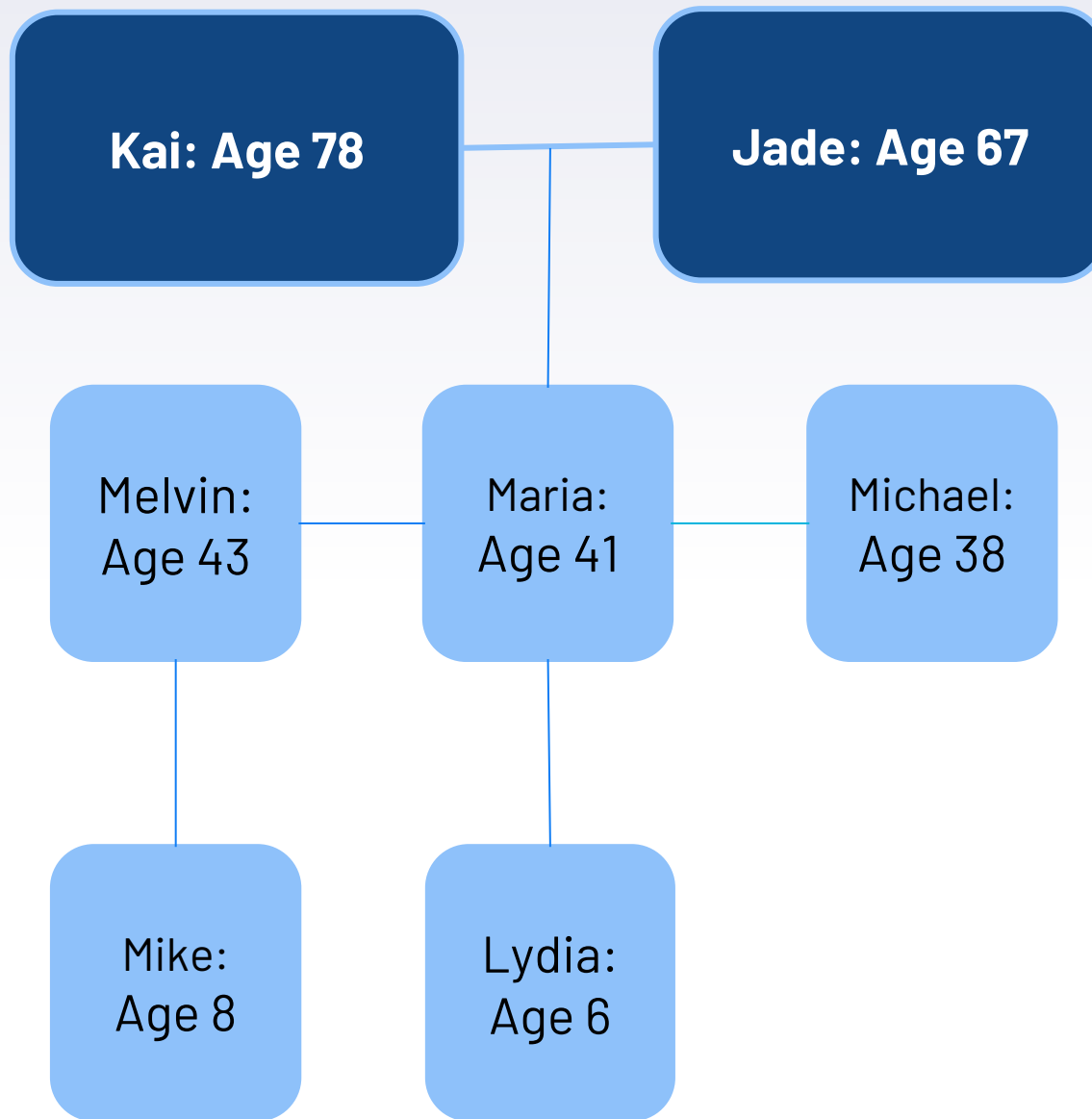


# ► The Grandchildren

- ▶ **Mike**, Melvin's Son, Age 8
- ▶ **Lydia**, Maria's Daughter, Age 6



# Family Tree



# The Business – Cloud Dragon, Inc.



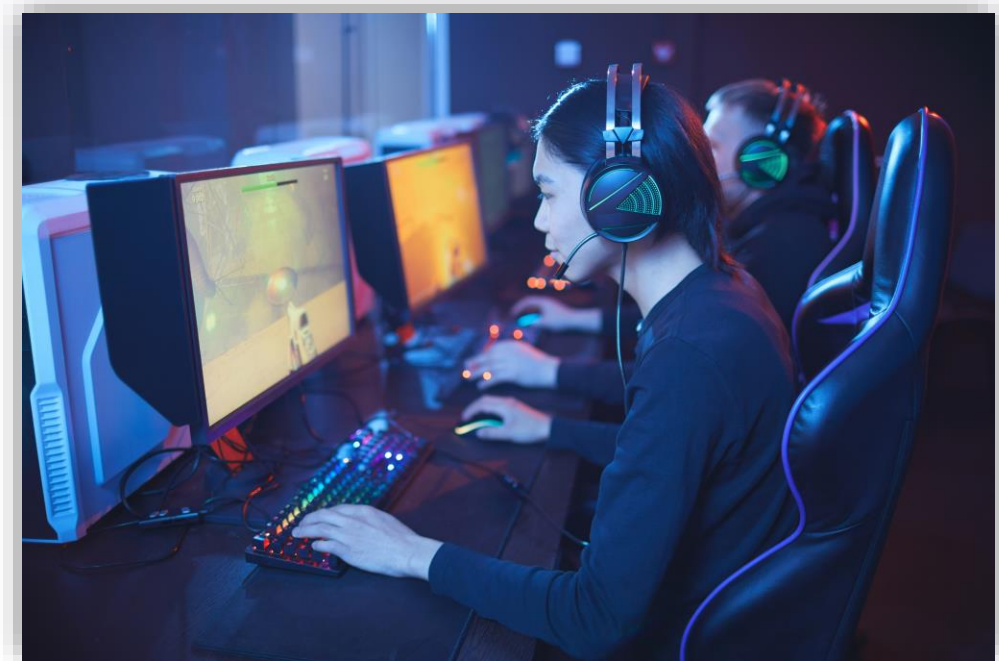
- ▶ Computer Software Company
  - ▶ S-Corp
- ▶ Kai owns 94% of the business
- ▶ Melvin and Maria (children) each own 3%
- ▶ Melvin and Maria are advocating for move into “A.I.” that could rapidly accelerate growth



# The Business – Cloud Dragon, Inc.



- ▶ Computer Software Company
  - ▶ S-Corp
- ▶ Offices in Niskayuna
- ▶ Plant in Rotterdam
- ▶ Last valuation in 1998 – \$18M
- ▶ Current family estimate – \$72M





# Current Challenges

- ▶ Given Kai's dementia and without the proper legal planning in place, no one can make legal and financial decisions on his behalf
- ▶ Jade and the children call a meeting with their team of advisors



***What steps are needed swiftly to fill the leadership gap and make moves to stabilize and modernize the company, maximize wealth, minimize tax and risk, and create a legacy for future generations?***





# GRAYPOINT

WHERE WEALTH **meets purpose**

Dan Nolan and Sean Leonard

18<sup>th</sup> Annual InterGen November 8, 2023

# Developing an Investment Strategy

## ▶ Establishing Investment Objectives

- ▶ Cash Flow Needs
- ▶ Wealth Accumulation
- ▶ Gifting
- ▶ Other

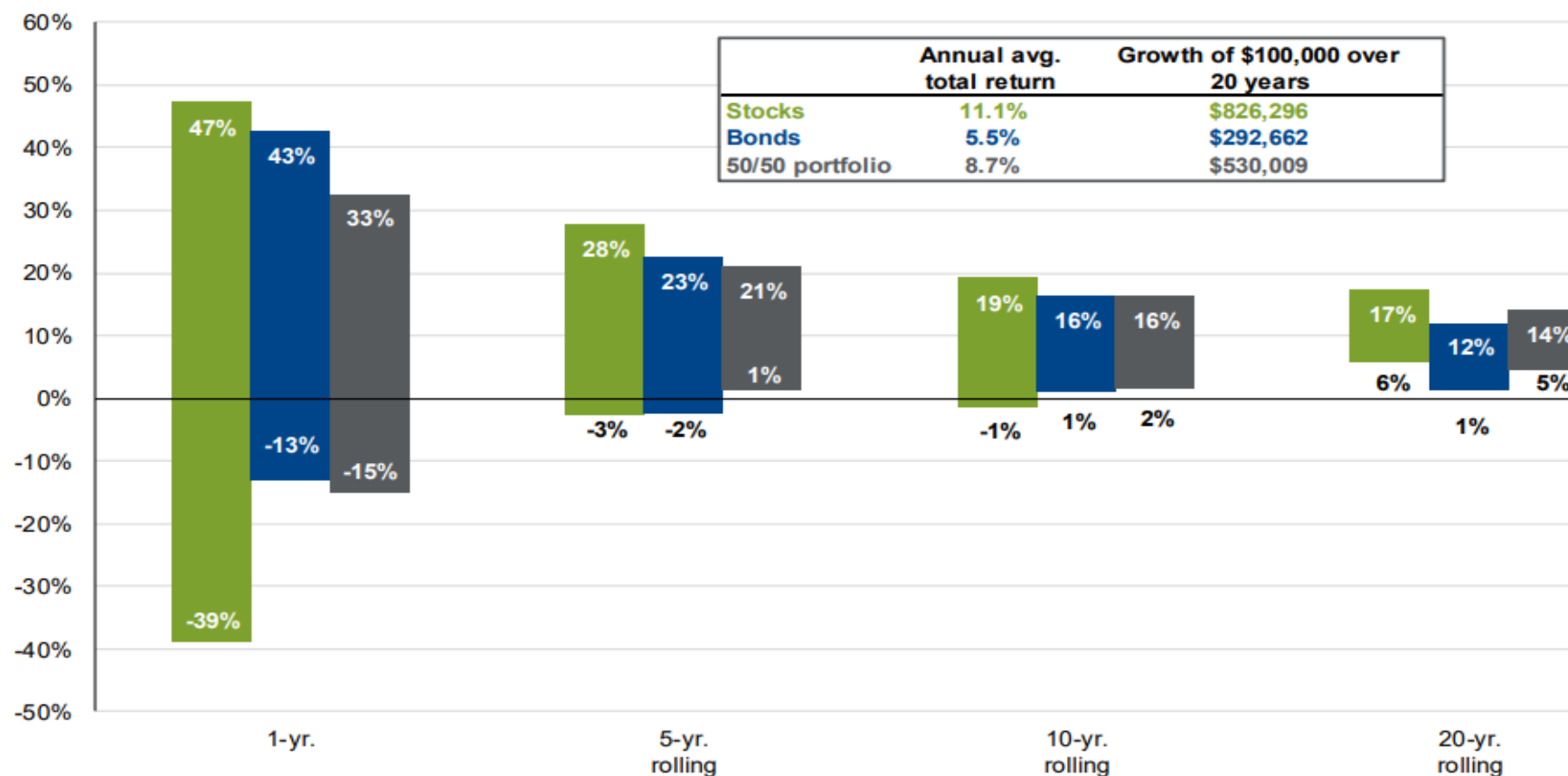
## ▶ Determining Risk Tolerance

- ▶ What is risk?
  - ▶ Price Volatility
  - ▶ Permanent Loss of Capital

# Time in the market, not timing, matters

## Range of stock, bond and blended total returns

Annual total returns, 1950-2022



Source: Bloomberg, FactSet, Federal Reserve, Robert Shiller, Strategas/Ibbotson, J.P. Morgan Asset Management. Returns shown are based on calendar year returns from 1950 to 2022. Stocks represent the S&P 500 Shiller Composite and Bonds represent Strategas/Ibbotson for periods from 1950 to 2010 and Bloomberg Aggregate thereafter. Growth of \$100,000 is based on annual average total returns from 1950 to 2022.

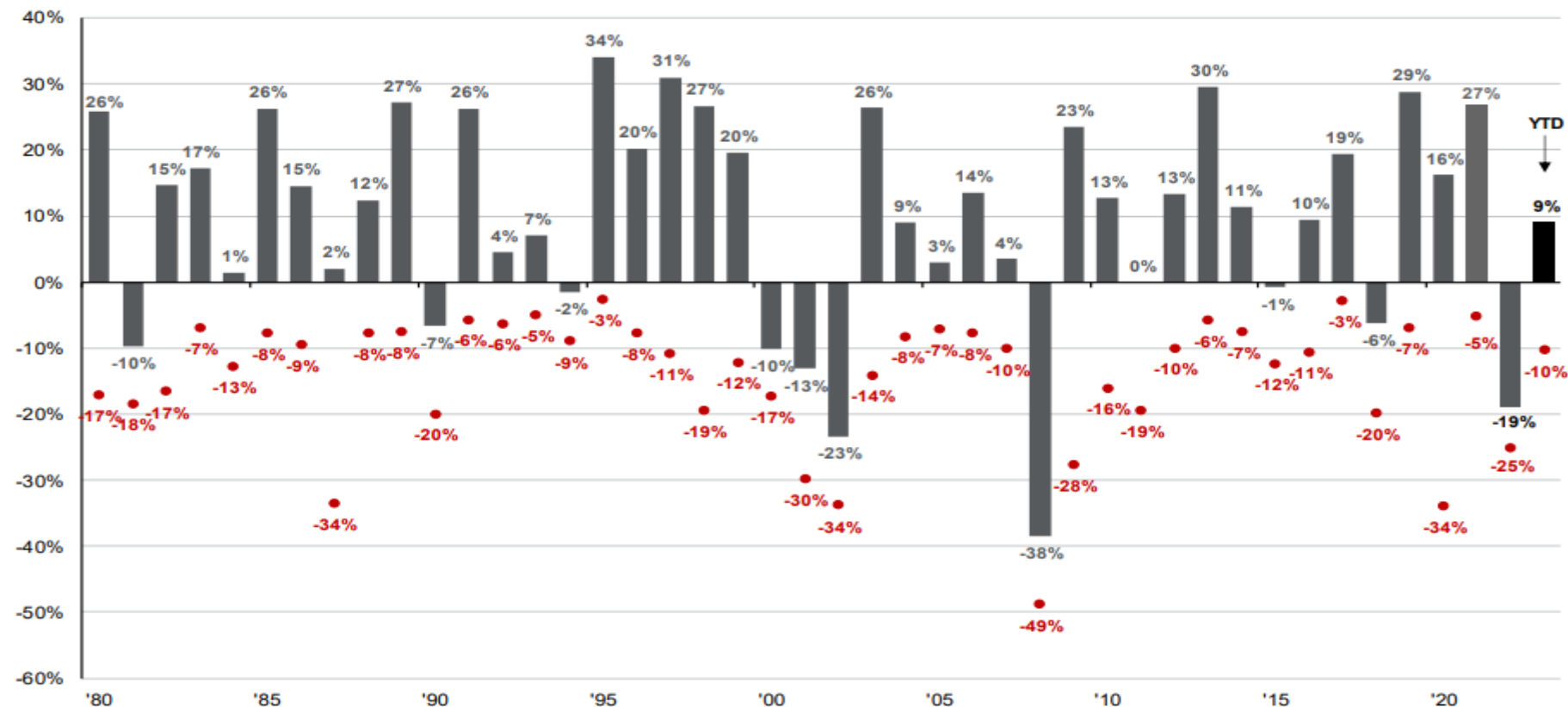
Guide to the Markets – U.S. Data are as of October 31, 2023.

**J.P.Morgan**  
ASSET MANAGEMENT

# It's never entirely safe to go in the water

## S&P intra-year declines vs. calendar year returns

Despite average intra-year drops of 14.3%, annual returns were positive in 32 of 43 years



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.

Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1980 to 2022, over which time period the average annual return was 8.7%.

Guide to the Markets – U.S. Data are as of October 31, 2023.

**J.P.Morgan**  
ASSET MANAGEMENT

# Asset Allocation improves risk-adjusted returns

2008 - 2022		Ann.	Vol.	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	YTD
Large Cap	REITs	8.8%	23.4%	Fixed Income	EM Equity	REITs	REITs	REITs	Small Cap	REITs	REITs	Small Cap	EM Equity	Cash	Large Cap	Small Cap	REITs	Comdty.	Large Cap
Small Cap	Small Cap	7.7%	23.2%	Cash	High Yield	Small Cap	Fixed Income	High Yield	Large Cap	Large Cap	Large Cap	High Yield	DM Equity	Fixed Income	REITs	EM Equity	Large Cap	Cash	Cash
REITs	EM Equity	6.6%	23.0%	Asset Alloc.	DM Equity	EM Equity	High Yield	EM Equity	DM Equity	Fixed Income	Fixed Income	Large Cap	Large Cap	REITs	Small Cap	Large Cap	Comdty.	High Yield	High Yield
Asset Alloc.	Comdty.	6.1%	20.2%	High Yield	REITs	Comdty.	Large Cap	DM Equity	Asset Alloc.	Asset Alloc.	Cash	Comdty.	Small Cap	High Yield	DM Equity	Asset Alloc.	Small Cap	Fixed Income	DM Equity
High Yield	DM Equity	5.4%	20.0%	Small Cap	Small Cap	Large Cap	Cash	Small Cap	High Yield	Small Cap	DM Equity	EM Equity	Asset Alloc.	Large Cap	Asset Alloc.	DM Equity	Asset Alloc.	Asset Alloc.	Asset Alloc.
Fixed Income	Large Cap	2.7%	17.7%	Comdty.	Large Cap	High Yield	Asset Alloc.	Large Cap	REITs	Cash	Asset Alloc.	REITs	High Yield	Asset Alloc.	EM Equity	Fixed Income	DM Equity	DM Equity	EM Equity
DM Equity	High Yield	2.3%	13.0%	Large Cap	Asset Alloc.	Asset Alloc.	Small Cap	Asset Alloc.	Cash	High Yield	High Yield	Asset Alloc.	REITs	Small Cap	High Yield	High Yield	High Yield	Large Cap	Fixed Income
EM Equity	Asset Alloc.	1.0%	12.4%	REITs	Comdty.	DM Equity	DM Equity	Fixed Income	Fixed Income	EM Equity	Small Cap	Fixed Income	Fixed Income	Comdty.	Fixed Income	Cash	Cash	EM Equity	Comdty.
Cash	Fixed Income	0.6%	12.2%	DM Equity	Fixed Income	Fixed Income	Comdty.	Cash	EM Equity	DM Equity	EM Equity	DM Equity	Comdty.	DM Equity	Comdty.	Comdty.	Fixed Income	Small Cap	Small Cap
Comdty.	Cash	-2.6%	0.4%	EM Equity	Cash	Cash	EM Equity	Comdty.	Comdty.	Comdty.	Comdty.	Cash	Cash	EM Equity	Cash	REITs	EM Equity	REITs	REITs

Source: Bloomberg, FactSet, MSCI, NAREIT, Russell, Standard & Poor's, J.P. Morgan Asset Management.

Large cap: S&P 500, Small cap: Russell 2000, EM Equity: MSCI EME, DM Equity: MSCI EAFE, Comdty: Bloomberg Commodity Index, High Yield: Bloomberg Global HY Index, Fixed Income: Bloomberg US Aggregate, REITs: NAREIT Equity REIT Index, Cash: Bloomberg 1-3m Treasury. The "Asset Allocation" portfolio assumes the following weights: 25% in the S&P 500, 10% in the Russell 2000, 15% in the MSCI EAFE, 5% in the MSCI EME, 25% in the Bloomberg US Aggregate, 5% in the Bloomberg 1-3m Treasury, 5% in the Bloomberg Global High Yield Index, 5% in the Bloomberg Commodity Index and 5% in the NAREIT Equity REIT Index. Balanced portfolio assumes annual rebalancing. Annualized (Ann.) return and volatility (Vol.) represents period from 12/31/2007 to 12/31/2022. Please see disclosure page at end for index definitions. All data represents total return for stated period. The "Asset Allocation" portfolio is for illustrative purposes only. Past performance is not indicative of future returns.

Guide to the Markets – U.S. Data are as of October 31, 2023.

**J.P.Morgan**  
ASSET MANAGEMENT

# Primary Investment Considerations

- ▶ \$14MM liquid portfolio, \$5MM Kai 401K, \$750K Jade 401K
- ▶ Historical Income: ~\$1.7MM pre-tax, \$875K after-tax
  - ▶ \$1MM business income between Kai and Jade (expected to continue)
  - ▶ Estimated \$370K liquid portfolio income
  - ▶ \$220K Kai RMDs
  - ▶ \$100K real estate income
- ▶ Historical Spending - \$500K
- ▶ Historical Cash Flow buffer after spending - \$375K
- ▶ New cash flow buffer after \$305K health care aide expense - \$70K
- ▶ **Conclusion: Income sufficiency but lack of buffer will create anxiety**



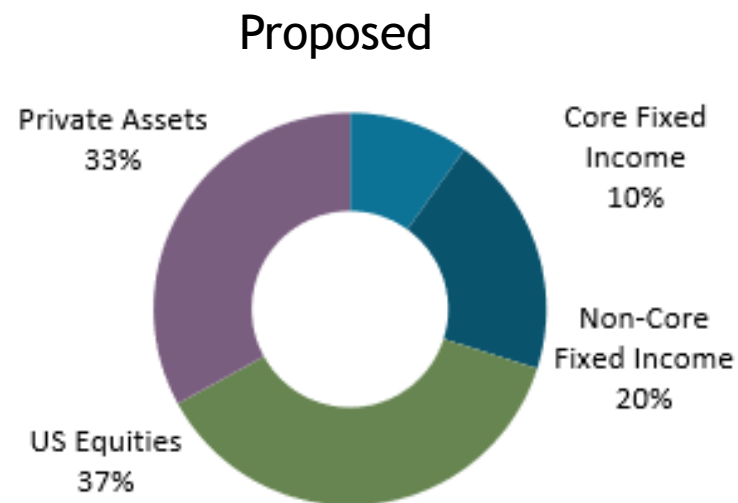
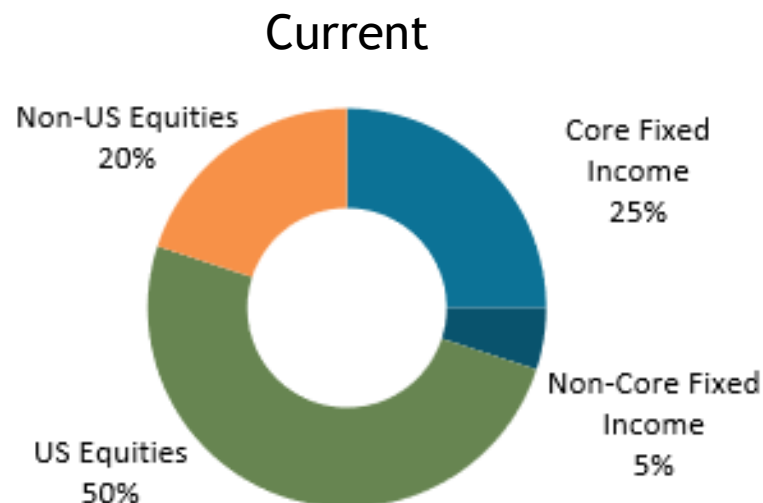
# Other Considerations

- ▶ Can the portfolio be structured to improve peace of mind for Jade?
  - ▶ What is the risk profile of the portfolio
  - ▶ What are the income tax consequences
  - ▶ What is Jade's ability to weather market volatility
- ▶ Will future cash flow growth keep pace with inflation?
- ▶ Can assets be better utilized to maximize estate transfer?
  - ▶ Capital needed for insurance
  - ▶ Ability to maximize estate transfer in the future

# Current Environment

- ▶ Today's markets provide unique opportunity to restructure portfolio
  - ▶ Highest yields in years means many investors have capital losses in their bond portfolios and ability to lock in attractive municipal bond yields farther out the curve
  - ▶ 2022 equity sell-off means many equity mutual fund investors have low capital gains exposures as managers paid out gains following 2021 and are now sitting on losses
  - ▶ Private assets provide ability to enhance cash flows while dampening risk and the liquidity profile lines up well with long-horizon retirement dollars here

# Proposed Portfolio Changes



## Return Estimates

	Current	Proposed
Pre-Tax Return	8.1%	8.7%
After-Tax Return	5.2%	6.0%
After-Tax Yield	1.7%	2.9%
Pre-Tax Yield (\$MM)	\$0.6	\$0.8

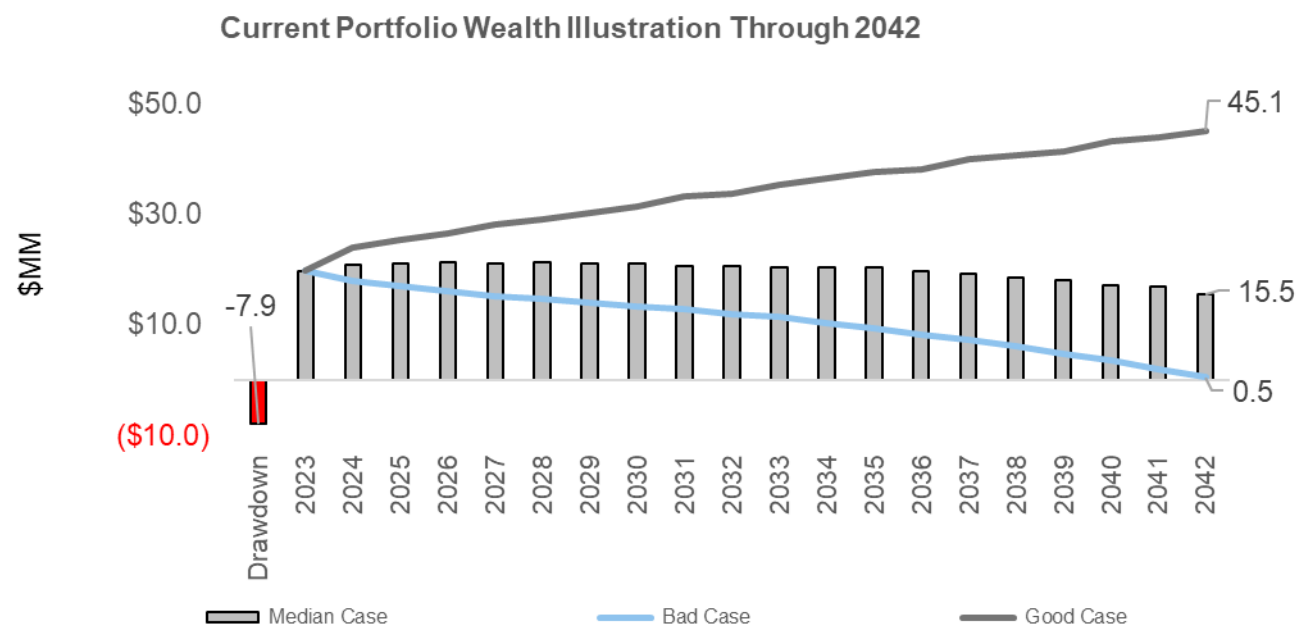
## Risk Characteristics

	Current	Proposed
Standard Deviation	11.2%	6.8%
Sharpe Ratio	0.38	0.74
Maximum Drawdown %	-40.2%	-31.5%
Maximum Drawdown (\$MM)	(\$7.9)	(\$6.2)

- Given high net wealth and still long horizon, adopting a less conventional portfolio structure can solve income needs while reducing volatility for Jade

# Cash flow analysis - current

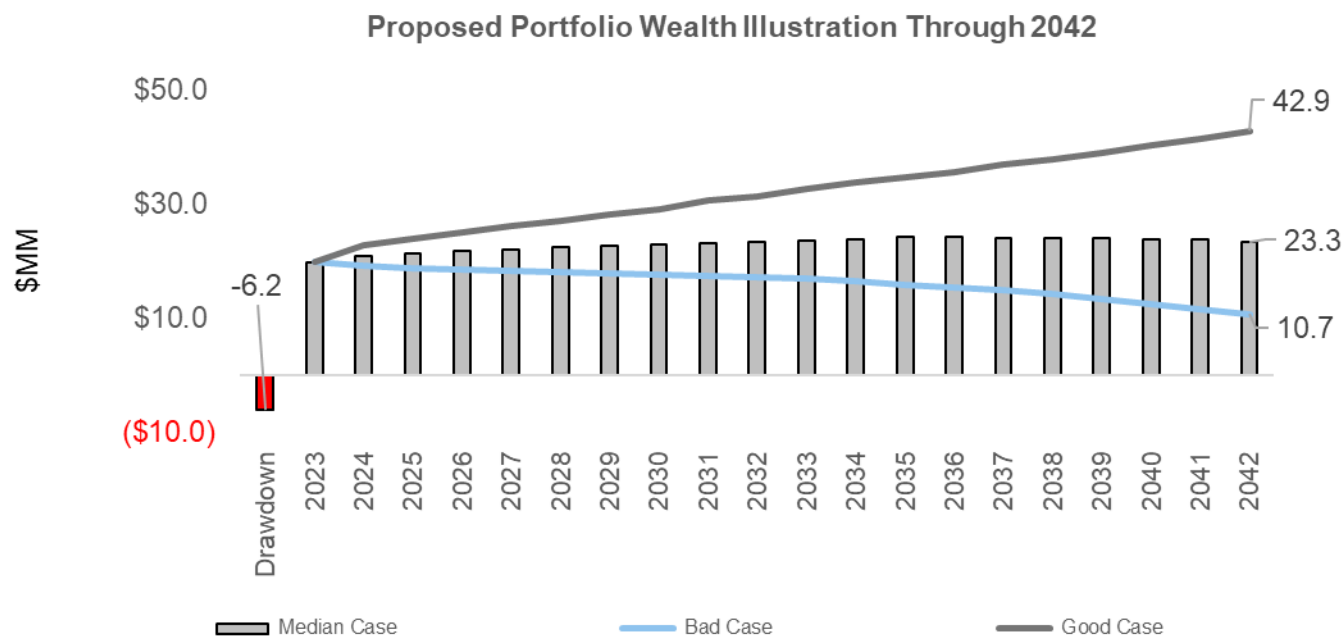
- Current cash flow analysis assuming 4% per year spending inflation, 70/30 stock/bond portfolio with estimated 5.2% after-tax return



- Conclusion: asset level likely to support future spending needs but potentially vulnerable if poor equity market returns over the next several years, limiting ability to carve out assets for estate planning purposes

# Cash flow analysis - proposed

- Current cash flow analysis assuming 4% per year spending inflation, 37% stock/30% bond/33% alternatives with estimated 6.0% after-tax return



- Conclusion: properly selected alternatives can reduce drawdown and improve outcomes in poor equity markets, freeing up capital for wealth transfer (insurance and GRATs)

# Implementation considerations

- ▶ Invert normal liquid/IRA conversation due to potential for excess wealth transfer
  - ▶ Usually IRA growth and reinvestment is maximized for income tax efficiency
  - ▶ Here, putting high yielding private investments in IRA can provide durable income and portfolio stability while maximizing liquid asset flexibility for estate transfer
- ▶ Asset sufficiency depends on overall spending levels on the portfolio as well as the sequence of returns.
  - ▶ Weak initial returns result in poor outcomes and increase depletion risk
  - ▶ Moderate initial returns imply no depletion risk for this client
  - ▶ Strong initial returns result in higher outcomes but increase future estate tax liability
  - ▶ A GRAT (Grantor Retained Annuity Trust) strategy for the equity portion of liquid assets is a very effective estate transfer tool here. Excess appreciation if there are strong initial returns can be transferred to heirs without increasing risk of depletion.



# GRAT investment considerations

- ▶ Inflows and outflows should be cash or liquid stocks to avoid need for third party valuations on asset transfers
  - ▶ E.g., Do not transfer municipal bonds
- ▶ GRATs transfer excess appreciation above required annuity payments to beneficiaries. Higher volatility assets (e.g., single stocks) are better candidates for GRATs.
- ▶ Buy, sell and substitute more complicated securities within the GRAT to avoid valuation issues.
  - ▶ E.g., fund with cash, buy a structured note within the GRAT then sell the note and purchase municipal bonds within the GRAT to lock-in gains rather than swapping in externally held municipal bonds for the GRAT note to lock in gains.
- ▶ In this fact pattern, invest some of the liquid assets in a tax-loss harvesting strategy to build a tax-loss deferral against successful GRAT income taxes.



# Guardianship Planning

Jacob Verchereau, Esq.

Pierro, Connor & Strauss, LLC

# Why Is “Guardianship” Being Presented Today?

- ▶ Kai has been diagnosed with dementia; he can no longer make legal decisions for himself.
- ▶ The “simple” POA Kai executed before he lost mental capacity does not grant Jade gifting power; thus, she is presently unable to do any of the above planning for Kai (i.e., financial, insurance, tax, trust/ estate, business/ corporate, etc.)
- ▶ Therefore, the Court must now appoint a guardian over Kai’s “property” before any of his planning can be done.

# Guardianship In New York – Article 81 Of The Mental Hygiene Law

## THE THESIS

- ▶ A model statute with appropriate focus on individual rights
- ▶ But policies and practices can diminish those rights in some cases

## THE CAUSE

- ▶ Well-intentioned tendency to favor paternalism over autonomy

## THE FACTS

- ▶ Growing numbers of incapacitated seniors and younger persons with disabilities who have no advance directives

# Guardianship in New York State

- ▶ A judicial process by which a person (generally, a close relative) petitions the New York Supreme Court.
- ▶ A judge can appoint another person (or persons) to handle the medical and/or financial affairs of a person who is believed to be incapacitated (the “Alleged Incapacitated Person” or “AIP”).



# Distinguishing a Power of Attorney

- ▶ Powers under a POA are similar to guardianship (in fact, POAs are often preferable if the forms have been prepared correctly).
- ▶ A POA is a legal document, executed by a “Principal,” which appoints someone of their choosing (the “Agent”) to act on his/her behalf.
- ▶ The Agent can make financial decisions for the Principal, but [specific gifting and trust making] powers must be added to authorize further estate planning
- ▶ Kai’s POA was drafted by his real estate attorney and lacks the appropriate powers

# Health Care Proxies

- ▶ Similar to a POA, but relates to medical decision-making
- ▶ HCPs appoint someone to make critical health decisions, including end of life choices
- ▶ Kai does not have a Health Care Proxy





# Are Guardianship Cases Adversarial?

Article 81 Guardianships are considered “adversarial” proceedings, even though they are usually pursued with the AIP’s best interests in mind.

- ▶ The “Petitioner” is asking the Court to take away a person’s right to make his or her own medical and/or financial decisions and give those rights to someone else (the Guardian).
  - ▶ That is why you are required to “serve” the Alleged Incapacitated Person (“AIP”) with a Petition, and the Court grants the AIP the right to a hearing (to challenge or consent to the guardianship).

# When Is ART. 81 Guardianship Needed?

New York Courts ask two questions:

1. Is the AIP unable to care for their own property (i.e., financial) and personal (i.e., medical) needs?
2. Is the AIP likely to suffer harm because s/he cannot understand the consequences of not being able to care for their property and/or personal needs?

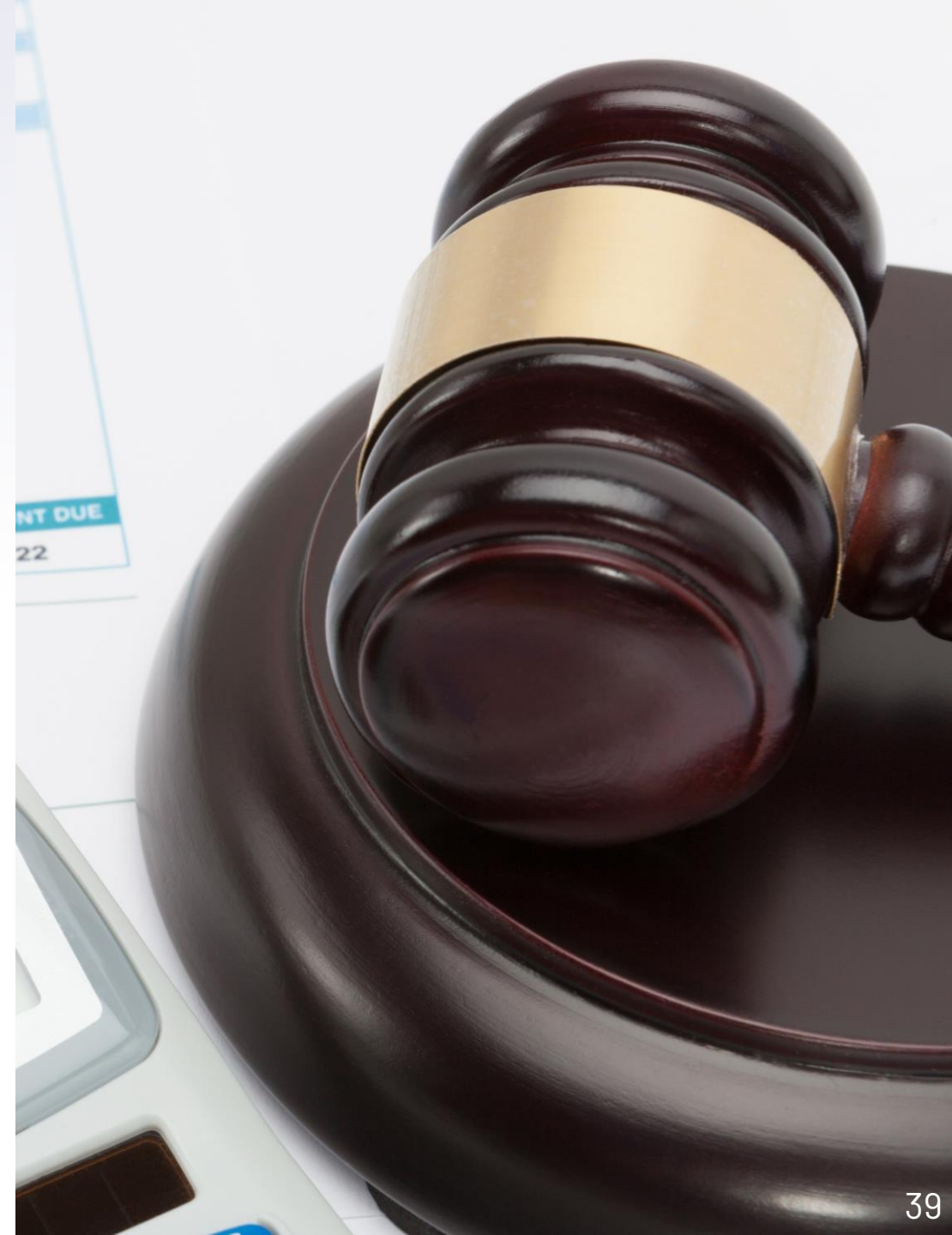
*\*\*The Court's analysis focuses on functional capacity, as opposed to an AIP's medical diagnoses\*\**

# Problems With Guardianship

- ▶ Guardianship as a highly intrusive intervention should be used only as a last resort
- ▶ Cost
- ▶ Court Process is Public
- ▶ Contested vs. Uncontested
- ▶ Court Evaluator/Court Appointed Attorney
- ▶ Availability / Admissibility of Financial & Medical Records
- ▶ No alternative for Kai
- ▶ Not an issue for Kai
- ▶ Kai and Jade's standing in the community
- ▶ Kai's family is in agreement
- ▶ The complex plan being proposed for Kai must be accepted by the judge, who relies on outside attorneys
- ▶ Kai's condition is clear

# Court Evaluator

- ▶ The Court may appoint any person drawn from a list maintained by the Office of Court Administration
- ▶ Has knowledge of property management, personal care skills, problems associated with disabilities, etc.
- ▶ Including, but not limited to, an attorney-at-law, physician, psychologist, accountant, social worker, or nurse
- ▶ Limited pool of business and tax expertise



# ▶ The Court Decides “Who”

If the Court determines that a guardian is needed, then the focus shifts to who should be appointed.

The selection of particular a guardian (or, co-guardians) is in the court’s discretion

***The Court considers a wide range of factors...***

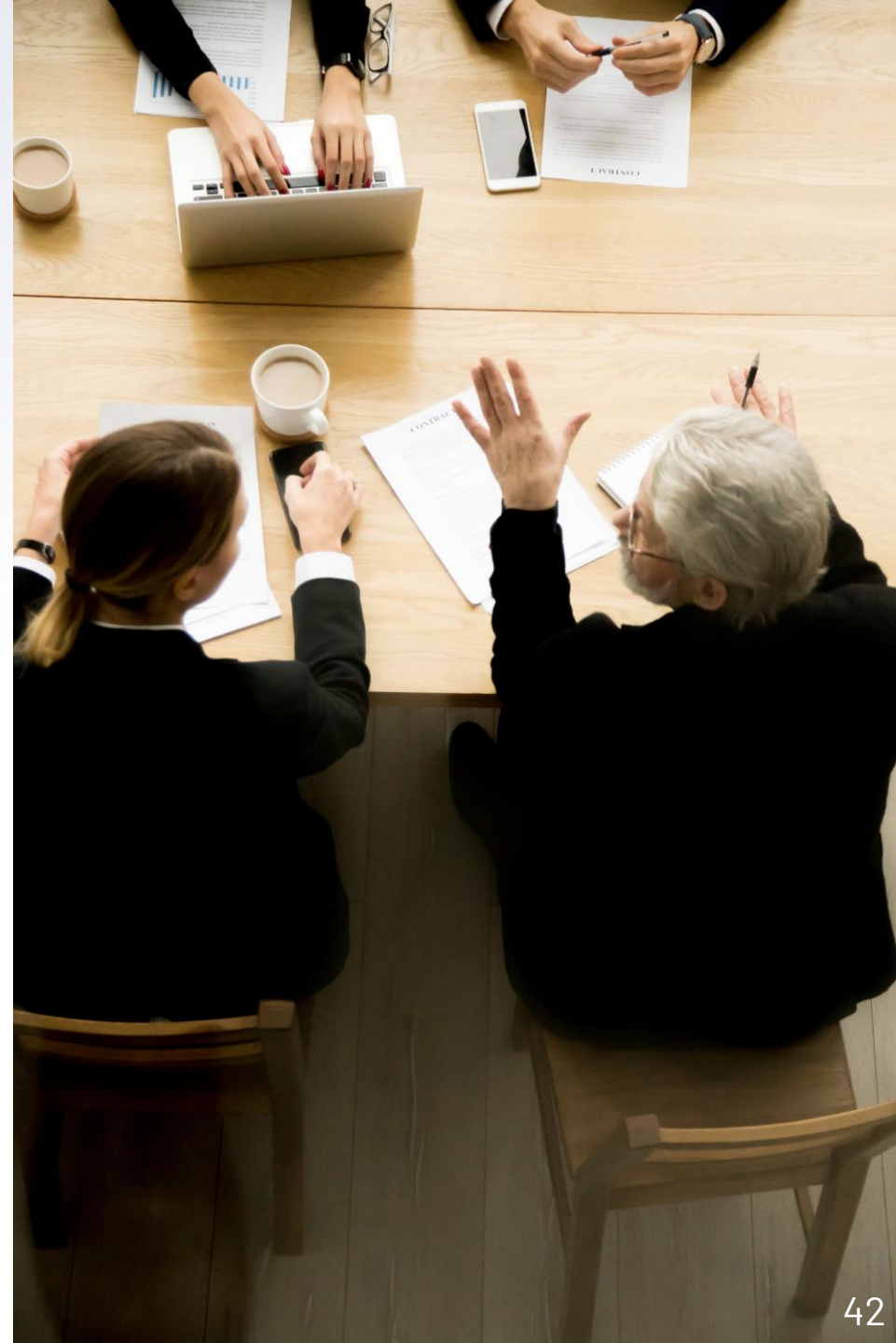
# The Guardianship Process For Kai

- ▶ Jade files a petition jointly with the kids, seeking co-guardianship.
- ▶ The family all gets along, so it's unlikely that the petition will be contested.  
(But Michael's attorney is involved)
- ▶ All agree that Jade is the best candidate to manage Kai's personal/ medical needs
- ▶ The kids Melvin and Maria are the best candidates to serve as co-guardians of the property to manage assets, pay bills and plan for business and tax matters



# The Guardianship Process For Kai

- ▶ A court evaluator will conduct an investigation (written report will be finalized and submitted to the Court within 2 to 3 weeks after the petition has been filed)
- ▶ Then a hearing will be held. The Judge will ask questions and allow testimony. If anyone were to object, this would be their opportunity to put on witnesses.



# The Guardianship Process For Kai

- Assuming the Judge agrees, he would grant the Petition formally appointing:

**Jade as Guardian  
of the Person**



**Melvin and Maria as co-guardians  
of Kai's property**



# What Planning Can Be Done

***Case law: Florence, Sur. Ct., Nassau Co. 1988***

## **Doctrine of Substituted Judgement**

- ▶ Court permitted transfers in the interest of tax savings
- ▶ Must be consistent with the incapacitated person's wishes

## **"Florence" is an estate planning case**

- ▶ The court considers life expectancy, care needs and health status

# Solving Challenges for Kai

The statute allows the court to authorize the guardian to exercise powers on behalf of the incapacitated person:

- ▶ Manage the property and financial affairs
- ▶ Transfer a part of the person's assets for the benefit of another person
- ▶ Make gifts
- ▶ Enter into contracts
- ▶ Create trusts which can extend beyond the person's life

# Solving Challenges for Kai (continued)

Petitioner must establish:

- ▶ Reasons why proposed disposition of Kai's property should be made
- ▶ Kai's needs can be met from remainder of assets once plan is adopted
- ▶ Proposed plan will produce estate, gift, income or other tax savings which will significantly benefit Kai and family
- ▶ A competent, reasonable individual in Kai's position would be likely to perform the acts under the same circumstance

***A comprehensive legal and financial plan will need to be prepared and presented to the Court.***





# Thank You

**Jacob Verchereau, Esq.**

Associate Attorney

[jverchereau@pierrolaw.com](mailto:jverchereau@pierrolaw.com)

518-459-2100





# Estate Planning

Louis Pierro, Esq., Founding Partner  
Pierro, Connor & Strauss, LLC

# \$12.92 Million Gift and Estate Tax Exemption \$25.84 Million for Married Couples

## REASONS TO DO ESTATE PLANNING NOW:

1. Reduction to \$5 mil. (adjusted – anticipate ~\$7 mil) on 12/31/25
2. Remove future appreciation
3. Utilize Grantor Trust “Burn” (more later)
4. Interest rates continue to rise (GRAT’s, Note Sales)
5. FLP/LLC Discounts may be disallowed (okay for now)
6. No portability of GST Exemption
7. No NYS Gift Tax, and 3-year clawback
8. Can use LLC’s, SLAT’s, BDIT’s, etc. to retain use + control

# Tax Planning & Interest Rates

## **Lower Rates Favor**

- GRATs
- Sales to IDGT
- CLATs
- Private Annuities
- Split-Dollar Life Insurance
- Sales to SLATs
- Sales to BDITs

## **Higher Rates Favor**

- QPRTs
- GRITs
- CRATs
- Graegin Loans
- Farmland Alternative Valuation

## **Generally Neutral**

- CRUTs
- CLUTs
- ILITs

# Spousal Lifetime Access Trusts (SLATs)

## Planning Objectives

- ▶ Capture full current gift/estate tax and GST exemptions
- ▶ Remove future growth from estate tax base
- ▶ Reduce exposure to New York estate tax
- ▶ Preserve access to assets if needed
- ▶ Retain asset management and control



# ► Jade – Trust for Kai and Descendants

- ▶ Funding target – \$12–\$13 million
- ▶ Liquid assets (not 401(k))
- ▶ Sever joint tenancy; avoid step transaction treatment
- ▶ High basis assets first – no step-up at death



# Trust Design – Jade’s Trust for Kai and Descendants

- ▶ Full distribution discretion
- ▶ Grantor Trust for Income Tax Purposes
- ▶ Remainders in trust to preserve GST exemption, protection from creditor, spousal and “significant other” claims
- ▶ Trustee choice – Children? Independent?
- ▶ Management strategy – 401(k) distributions used first; absorb medical expense deductions?
- ▶ What if Kai dies first? Loans to Jade? Power to add Jade as a beneficiary?



# Kai – Trust for Jade and Descendants

- ▶ Funding target - \$12 - \$13 million
- ▶ Guardianship court- must approve gifting plan
- ▶ Cloud Dragon shares – discounted value
- ▶ Defined value formula clause?
- ▶ Use Delaware for Fully Directed Trust?



# Trust Design – Kai's Trust for Jade and Descendants

- ▶ Full distribution discretion
- ▶ Grantor Trust for income tax purposes
- ▶ Corporate management – director and shareholder provisions
- ▶ S Corporation status preservation – QSST and ESBT issues
- ▶ Management of S Corporation shareholder income taxes
- ▶ Will existing estate plan constrain court approval of trust beneficiaries?
- ▶ Reciprocal trust issues if two SLATs are created

# Trust Design – Kai's Trust for Jade and Descendants (cont.)

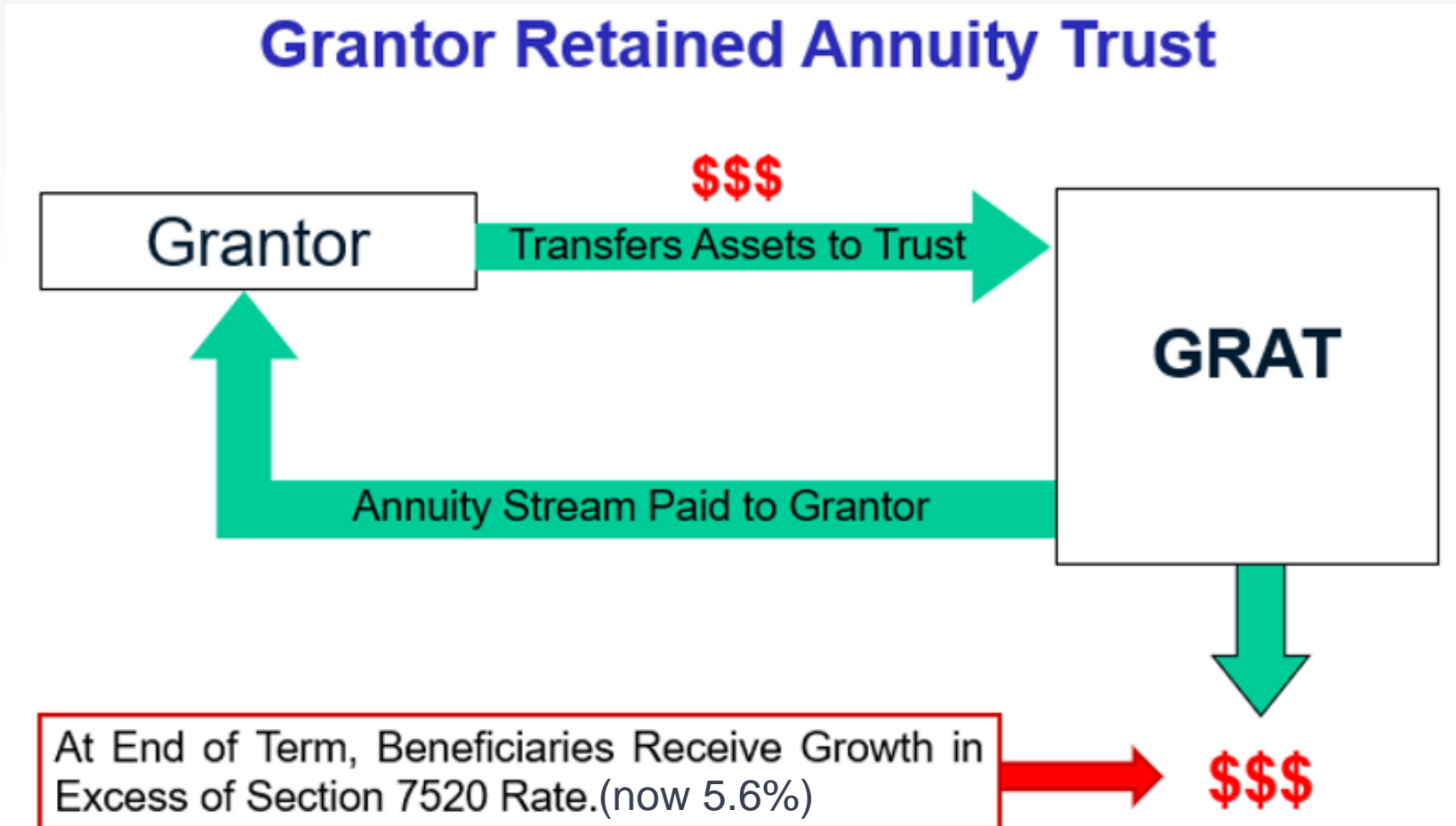
- ▶ Will existing estate plan constrain court approval of trust beneficiaries?
- ▶ Kai's existing will – spouse, then children equally
- ▶ Must follow intent – how will Michael be equalized?
- ▶ Reciprocal trust issues if two SLATs are created –
  - ▶ Vary funding, timing and terms



# Grantor Retained Annuity Trust (GRAT)

- ▶ Irrevocable lifetime trust.
- ▶ Grantor retains an annuity from transferred property for a number of years or lifetime.
- ▶ Following Grantor's annuity term, all property (plus appreciation) passes to Grantor's heirs with no further transfer tax.
- ▶ *CAVEAT: Taxable gift of the projected value of the REMAINDER interest to Grantor's heirs may occur upon creation if not "Zero'd" out*
- ▶ Taxable Gift = Fair Market Value of Property minus Present Value of Grantor's Annuity Stream based on IRS 7520 rate.

# Grantor Retained Annuity Trust (GRAT)





# Interest Rate Arbitrage Fading

	<u>Nov. 2021</u>	<u>Nov. 2022</u>	<u>Oct. 2023</u>
Short Term AFR =	<b>.22%</b>	<b>4.1%</b>	<b>5.12%</b>
Mid Term AFR =	<b>1.08%</b>	<b>3.97%</b>	<b>4.19%</b>
Long Term AFR =	<b>1.86%</b>	<b>3.92%</b>	<b>4.19%</b>
7520 Rate =	<b>1.4%</b>	<b>4.8%</b>	<b>5.0%</b>

# Grantor Retained Annuity Trust (GRAT)

- ▶ Assume Kai gifted \$4,000,000 to a 5-year GRAT in November 2023 when the 7520 rate is 5.6%
- ▶ Assume Cloud Dragon has annual growth of 3%
- ▶ Kai retains an annuity stream of 7% of the fair market value of Cloud Dragon, valued each year.
- ▶ Result: Kai will have made a taxable gift of \$2,791,000 and, at the end of 5 years, the children will receive \$3,140,000.

Economic Schedule						
<u>Year</u>	<u>Beginning Principal</u>	<u>3.00% Growth</u>	<u>0.00% Annual Income</u>	<u>Required Payments</u>	<u>Distributed Discount</u>	<u>Remainder</u>
1	\$4,000,000.00	\$117,900.00	\$0.00	\$280,000.00	\$0.00	\$3,837,900.00
2	\$3,837,900.00	\$113,037.00	\$0.00	\$280,000.00	\$0.00	\$3,670,937.00
3	\$3,670,937.00	\$108,028.12	\$0.00	\$280,000.00	\$0.00	\$3,498,965.12
4	\$3,498,965.12	\$102,868.96	\$0.00	\$280,000.00	\$0.00	\$3,321,834.08
5	\$3,321,834.08	\$97,555.02	\$0.00	\$280,000.00	\$0.00	\$3,139,389.10
Summary	\$4,000,000.00	\$539,389.10	\$0.00	\$1,400,000.00	\$0.00	\$3,139,389.10



# Grantor Retained Annuity Trust (GRAT)

- ▶ Use "zeroed-out GRAT" if no taxable gift is desired.
- ▶ For example: If instead Kai retains a 23.16% annuity, the taxable gift will be 0.
- ▶ Suggestion: Leave a minimal taxable gift to start the statute of limitations and prevent IRS step-transaction argument.



# ► Grantor Retained Annuity Trust (GRAT)

**Successful GRAT = choosing appreciating property that will outperform the IRS 7520 rate!**

## Key Tradeoffs

- ▶ If the GRAT property underperforms the Section 7520 rate, no tax savings is achieved (and if the GRAT is depleted, no property is transferred to the remainder beneficiaries.)
- ▶ If the GRAT property underperforms the Section 7520 rate, gift taxes paid and/or any applicable exclusion amount used will be wasted (though the amounts would be minimal).
- ▶ If the grantor does not outlive the term of years, any property remaining in the GRAT is includable in the grantor's gross estate for federal gift and estate tax purposes.
- ▶ If the GRAT is unsuccessful, any costs incurred to create and maintain the GRAT will have been wasted.

# Grantor Retained Annuity Trust (GRAT)

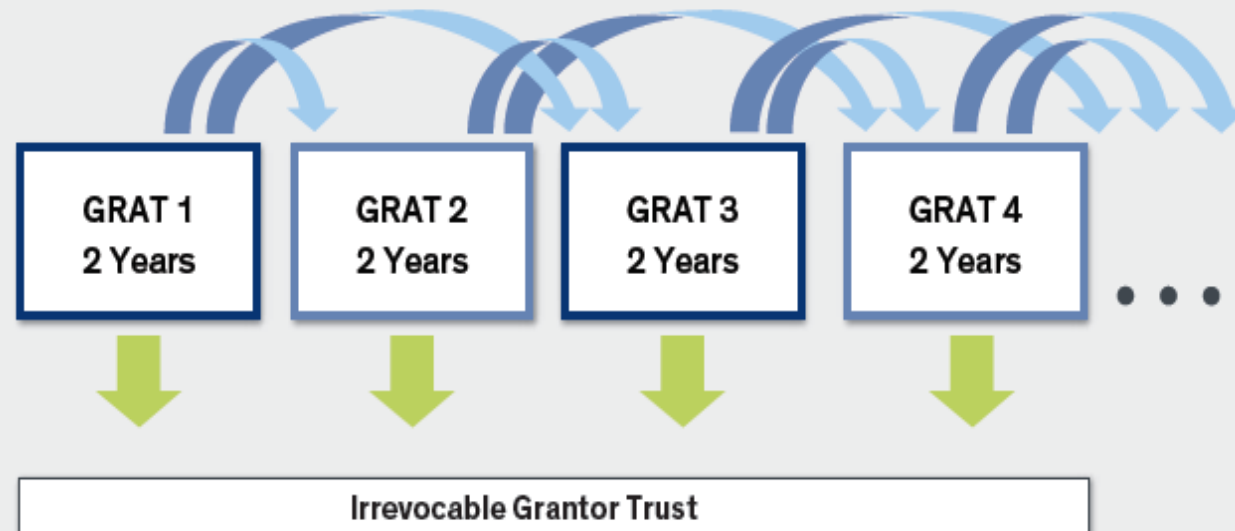
## How is it implemented?

- ▶ Hire an experienced attorney to draft the GRAT document.
- ▶ Have property that is transferred to GRAT professionally appraised.
- ▶ Transfer property to GRAT (i.e., retitle assets).
- ▶ File gift tax return(s).
- ▶ Manage GRAT assets carefully

# Grantor Retained Annuity Trust (GRAT)

## CASCADING SHORT TERM GRATs AS A MORTALITY HEDGE

- Contribute initial assets to a two-year trust
- Annual payout is contributed to a new two-year GRAT every year
- Any assets remaining in a GRAT at the end of its term pass tax-free to a grantor trust for the children\*



*\*Assuming the GRAT is zeroed-out so that the present value of the annuity stream, discounted by the Section 7520 rate, equals the original contribution, and assuming the grantor survives the term of the GRAT*

*Source: AB*



Thank You

**Louis Pierro, Esq.**

Founding Partner

[lpierro@pierrolaw.com](mailto:lpierro@pierrolaw.com)

518-459-2100



BUSINESS  
ADVISORS  
AND CPAS

# Accounting Issues and Tax Planning

John Sobieski, Principal, CPA  
MMB + CO



BUSINESS  
ADVISORS  
AND CPAS

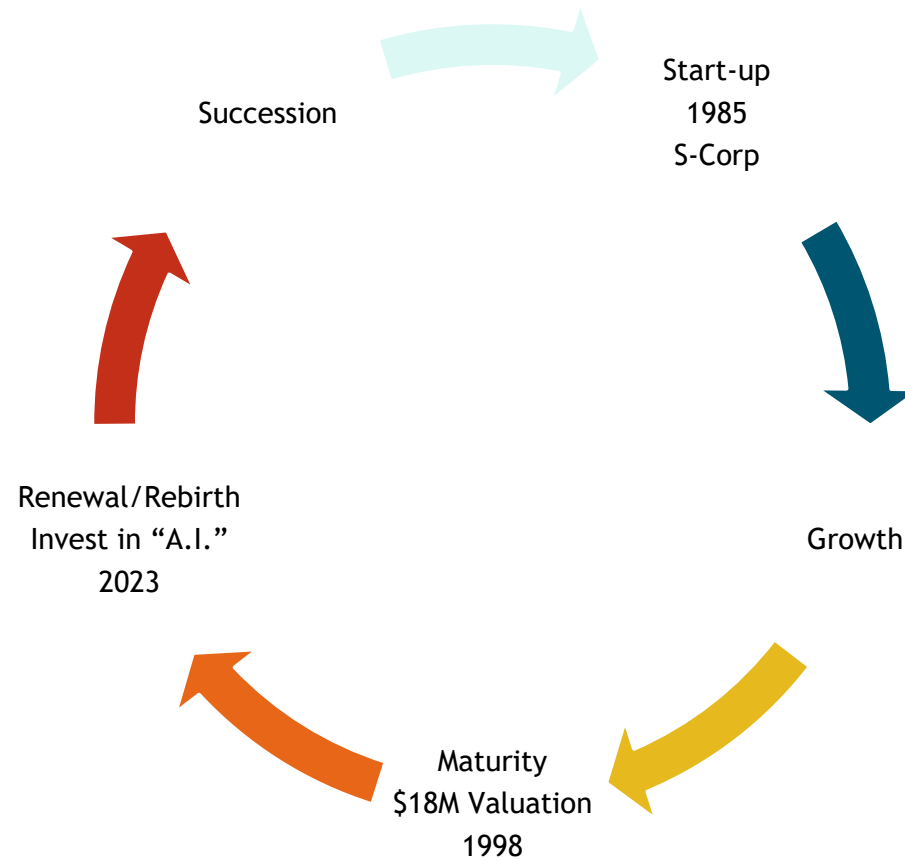
# Intergen Estate Planning Conference

November 8, 2023



# Tax Considerations

## ► Life Cycle of a Business - Cloud Dragon, Inc.



# Tax Considerations

- ▶ Historical (Tax) Approach to Entity Creation/Operation
- ▶ Small Businesses Formation:
  - ▶ Partnerships
  - ▶ S-Corporation
  - ▶ Limited Liability Company (LLC)
- ▶ Why?
  - ▶ Earnings and/or Losses “flow-through” to the individual owners (no tax paid by the entity)





# Tax Considerations

- ▶ But Why Not a C-Corporation?
  - ▶ “Double Taxation”
    - ▶ Corporation pays tax
    - ▶ Shareholder pays tax on salary or dividend
  - ▶ Prior to a 2017 Tax Act
    - ▶ Flow-through owners could keep 55% of earnings
    - ▶ C-corp owners could keep 45% of earnings
    - ▶ 10% swing

# Tax Considerations



## 2017 Tax Act (The Tax Cuts and Jobs Act of 2017)

C-corp now has a 21% flat tax rate

- Still double taxation

Qualified Business Income (QBI) Deduction

- 20% deduction for certain taxpayers



Did this change anything?

# Tax Considerations

- ▶ Cloud Dragon, Inc. - Goals for the Future
  - ▶ Renewal/Rebirth Stage
    - ▶ Kai's health and age spur change
    - ▶ The family wants to fortify ownership and leadership
    - ▶ Kai's health and reluctance has created a need for estate planning
    - ▶ Both Melvin and Maria are advocating a move into "A.I."
    - ▶ This move to A.I. should provide much needed expansion and growth
    - ▶ The family would like to minimize taxes in any way possible
    - ▶ Cloud Dragon would like to retain as much of earnings as possible
  - ▶ Should Cloud Dragon consider a Conversion to a C-Corporation

# Tax Considerations

## ► S corporation vs. C corporation

	C-Corp	S-Corp
Taxes	Double Taxation	Single layer
Losses	NOL carryforward	Offset personal income
Number of Shareholders	Unlimited	100
Types of Shareholders	Any	Limited
Origin of Shareholders	Domestic/Foreign	Domestic only
Classes of Stock	Multiple classes	One class
Equity Financing/Reward	Easier to raise/issue	Harder to raise/issue



# Tax Considerations

- ▶ Conversion from S-corp to C-corp considerations:
  - ▶ Easy to do
  - ▶ Kai's written consent needed
    - ▶ If ownership is changed before conversion - owners with 50% more of stock must consent
  - ▶ If Kai has any built-up equity (retained earnings) in the s-corp, it might make sense to distribute those earnings to Kai before converting to a c-corp
  - ▶ Cloud Dragon recapitalized - creates voting and non-voting shares for Kai, Melvin and Maria. Potential class A and class B shares.



# Tax Considerations

- ▶ Conversion from S-corp to C-corp considerations:
  - ▶ Dragon creates a stock option plan
    - ▶ The plan will provide additional equity opportunities for Melvin and Maria
    - ▶ The plan can be used as an incentive to lure new potential hires for the “A.I.” venture
    - ▶ Stock can be offered to potential new/nonfamily executives
  - ▶ Dragon’s financial statements will now need to account for a deferred tax asset/liabilities - changing the presentation
  - ▶ Dragon will now be able to offer equity stakes in the company to a potential investor if capital for the “A.I.” investment is needed or other future needs
  - ▶ Dragon will now be able to deduct any state taxes owed as his was formally a liability of each of its shareholders

# Tax Considerations

- ▶ If Dragon decides not to convert to a C-corp, care must be taken with any stock transferred to a Trust
  - ▶ An S-corporation can only have certain shareholders
- ▶ Kai's Trust for Jade and/or Descendants
  - ▶ QSST (Qualified Sub-chapter S Trust) or ESBT (Electing Small Business Trust)
  - ▶ Can be a shareholder in Dragon
  - ▶ Modeled after the “grantor” type trust
  - ▶ Beneficiary/Trustee must elect QSST/ESBT status
    - ▶ All income of the trust must be (or must be required to be) distributed to Jade
    - ▶ Jade is essentially now treated as the S-corp shareholder
  - ▶ A QSST instrument is required

# Tax Considerations



- ▶ Commercial Real Estate - Jointly owned by Jade & Kai
  - ▶ Convert ownership to an LLC (partnership)
  - ▶ Consider terms of LLC agreement
  - ▶ Potential borrow against equity
  - ▶ Make NYS PTET Election

# Tax Considerations

## ▶ Other Tax Planning

- ▶ Research and Development Credit/Expensing/Study - Dragon and Kai likely felt the pain of the change the tax law change in 2022
  - ▶ Dragon should take careful consideration of how this change will affect any future expenses incurred for the new “A.I.” venture
- ▶ IRC 1202 Planning/Potential (Qualified Small Business Stock)
  - ▶ Dragon, Melvin and Maria should consider the possibility of forming a separate entity for the new “A.I.” venture with the provisions of 1202 in mind
  - ▶ If Dragon were to seek a long-term future investor (owner), consideration should be made as to converting Dragon into a new C-corp

# Tax Considerations

## ► Other Tax Planning

- Although Cloud Dragon's main customers are NYS based, new out of state operations and customers will require proper state tax planning and compliance
- Kai and Jade may want to consider structuring a Family Limited Partnership to manage their non-Dragon assets and utilize any gifting opportunities using a discount



# John Sobieski, CPA

- ▶ Principal
- ▶ 11 British American Blvd,  
Latham, NY 12110
- ▶ [JSobieski@mmb-co.com](mailto:JSobieski@mmb-co.com)
- ▶ 518-785-0134



BUSINESS  
ADVISORS  
AND CPAS





# Business Valuation for Cloud Dragon

Nathan Schroeder

Senior Manager, Empire Valuation Consultants, LLC





# Valuation of Cloud Dragon & a Court Decision Impacting Valuation

---

Nathan Schroeder  
Senior Manager  
(585) 794-5721  
[nschroeder@empireval.com](mailto:nschroeder@empireval.com)

**Privileged & Confidential**

# Agenda

- Empire Overview
- Why Do I Need A Valuation?
- Overview Of Valuation Process
- Standards of Value
- Basic valuation methodologies
  - Income Approaches
  - Market Approaches
  - Cost Approach
- General Factors Affecting Valuation
- Current Factors Affecting Valuation



# Agenda-Continued

---

- Valuation of Cloud Dragon
  - Exit or Growth?
  - What's its Story?
  - Historical Financials
  - Levels of Value
  - Earnings Capitalization and Guideline Company Approaches
  - S-Corp / Tax Pass-through Adjustment Calculation
- Cecil v Commissioner
  - Tax Court decision on Tax Affecting a S-Corp
  - Other Tax Court decisions



# Empire Corporate Overview

---

- One of the largest independent valuation firms in the U.S.
- Founded in 1988; have performed tens of thousands of business and intangible valuations across the globe
- Specialize in providing independent valuations
  - Valuation is our specialty and our only business
  - Your valuation project is our #1 priority and only focus
- Highly credentialed and experienced staff
- Offices in New York, Long Island, San Francisco, Rochester, and Boston

# Our Experience and Expertise

- We have over 35 years of experience in business valuation
- We perform over 1,500 valuations per year
- Our experience transcends industries and all sizes and stages of a company's life cycle
  - Our professionals apply both common and uncommon valuation methods that are in the best interest of our clients



# Trust & Estate Group Experience

---

- Empire performs over 600 estate and trust valuations each year
- Operating companies
- Real estate and investment holding companies
- Carried interest
- Royalty interest
- Sports franchises
- Promissory notes
- Split-Dollar Insurance

# Why Do I Need A Valuation?

---

- Estate/corporate planning
- Income tax reporting, including gift tax
- Financial reporting



# Overview of Empire's Valuation Process

## SCOPE OUT ENGAGEMENT

Speak with client to get preliminary information and determine scope of valuation

Economic and industry research

Financial market research and analysis and value determination

Follow-up questions; Draft analysis provided; review analysis with management

## VALUATION

## DATA & INFORMATION GATHERING

Financials and projections prepared and submitted to valuation firm, along with additional company information

Due Diligence Meeting held with management

## COMPLETION

Finalize analysis and report



# Scope Out Engagement - an Empire Process

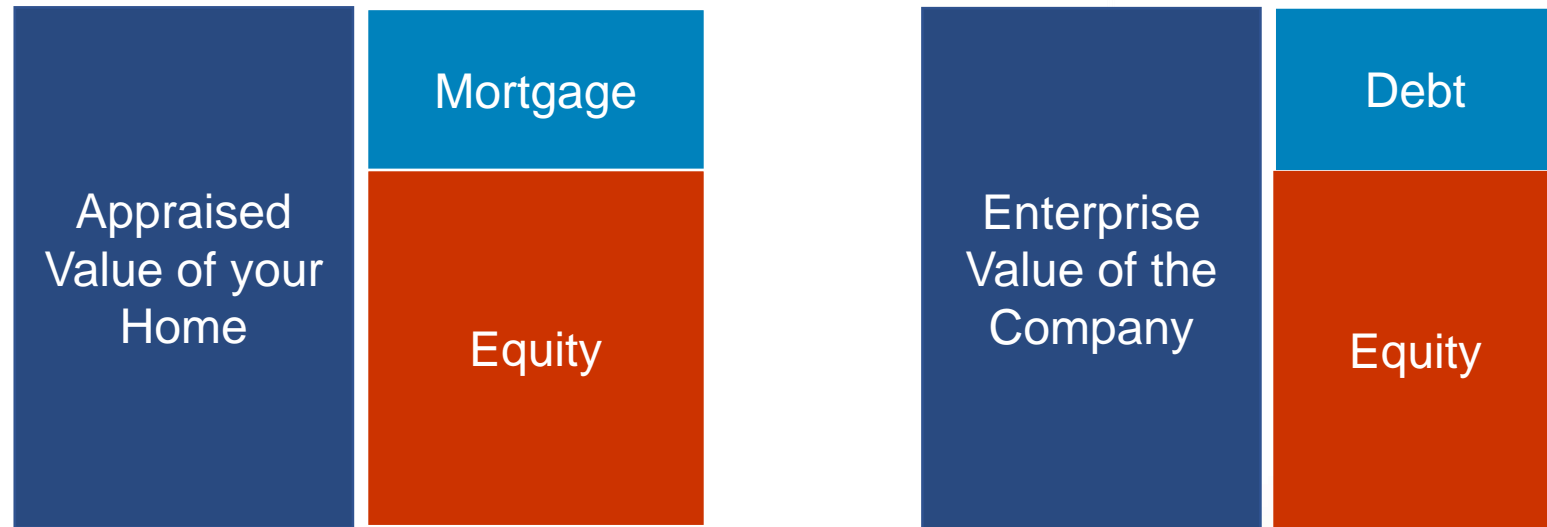
---

- Information requested to scope out engagements:
  - Purpose (gift, corporate/estate planning, potential sale, etc.)
  - Five years of financial statements
  - Capital structure of company
  - Industry info
  - Any potential financing in the near-term
  - Any potential transactions in the near-term (sale, acquisition, etc.)

# Basic Valuation Theory

- What is a valuation?

- A valuation is similar to a real estate appraisal. Instead of determining how much your home is worth, it determines the enterprise value of the business.



# Standards of Value

---

## ■ Fair Market Value

- **Definition:** “the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts” (IRS Treasury Regulations 20.2031-1(b))
- **Focus:** Buyer and seller are hypothetical and typical
  - Used for gift and estate tax planning and reporting, charitable contributions, and employee stock ownership plans (ESOPs)

# Standards of Value (continued)

---

## ■ Fair Value (financial reporting)

- **Definition:** “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date” (Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820))
- **Focus:** Market participants and willing buyer but NOT necessarily a willing seller

## ■ Fair Value (legal)

- varies state to state and is defined by legal statutes and case law.
- Used on shareholder disputes and marital disputes

# Valuation Methodologies

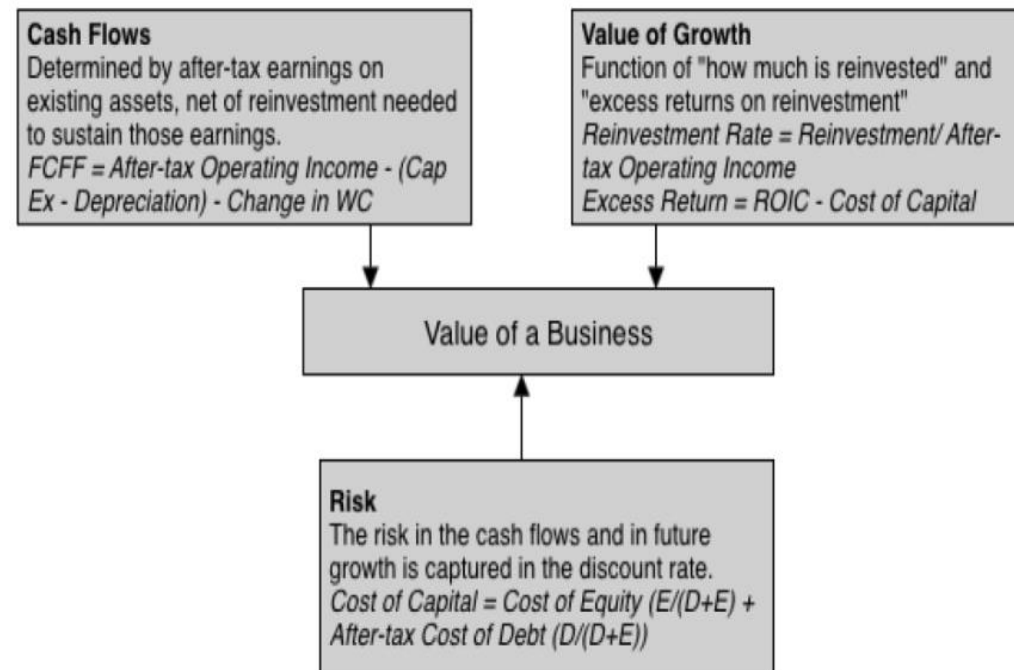
---

- Income Approach
  - Capitalization of historical cash flow
  - Discounted cash flow (“DCF”)
- Market Approach
  - Guideline publicly-traded
  - Guideline transactions
  - Prior transactions
- Cost or Asset Approach
  - Adjusted net asset value
- Each may be used separately and in conjunction with each other in a weighted approach or as a reasonableness test



# Income Approach

- The **Income Approach** uses valuation techniques to estimate value based on an expected stream of benefits (earnings or cash flows) adjusted for projected growth and estimated risk.
- Two common methods under this approach are:
  - capitalization of benefits method (“Earn Cap”), which is based on adjusted historical results; and
  - the discounted future benefits method (“DCF”), which is based on discrete projections for several future periods.



Source: Aswath Damodaran, *Musings on Markets: Tax Reform, 2017: Promise of Plenty or Poisoned Chalice?*, October 10, 2017



# Market Approach

© Randy Glasbergen  
www.glasbergen.com



**“Is it better to invest during a bull market or bear market?  
Depends...would you rather be gored or mauled?”**

- The **Market Approach** uses prices and other relevant information generated by market transactions.
- Two common methods under this approach are:
  - the guideline company method, which considers transactions that generally involve minority positions in publicly-traded companies; and
  - the guideline transaction method, which considers third-party and arms-length transactions in the subject company as well as transactions in similar entities.

# Cost or Asset Approach

- The **Asset Approach** determines the value of a business based on the value of its assets net of liabilities.
- Typically, the asset-based approach should be considered in valuations conducted at the enterprise level and involving:
  - real estate holding company
  - investment holding company
  - a business appraised on a basis other than as a going concern
    - nascent companies, troubled companies with minimal earning potential, or companies facing likely near-term liquidation



# General Factors Affecting Valuations

- Profitability
- Company's performance, relative to similar companies in the industry
- Balance sheet
- General economic conditions
- Industry and industry trends
- Management team and company outlook

# Current Factors Affecting Valuations

---

- General economic uncertainty
- Interest rates
- Recent supply chain and labor market issues
- Overall market multiples/M&A activity
- Sunset of the Tax Cuts and Jobs Act (2025)
  - Immediate expensing of capital expenditures (already partially decreased); expires January 1, 2027
  - Current corporate tax rate lowered to 21% in 2017; expected to remain at this level, unless Congress changes it
  - Gift tax exclusion (\$12.92MM in 2023) amount may decrease by half (\$6.2MM) at end of 2025





# Cloud Dragon Valuation – Exit or Growth?

---

## ■ Potential Exit Strategies

- Sale or transfer to family members
- Sale to a third party (competitor, or company in a complementary industry)
- Sale to a third party (private equity or investor)
- Sale to ESOP
- Sale to management team

## ■ Potential Growth Strategies

- Acquisition of a competitor or company in a complementary industry to gain market share or size
- Entry into new market/product line; could be organic growth or acquisition

# Cloud Dragon – What's the Company's Story

---

## Fundamentals

- Distressed or fundamentally strong

## Business cycle sensitivities

- cyclical, sensitive, defensive

## Lifecycle stage

- start-up, high growth, slow growth, decline

## Degree of specialization

- franchise or commodity-like

**COMPARATIVE INCOME STATEMENTS**  
**CLOUD DRAGON**  
**FOR THE YEARS ENDED DECEMBER 31,**

	HISTORY 2017	HISTORY 2018	HISTORY 2019	HISTORY 2020	HISTORY 2021	HISTORY 2022
<b>TOTAL REVENUES</b>	35,831,808	37,324,800	38,880,000	40,500,000	45,000,000	50,000,000
Materials	7,166,362	7,464,960	7,776,000	8,100,000	9,000,000	10,000,000
Labor	8,241,316	8,584,704	8,942,400	9,315,000	10,350,000	11,500,000
Less Cost of Goods Sold	15,407,677	16,049,664	16,718,400	17,415,000	19,350,000	21,500,000
<b>GROSS PROFIT</b>	20,424,131	21,275,136	22,161,600	23,085,000	25,650,000	28,500,000
Kai (Patriarch)	800,000	1,000,000	1,000,000	1,000,000	1,000,000	1,200,000
Jade (Wife)	180,000	200,000	200,000	200,000	200,000	220,000
Melvin (Son)	285,077	300,081	315,875	332,500	350,000	350,000
Maria (Daughter)	285,077	300,081	315,875	332,500	350,000	350,000
Michael (Son, at-large board member)	8,000	10,000	10,000	10,000	10,000	10,000
Other Officers	1,505,465	1,381,108	1,482,490	1,587,750	1,937,500	2,145,000
Officers' Salaries	3,063,620	3,191,270	3,324,240	3,462,750	3,847,500	4,275,000
Admin & Warehouse	3,676,344	3,829,524	3,989,088	4,155,300	4,617,000	5,130,000
Depreciation	4,374,000	4,374,000	4,617,000	4,878,000	5,233,500	5,986,800
<b>Total Operating Expenses</b>	11,113,963	11,394,795	11,930,328	12,496,050	13,698,000	15,391,800
<b>NET OPERATING INCOME</b>	9,310,167	9,880,341	10,231,272	10,588,950	11,952,000	13,108,200
Interest Income	6,987	7,133	7,430	7,740	10,260	17,100
Interest Expense	(18,688)	(66,138)	(122,525)	(167,619)	(302,800)	(584,700)
<b>Total Other Income (Expense)</b>	(11,700)	(59,005)	(115,095)	(159,879)	(292,540)	(567,600)
<b>PRE-TAX INCOME</b>	9,298,467	9,821,336	10,116,177	10,429,071	11,659,460	12,540,600
Provision (Benefit) for Taxes	0	0	0	0	0	0
<b>NET INCOME</b>	9,298,467	9,821,336	10,116,177	10,429,071	11,659,460	12,540,600



**COMPARATIVE BALANCE SHEETS****CLOUD DRAGON****FOR THE YEARS ENDED DECEMBER 31,****ASSETS**

	HISTORY 2017	HISTORY 2018	HISTORY 2019	HISTORY 2020	HISTORY 2021	HISTORY 2022
Cash and Equivalents	1,074,954	1,119,744	1,166,400	1,215,000	1,350,000	1,500,000
Accounts Receivable	3,435,927	3,272,311	3,621,699	5,769,863	5,301,370	6,164,384
Inventory	3,208,174	2,858,159	2,931,445	1,335,945	1,908,493	2,768,493
<b>Total Current Assets</b>	<b>7,719,055</b>	<b>7,250,215</b>	<b>7,719,544</b>	<b>8,320,808</b>	<b>8,559,863</b>	<b>10,432,877</b>
Fixed Assets	15,000,000	20,400,000	26,400,000	33,400,000	43,400,000	55,400,000
Less: Accumulated Depreciation	(4,500,000)	(8,874,000)	(13,491,000)	(18,369,000)	(23,602,500)	(29,589,300)
<b>Net Fixed Assets</b>	<b>10,500,000</b>	<b>11,526,000</b>	<b>12,909,000</b>	<b>15,031,000</b>	<b>19,797,500</b>	<b>25,810,700</b>
Intangible Assets	650,000	650,000	650,000	650,000	650,000	650,000
<b>Total Other Assets</b>	<b>650,000</b>	<b>650,000</b>	<b>650,000</b>	<b>650,000</b>	<b>650,000</b>	<b>650,000</b>
<b>TOTAL ASSETS</b>	<b>18,869,055</b>	<b>19,426,215</b>	<b>21,278,544</b>	<b>24,001,808</b>	<b>29,007,363</b>	<b>36,893,577</b>

**LIABILITIES & MEMBERS' CAPITAL**

Line of Credit	450,000	800,000	1,300,000	1,000,000	2,500,000	500,000
Current Portion of Long-term Debt	200,000	600,000	725,000	750,000	1,000,000	1,200,000
Accounts Payable	2,730,531	2,717,890	2,699,454	2,674,764	2,590,940	2,540,137
<b>Total Current Liabilities</b>	<b>3,380,531</b>	<b>4,117,890</b>	<b>4,724,454</b>	<b>4,424,764</b>	<b>6,090,940</b>	<b>4,240,137</b>
Long-term Debt, Less Current Portion	500,000	1,520,000	2,595,000	3,945,000	5,945,000	8,345,000
<b>Total Other Liabilities</b>	<b>500,000</b>	<b>1,520,000</b>	<b>2,595,000</b>	<b>3,945,000</b>	<b>5,945,000</b>	<b>8,345,000</b>
<b>TOTAL LIABILITIES</b>	<b>3,880,531</b>	<b>5,637,890</b>	<b>7,319,454</b>	<b>8,369,764</b>	<b>12,035,940</b>	<b>12,585,137</b>
Capital Stock	100	100	100	100	100	100
Additional Paid-in Capital	8,000,000	8,000,000	8,000,000	8,000,000	8,000,000	8,000,000
Retained Earnings	6,988,424	5,788,225	5,958,990	7,631,944	8,971,323	16,308,340
<b>Total Members' Capital</b>	<b>14,988,524</b>	<b>13,788,325</b>	<b>13,959,090</b>	<b>15,632,044</b>	<b>16,971,423</b>	<b>24,308,440</b>
<b>TOTAL LIABILITIES &amp; MEMBERS' CAPITAL</b>	<b>18,869,055</b>	<b>19,426,215</b>	<b>21,278,544</b>	<b>24,001,808</b>	<b>29,007,363</b>	<b>36,893,577</b>

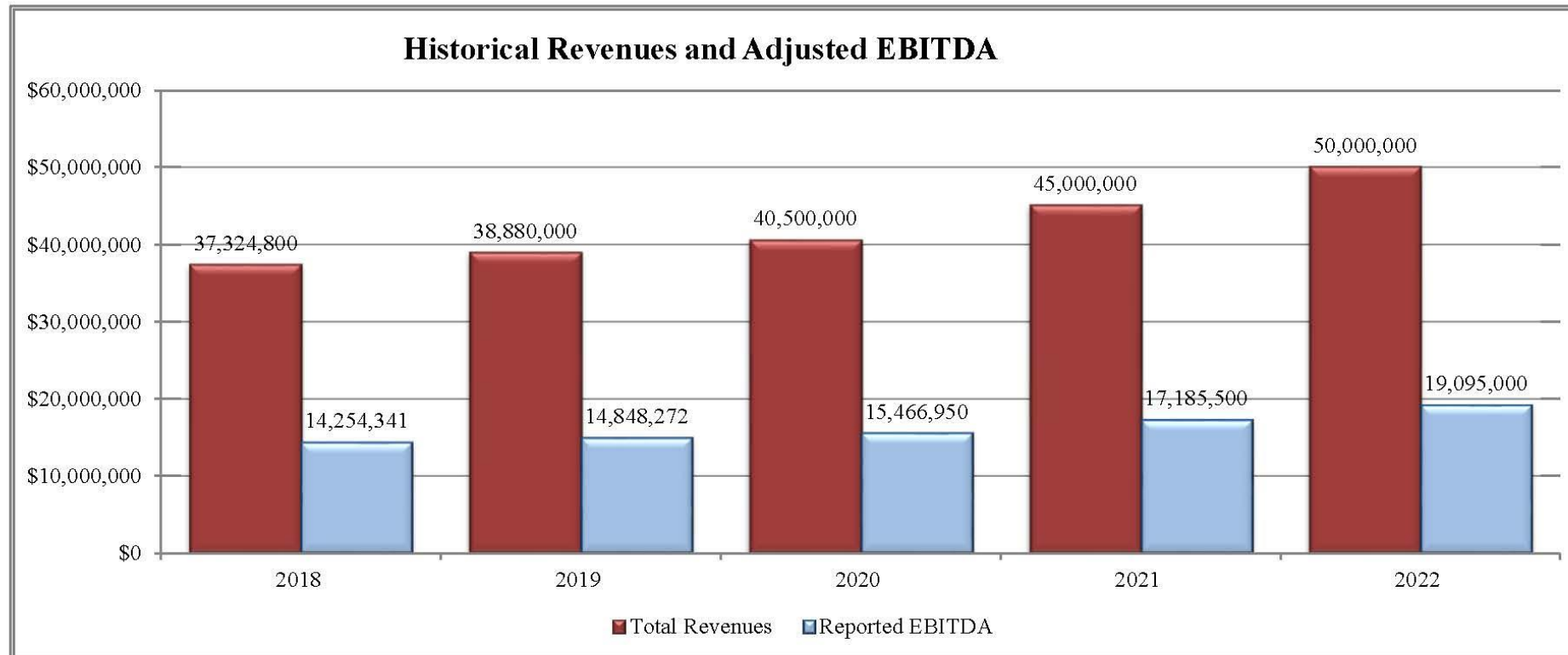
**COMPARATIVE CASH FLOW STATEMENTS****CLOUD DRAGON****FOR THE YEARS ENDED DECEMBER 31,**

	HISTORY 2018	HISTORY 2019	HISTORY 2020	HISTORY 2021	HISTORY 2022
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>					
Net Income	9,821,336	10,116,177	10,429,071	11,659,460	12,540,600
Adjustments to reconcile Net Income to Net Cash					
Provided from Operating Activities					
Depreciation	4,374,000	4,617,000	4,878,000	5,233,500	5,986,800
Amortization	0	0	0	0	0
(Inc.) Dec. in Accounts Receivable	163,616	(349,387)	(2,148,164)	468,493	(863,014)
(Inc.) Dec. in Inventory	350,015	(73,286)	1,595,500	(572,548)	(860,000)
Inc. (Dec.) in Accounts Payable	(12,641)	(18,435)	(24,690)	(83,825)	(50,803)
<b>Net Cash Provided By (Used In) Operating Activities</b>	<b>14,696,325</b>	<b>14,292,068</b>	<b>14,729,717</b>	<b>16,705,081</b>	<b>16,753,584</b>
<b>CASH FLOW FROM INVESTING ACTIVITIES</b>					
Capital Expenditures	(5,400,000)	(6,000,000)	(7,000,000)	(10,000,000)	(12,000,000)
Intangible Assets	0	0	0	0	0
<b>Net Cash Provided By (Used In) Investing Activities</b>	<b>(5,400,000)</b>	<b>(6,000,000)</b>	<b>(7,000,000)</b>	<b>(10,000,000)</b>	<b>(12,000,000)</b>
<b>CASH FLOW FROM FINANCING ACTIVITIES</b>					
Line of Credit	350,000	500,000	(300,000)	1,500,000	(2,000,000)
Long-term Debt	1,620,000	1,800,000	2,100,000	3,000,000	3,600,000
Distributions	(11,221,535)	(10,545,412)	(9,481,117)	(11,070,081)	(6,203,584)
<b>Net Cash Provided By (Used In) Financing Activities</b>	<b>(9,251,535)</b>	<b>(8,245,412)</b>	<b>(7,681,117)</b>	<b>(6,570,081)</b>	<b>(4,603,584)</b>
<b>NET INCREASE (DECREASE) IN CASH</b>	<b>44,790</b>	<b>46,656</b>	<b>48,600</b>	<b>135,000</b>	<b>150,000</b>
Beginning Cash	1,074,954	1,119,744	1,166,400	1,215,000	1,350,000
Ending Cash	1,119,744	1,166,400	1,215,000	1,350,000	1,500,000

## ADJUSTED EBITDA ANALYSIS CLOUD DRAGON

FOR THE YEARS ENDED DECEMBER 31,

	HISTORY 2017	HISTORY 2018	HISTORY 2019	HISTORY 2020	HISTORY 2021	HISTORY 2022
<b>Total Revenues</b>	35,831,808	37,324,800	38,880,000	40,500,000	45,000,000	50,000,000
Reported Operating Income	9,310,167	9,880,341	10,231,272	10,588,950	11,952,000	13,108,200
Plus: Depreciation	0	4,374,000	4,617,000	4,878,000	5,233,500	5,986,800
Plus: Amortization	0	0	0	0	0	0
<b>Reported EBITDA</b>	9,310,167	14,254,341	14,848,272	15,466,950	17,185,500	19,095,000
<b>Note:</b>						
Revenue Growth		4.2%	4.2%	4.2%	11.1%	11.1%
Reported Operating Margin		26.5%	26.3%	26.1%	26.6%	26.2%
Reported EBITDA Margin		38.2%	38.2%	38.2%	38.2%	38.2%

**FINANCIAL STATEMENT ANALYSIS: CHARTS & GRAPHS****CLOUD DRAGON****FOR THE YEARS ENDED DECEMBER 31,**



# Cloud Dragon – Valuation Approaches Used

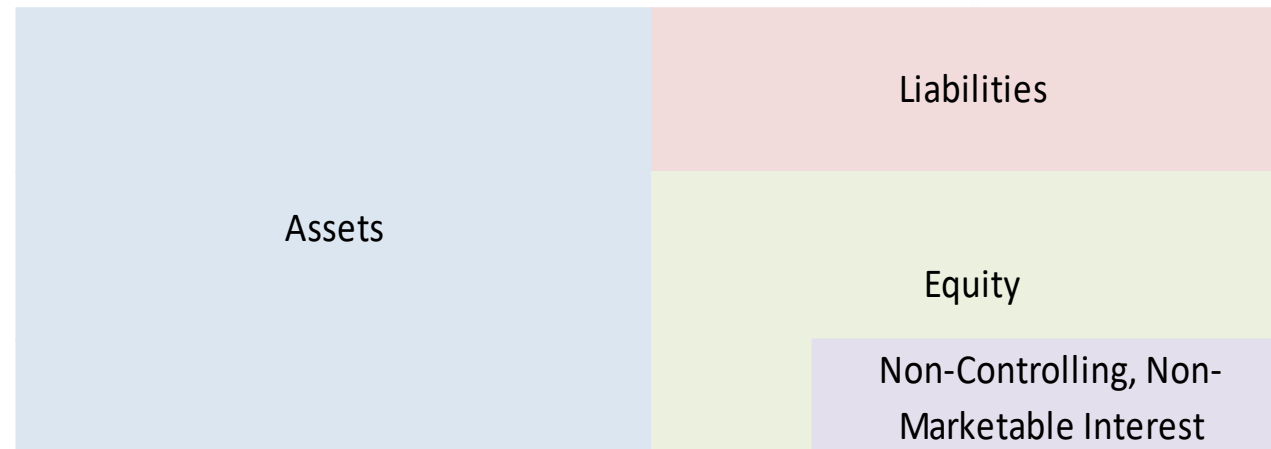
---

- Capitalization of Debt-Free Cash Flow, Controlling Interest (informative only)
- Capitalization of Cash Flow, Minority Interest
- Guideline Company, Minority Interest
  - MVIC to EBTIDA basis
  - MVIC to Revenue
  - MVIC to Book Value
  
- MVIC (Market Value of Invested Capital)



# Cloud Dragon – Levels of Value

- Controlling (marketable)
- Non-controlling, marketable
- Non-controlling, non-marketable



# CAPITALIZATION OF ADJUSTED DEBT-FREE CASH FLOW - CONTROLLING INTEREST BASIS

## CLOUD DRAGON

AS OF OCTOBER 31, 2023

	HISTORY 2018	HISTORY 2019	HISTORY 2020	HISTORY 2021	HISTORY 2022	
Pre-tax Income	9,821,336	10,116,177	10,429,071	11,659,460	12,540,600	
Plus: Interest Expense on Debt	66,138	122,525	167,619	302,800	584,700	
<u>Control Adjustments</u>						
Plus: Actual Officers' Compensation Expense	3,191,270	3,324,240	3,462,750	3,847,500	4,275,000	
Less: Normalized Officers' Compensation Expense	(1,981,108)	(2,082,490)	(2,187,750)	(2,537,500)	(2,745,000)	
Plus: Discretionary Expenses - Yacht Club Membership (in Admin & Other)	30,000	30,000	32,000	35,000	35,000	
Adjusted Debt-Free Pre-tax Income	11,127,638	11,510,452	11,903,690	13,307,260	14,690,300	
<u>Weighting Considerations</u>						
5-Year Straight Line	1	1	1	1	1	\$12,507,868
5-Year Weighted Average	1	2	3	4	5	\$13,102,677
3-Year Straight Line	0	0	1	1	1	\$13,300,417
3-Year Weighted Average	0	0	1	2	3	\$13,764,852
Trailing 12 Months	0	0	0	0	1	\$14,690,300
<b>Selected Debt-Free Income Base</b>						<b>\$14,700,000</b>
Less: City, State & Federal Taxes, Calculated			33.2%			(4,882,181)
Adjusted Debt-Free Net Income						<b>\$9,817,819</b>
Plus: Normalized Depreciation						\$5,986,800
Less: Normalized Capital Expenditures						(6,405,876)
Less: Normalized Working Capital Requirements						(205,605)
<b>Adjusted Free Cash Flow to Total Invested Capital from Operations (Cf)</b>						<b>\$9,193,138</b>
Capitalization Rate (r - g)			13.3%			
Aggregate Total Invested Capital from Operations (Vo) <sup>1</sup>						\$71,194,978
Less: Net Interest-Bearing Debt on Valuation Date						(8,545,000)
<b>Aggregate Marketable Controlling Interest Value of Equity from Operations</b>						<b>\$62,649,978</b>
Add: Premium for Control			5%			3,132,499
<b>Aggregate Marketable Controlling Interest Value of Equity from Operations</b>						<b>\$65,782,477</b>

**Aggregate Value of Equity, Controlling Interest Basis, rounded**
**\$65,800,000**

### Cost of Equity Build-up

20 Year Treasuries at Valuation Date	5.00%
Generic Stock Premium	6.00%
Small Stock Premium	6.30%
Industry/Company Specific Risk	2.00%
Equity Discount Rate, rounded	19.30%

### Cost of Debt

Company's Cost of Debt	6.6%
Tax Rate	33.2%
After-Tax Cost of Debt, rounded	4.40%

### Weighted Average Cost of Capital

Equity	19.30%	80%	15.44%
Debt	4.40%	20%	0.88%
WACC, rounded			16.30%
Less: Long Term Growth Rate			3.00%
Debt-free Capitalization Rate, rounded			13.30%

<sup>1</sup> Gordon Growth Model:  $Vo = [Cf \times (1 + g)] / (r - g)$



# CAPITALIZATION OF ADJUSTED CASH FLOW - MINORITY INTEREST VALUE

## CLOUD DRAGON

AS OF OCTOBER 31, 2023

	HISTORY 2018	HISTORY 2019	HISTORY 2020	HISTORY 2021	HISTORY 2022	
Pre-tax Income	9,821,336	10,116,177	10,429,071	11,659,460	12,540,600	
<u>Normalizing Adjustments/Adjustments for Non-Recurring Items</u>						
Plus: Non-Employee Family Salaries	188,000	210,000	210,000	210,000	210,000	
Adjusted Pre-tax Income	10,009,336	10,326,177	10,639,071	11,869,460	12,750,600	
<u>Weighting Considerations</u>						
5-Year Straight Line	1	1	1	1	1	\$11,118,929
5-Year Weighted Average	1	2	3	4	5	\$11,587,316
3-Year Straight Line	0	0	1	1	1	\$11,753,044
3-Year Weighted Average	0	0	1	2	3	\$12,104,965
Trailing 12 Months	0	0	0	0	1	\$12,750,600
<b>Selected Pre-Tax Income Base</b>						<b>\$12,750,000</b>
Less: City, State & Fed. Taxes, Calculated			33.2%			(4,234,545)
<b>Average Adjusted Net Income</b>						<b>\$8,515,455</b>
Plus: Normalized Depreciation						\$5,986,800
Less: Normalized Capital Expenditures						(6,405,876)
Less: Normalized Working Capital Requirements (from Exhibit G)						(205,605)
<b>Adjusted Free Cash Flow to Equity from Operations (Cf)</b>						<b>\$7,890,774</b>
Capitalization Rate (r - g)			16.3%			
<b>Aggregate Fully Marketable Minority Interest Equity Value from Operations (C-Corp Equivalent) (Vo)<sup>1</sup></b>						<b>\$48,409,656</b>
Pass Through Premium			15%			7,261,448
<b>Aggregate Fully Marketable Minority Interest Equity Value from Operations</b>						<b>\$55,671,105</b>
<b>Value of Cloud Dragon, on an Aggregate Minority Interest Basis, rounded</b>						<b>\$55,700,000</b>

### Cost of Equity Build-up

20 Year Treasuries at Valuation Date	5.00%
Generic Stock Premium	6.00%
Small Stock Premium	6.30%
Industry/Company Specific Risk	2.00%
Discount Rate, rounded (r)	19.30%
Less: Long Term Growth Rate (g)	3.00%
Capitalization Rate, rounded (r - g)	16.30%

<sup>1</sup> Gordon Growth Model:  $Vo = [Cf \times (1 + g)] / (r - g)$

**DETERMINATION OF MAXIMUM POTENTIAL PASS-THROUGH ADJUSTMENT**  
**CLOUD DRAGON**  
**AS OF OCTOBER 31, 2023**

	C-CORP	PASS-THROUGH NO DEDUCTION	PASS-THROUGH 20% DEDUCTION
<b>Pre-Tax Income</b>	<b>\$100.00</b>	<b>\$100.00</b>	<b>\$100.00</b>
<b>Corporate Level Taxes:</b>			
Federal Corporate Tax Rate	21.00%	N/A	N/A
State (NY) Corporate Tax Rate	7.25%	N/A	N/A
City (NYC) Corporate Tax Rate	8.85%	8.85%	8.85%
Net Income Available for Distribution	<b>\$66.79</b>	<b>\$91.15</b>	<b>\$91.15</b>
<b>Investor Level Taxes:</b>			
Pass-Through Income Deduction	N/A	0.00%	20.00%
Federal Income Tax - Personal	N/A	37.00%	37.00%
State (NY) Income Tax Rate - Personal	N/A	8.82%	8.82%
City (NYC) Income Tax Rate - Personal	N/A	N/A	N/A
<b>Net Income for Distribution</b>	<b>\$66.79</b>	<b>\$49.39</b>	<b>\$56.13</b>
City (NYC) Dividend Tax	3.876%	3.876%	3.876%
State (NY) Dividend Tax	8.82%	N/A	N/A
Federal Dividend Tax	20.00%	N/A	N/A
<b>Net Income</b>	<b>\$45.18</b>	<b>\$47.47</b>	<b>\$53.95</b>
<b>Maximum Pass-Through Adjustment</b>		<b>5.1%</b>	<b>19.4%</b>

# GUIDELINE COMPANY VALUATION MEASURES

## CLOUD DRAGON

AS OF OCTOBER 31, 2023

### EBITDA BASIS <sup>(1)</sup>

	Latest	Aggregate	Weighted Average EBITDA			5-Year	MVIC / Weighted Average EBITDA		
Company	Quarter End	MVIC <sup>(2)</sup>	5 Year	3 Year	TTM	CAGR	5 Year	3 Year	TTM
(\$ in millions)									
ACM Research, Inc.	06/30/23	\$897.836	\$146.767	\$168.552	\$215.610	117%	6.1	5.3	4.2
Alpha and Omega Semiconductor Limited	06/30/23	\$710.373	\$254.359	\$202.797	\$174.146	3%	2.8	3.5	4.1
Amtech Systems, Inc.	06/30/23	\$116.801	\$14.963	\$14.777	\$13.560	7%	7.8	7.9	8.6
Applied Materials, Inc.	07/30/23	\$115,382.112	\$22,327.600	\$22,269.150	\$23,539.600	14%	5.2	5.2	4.9
Axcelis Technologies, Inc.	06/30/23	\$4,975.368	\$508.083	\$558.219	\$639.596	33%	9.8	8.9	7.8
AXT, Inc.	06/30/23	\$116.002	\$44.342	\$42.121	\$19.866	11%	2.6	2.8	5.8
Diodes Incorporated	06/30/23	\$3,419.371	\$1,316.703	\$1,335.832	\$1,418.055	25%	2.6	2.6	2.4
GLOBALFOUNDRIES Inc.	06/30/23	\$32,156.042	\$6,333.902	\$6,763.650	\$7,455.467	N/A	5.1	4.8	4.3
MKS Instruments, Inc.	06/30/23	\$10,152.306	\$2,303.180	\$2,254.050	\$2,287.600	12%	4.4	4.5	4.4
Maximum		\$115,382.112	\$22,327.600	\$22,269.150	\$23,539.600	117%	9.8	8.9	8.6
Minimum		\$116.002	\$14.963	\$14.777	\$13.560	3%	2.6	2.6	2.4
Average		\$18,658.468	\$3,694.433	\$3,734.350	\$3,973.722	28%	5.2	5.0	5.2
Median		\$3,419.371	\$508.083	\$558.219	\$639.596	13%	5.1	4.8	4.4

### Valuation Conclusion

#### Cloud Dragon

Multiplied by a Factor of:

Aggregate Market Value of Invested Capital

Less: Outstanding Interest Bearing Debt

Plus: Cash

Aggregate Marketable Minority Interest Equity Value

Weighted Average EBITDA		
5 Year	3 Year	TTM
\$16.971	\$17.854	\$19.095
4.3	4.0	3.8
<b>\$73.236</b>	<b>\$72.149</b>	<b>\$72.032</b>
(\$10.045)	(\$10.045)	(\$10.045)
\$1.500	\$1.500	\$1.500
<b>\$64.691</b>	<b>\$63.604</b>	<b>\$63.487</b>

Aggregate Marketable Minority Interest Equity Value

\$64.691 \$63.604 \$63.487

(1) EBITDA = adjusted earnings before net interest, taxes, depreciation and amortization.

(2) MVIC = market value of invested capital (i.e., market value of equity + total debt - cash).

## GUIDELINE COMPANY VALUATION MEASURES

## CLOUD DRAGON

AS OF OCTOBER 31, 2023

## MVIC TO REVENUE AND MVIC TO BOOK VALUE OF INVESTED CAPITAL

Company	Latest Quarter End	MVIC <sup>(1)</sup>	TTM Revenue	BVIC <sup>(2)</sup>	Implied Multiples	
					MVIC to TTM Rev.	MVIC to Latest BVIC
(\$ in millions)						
ACM Research, Inc.	06/30/23	\$897.836	\$461.084	\$503.082	1.95	1.78
Alpha and Omega Semiconductor Limited	06/30/23	\$710.373	\$691.321	\$767.535	1.03	0.93
Amtech Systems, Inc.	06/30/23	\$116.801	\$117.923	\$107.553	0.99	1.09
Applied Materials, Inc.	07/30/23	\$115,382.112	\$26,543.000	\$14,657.000	4.35	7.87
Axcelis Technologies, Inc.	06/30/23	\$4,975.368	\$1,023.216	\$368.518	4.86	13.50
AXT, Inc.	06/30/23	\$116.002	\$99.978	\$219.719	1.16	0.53
Diodes Incorporated	06/30/23	\$3,419.371	\$1,951.878	\$1,460.037	1.75	2.34
GLOBALFOUNDRIES Inc.	06/30/23	\$32,156.042	\$7,861.000	\$10,525.000	4.09	3.06
MKS Instruments, Inc.	06/30/23	\$10,152.306	\$3,837.000	\$6,861.000	2.65	1.48
Maximum			\$26,543.000	\$14,657.000	4.86	13.50
Minimum			\$99.978	\$107.553	0.99	0.53
Average			\$4,731.822	\$3,941.049	2.54	3.62
Median			\$1,023.216	\$767.535	1.95	1.78
<b>Valuation Conclusion</b>					<b>TTM Revenue</b>	<b>Latest BVIC</b>
<b>Cloud Dragon</b>					\$50.000	\$36.894
Then, Multiplied by a factor of					1.66	1.52
<b>Aggregate Market Value of Invested Capital</b>					<b>\$82.757</b>	<b>\$55.966</b>
Less: Outstanding Interest Bearing Debt					(\$10.045)	(\$10.045)
Plus: Cash					\$1.500	\$1.500
<b>Aggregate Marketable Minority Equity Value</b>					<b>\$74.212</b>	<b>\$47.421</b>
<b>Aggregate Marketable Minority Equity Value</b>					<b>\$74.212</b>	<b>\$47.421</b>

(1) MVIC = market value of invested capital (i.e., market value of equity + total debt - cash).

(2) BVIC = book value of invested capital (i.e., book value of equity + total debt - cash).

## CONCLUSION OF VALUE

## CONCLUSION OF VALUE

## CLOUD DRAGON

AS OF OCTOBER 31, 2023

Valuation Method	Aggregate Fully Marketable Value of <u>Equity</u>		Exhibit	Weighting	Weighted FMV
	Controlling	Non-Controlling			
Income Approaches					
Capitalization Of Adjusted Debt-Free Cash Flow - Controlling Interest Basis	\$65,800,000		Exhibit E-1	N/A	N/A
Capitalization Of Adjusted Cash Flow - Minority Interest Value		\$55,700,000	Exhibit E-2	50.0%	\$27,850,000
Market Approaches					
MVIC to EBITDA (5 Year)		\$64,700,000	Exhibit F	5.0%	\$3,235,000
MVIC to EBITDA (3 Year)		\$63,600,000	Exhibit F	5.0%	\$3,180,000
MVIC to EBITDA (TTM)		\$63,500,000	Exhibit F	20.0%	\$12,700,000
MVIC to Revenue (TTM)		\$74,200,000	Exhibit F	10.0%	\$7,420,000
MVIC to Book Value		\$47,400,000	Exhibit F	10.0%	\$4,740,000
				100%	\$59,125,000
			Discount for Lack of Marketability	30%	<u>-\$17,737,500</u>

Fair Market Value of Cloud Dragon's Equity on Aggregate Minority Interest Basis, rounded

**\$41,387,500**

Valuation Exercise for Conversion to C-Corp

FMV of Equity	\$41,387,500 as provided above
Plus Net Debt	\$7,045,000 Exhibit B-2
<b>FMV of Cloud Dragon on Enterprise Basis</b>	<b><u>\$48,432,500</u></b>

# Discount for Lack of Marketability (DLOM)

---

- What effort and/or costs would be required to convert the subject interest into cash or liquidity?
- Very difficult to Quantify
- Restricted Stock Studies (RSS) are often used as the basis (medians ranging between 15%-35% for one- and two-year holding periods)
  - Factors impacting discount in the RSS (Very Strong Relationships)
    - Volatility
    - Block Size
    - Dividends
    - Profitability (only a Strong Relationship)

## DLOM (continued)

---

- Qualitative factors that Empire considers:
  - Level of Distributions
  - Information Access and Reliability
  - Transfer/Withdrawal Restrictions
  - Put Option Rights
  - Expected Holding Period
  - Historical Trading Activity
  
- Synthetic Put Option as a proxy DLDM





# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

---

## ■ Addresses

- Tax affecting in tax pass-through entities
- Assumptions regarding liquidation value of companies for minority interests
- Importance of relevant Guideline Companies and Transactions

## ■ Background

- TBC's (The Biltmore Company's) owners (William & Mary Cecil) gifted 1 Voting and various Non-Voting shares to each of their children & trusts.
- TBC is an S-Corp
- In 709 filing, each reported gift was valued at \$10.4MM (or \$20.9MM combined) in 2010
- IRS initially suggested TBC should be valued on Asset Approach (indicating \$140MM gift)



# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

---

- Trial
  - IRS expert used 2 approaches, Asset (\$92MM) & Income (\$36MM)
  - Because TBC is an S corporation, the IRS expert believed it was appropriate to tax-affect the future earnings and apply a pass-through adjustment, which resulted in a 17.6 percent valuation premium for the Company
  - IRS expert weighted the Income Approach more heavily
  - IRS expert used DLOMs of 19%, 22% and 27% for the Class A, and smaller & larger Class B stock



# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

## ■ Trial

- Taxpayer had two experts each using Income and Guideline Approaches
- 1<sup>st</sup> Expert applied:
  - Valuation multiples based on Size, Growth, & Liquidity from 5 Guideline Companies, then 15% lack of diversification discount and 30% DLOM
  - EBITDA multiples from 6 Guideline Transactions, then 20% DLOC and 30% DLOM
  - 15% Discount Rate and 30% DLOM to Income Approach (DCF) but did not tax affect
  - During testimony, agreed that Tax-Affecting would be appropriate, but did not apply a pass-through adjustment
- 2<sup>nd</sup> Expert applied:
  - MVIC to EBITDA, but only 1 Guideline Company, then a 25% DLOM and 2% DLOV
  - 10.7% Cap Rate and 25% DLOM to Income Approach (Earnings Cap), did tax affect and applied an adjustment

# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

## ■ The Court's Opinion

### ■ Three key valuation issues

- the tax-affecting of the S corporation earnings and the use of an adjustment
- the appropriate application of the asset liquidation assumption when valuing a noncontrolling interest in a company, and
- the selection of comparable companies and similar

### ■ Tax affecting, not the first time the Court has evaluated such analysis

### ■ In *Gross v. Commissioner* and *Wall v. Commissioner*, the Court completely disallowed the use of tax-affecting

### ■ Precedent shifted in *Jones v. Commissioner* in which tax affecting was conditionally accepted

### ■ In *Cecil*, however, the Court accepted the tax-affecting of an S corporation's earnings because the valuation experts retained by both sides agreed that the analyses were necessary





# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

---

- The Court's Opinion (continued)
  
- Appropriate Application of the Asset Liquidation Assumption
  - The valuation experts should consider the possibility of liquidation when applying an asset-based approach to value a noncontrolling interest,
  - The IRS initially valued TBC under the asset liquidation assumption
  - The Court decided that the liquidation of TBC was unlikely given the minority interest of the new owners



# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

---

- The Court's Opinion (continued)
  
- The Selection of Comparable Companies and Similar Transactions
  - The Court believed the Cecils' experts did not sufficiently identify comparable companies or similar transactions when valuing TBC
  - Court's main fault with the second Cecil expert's GPTC method was the use of a single company/transaction to calculate valuation multiples
  - The first Cecil expert used more than one company and transaction in his GPTC and similar transactions methods, but the Court still faulted his methodology
    - Pairi Daiza SA "operates a park which houses thousands of animals, and it does so at a location (in Belgium)
    - Premier Exhibitions, Inc. "presents museum exhibitions outside the hospitality industry and does that worldwide while TBC's operation is limited to a single city
    - Transactions: two of which occurred during the great Recession, and were deemed irrelevant





# Cecil v Commissioner (T.C. Memo 2023-24), 2/28/2023

---

- The Court's Final Decision
  
- The Court ultimately accepted
  - The 1<sup>st</sup> Expert's price per share valuation, before tax affecting and application of any discounts
  - The 1<sup>st</sup> Experts 20% DLOC
  - The IRS's DLOM discounts ranging from 19% to 27%

# Nathan Schroeder

---



Nathan is a senior manager for Empire Valuation Consultants where he has worked since 2008.

He has over 15 years of experience with business, financial asset and carried interest valuations. Prior to that he was in corporate finance and banking and trust administration areas.

Nathan manages and performs complex valuation engagements involving various classes of equity and debt. Representative industries alternative asset management, traditional asset management and investment advisory, real estate, technology and biotech start-ups, and a variety of manufacturing and service businesses

Nathan specializes in the valuation of carried interests in private equity and hedge funds, and has extensive experience in the valuation of limited partnership interests in such funds. Nathan has performed valuations of derivative instruments, intangible assets, and equity and debt interests for diverse purposes, including those of tax planning and reporting, lending purposes, and other corporate planning and reporting purposes.



# **18<sup>th</sup> ANNUAL INTERGENERATIONAL ESTATE PLANNING CONFERENCE**

## **COFFEE BREAK & NETWORKING**

**Our Program Resumes in 15 minutes.**



# Remarks from Our Breakfast Sponsor

Frank Melia, Division Manager  
Contour Mortgage  
[fmelia@contourmtg.com](mailto:fmelia@contourmtg.com)



# Corporate Planning

Theresa Skaine, Esq., Of Counsel  
Pierro, Connor & Strauss, LLC



# Ownership of Cloud Dragon, Inc.

- ▶ Cloud Dragon is an S-Corp with one class of stock.
- ▶ The shares of the Company are owned 94% by Kai and 3% each by Melvin and Maria.
- ▶ Melvin and Maria both wish to continue to own and operate the business together 50/50.
- ▶ Maria is advocating for a 51/49% split to allow Cloud Dragon to become a certified WBE in order to market to large scale companies.
- ▶ Jade does not wish to step into management of Cloud Dragon.
- ▶ Michael does not wish to own any of the stock of the Company or engage in any management.



# Management Succession

- ▶ Given Kai's decline, Melvin and Maria wish to become directors and officers of Cloud Dragon immediately.
- ▶ As guardians, they can act to vote his shares of the Company to elect themselves as directors.
- ▶ The directors then elect the officers of the Company with Maria being President/CEO and Secretary and Melvin acting as VP and Treasurer.



# Transfer of Shares of Cloud Dragon

- ▶ In order to facilitate planning and gifting, a restructure of the Corporation can occur to create voting and non-voting shares.
- ▶ Kai's 94% ownership is converted into 94 voting and 940 non-voting shares.
- ▶ Melvin and Maria each retain their 3% of voting shares and each gain 30 non-voting shares.



# Transfer Continued

- ▶ Kai retains the non-voting shares which carry a distribution right, so he receives distributions of profit from the Company every year.
- ▶ These non-voting shares are gifted by the guardians into two SLATs for the benefit of Kai and Jade.
- ▶ The voting shares are gifted to Melvin and Maria so they own 100% of the voting shares.

# Cloud Dragon After Transfer

- ▶ Create buy-sell agreement between Maria and Melvin
- ▶ Prevent either party from selling to outside third-parties without consent
  - ▶ CAVEAT – Maria has drag-along rights
- ▶ Upon either's death, Cloud Dragon will purchase their shares
- ▶ Use of life insurance
- ▶ Valuation of Company to be determined by 5 year rolling average of net revenue for buy-sell purposes
- ▶ Maria to have ultimate control if Cloud Dragon will apply for WBE certification – no deadlock provision needed

# Commercial Building

- ▶ Building was purchased in Kai and Jade's names.
- ▶ Transfer ownership of building to newly formed LLC
- ▶ Lease between new LLC and tenants to generate funds in LLC and to separate liability of real estate company





# Life Insurance Overview

November 8, 2023

Presented by: Gary Sancilio



# Buying Life Insurance:

- Identify need, Insured and Owner of policy
- Determine amount
- Choose suitable product (Term, Permanent or Hybrid)
- Choose financially strong insurance company
- Conversion Options

# Possible Insurance Needs

Kai (78) and Jade (67)

Three Children

- Child 1 (Melvin) and Child 2 (Maria) – in the business – Key Employees
    - Current Term Policies \$2.5m each
  - Child 3 (Michael) – Not in business
- 
- ✓ Significant Wealth
  - ✓ Potential estate tax issues
  - ✓ Valuable business
  - ✓ Liquid/Illiquid estate
  - ✓ Jade – Estate Tax – Estate equalization
  - ✓ Child 1 and Child 2 – Key person, Buy Sell, deferred compensation, Family Planning, Potential Estate Tax
  - ✓ Child 3 – Estate equalization (Equal vs. Equitable)

# Possible Insurance Needs/Life Insurance Ideas

## Kai (78) and Jade (67)

- Estate Value of approximately \$60m
- Estate tax liability                \$15-20m – assume \$12 million federal exemption  
   \$20-25m – assume \$6 million federal exemption
- Immediate Liquidity Needs

### Term Insurance

- ✓ \$10-15 million
- ✓ 10–20-year term
- ✓ Check conversion option

### Guaranteed UL

- ✓ No cash value
- ✓ Lifetime premiums
- ✓ Guaranteed death benefit

### Survivorship Policy

# **Potential Estate Tax Liability After Death Jade and Kai (\$6 million each exemption) (assume death after 2025)**

- Term Conversion for Kai of \$5m
- Fund UL policy for \$5m
- 3 children are beneficiary of Irrevocable Trust
- Buy \$10m Term or ULG for Jade
- Cost of term relatively inexpensive, approximately \$60k per year
- Potential to get \$20m out of their estate

# Kai's Existing Insurance

- \$5m - 10 year term – 2 years left to convert
- \$5m - Universal Life Policy – underfunded and at risk of lapsing
- Keep every bit of Kai's insurance regardless of cost
  - How do we get it
  - How do we pay for it

# ULG – Male - 78

Values shown do not reflect loans and/or withdrawals.

Year	Age End Year	Annual Premium Outlay*	1.00% Guaranteed Interest Rate		
			Account Value End Year	Net Surrender Value End Year	Death Benefit End Year
1	79	312,228	4,995	0	5,000,000
2	80	312,228	0	0	5,000,000
3	81	312,228	0	0	5,000,000
4	82	312,228	0	0	5,000,000
5	83	312,228	0	0	5,000,000
6	84	312,228	0	0	5,000,000
7	85	312,228	0	0	5,000,000
8	86	312,228	0	0	5,000,000
9	87	312,228	0	0	5,000,000
10	88	312,228	0	0	5,000,000
11	89	312,228	0	0	5,000,000
12	90	312,228	0	0	5,000,000
13	91	312,228	0	0	5,000,000
14	92	312,228	0	0	5,000,000
15	93	312,228	0	0	5,000,000
16	94	312,228	0	0	5,000,000
17	95	312,228	0	0	5,000,000
18	96	312,228	0	0	5,000,000
19	97	312,228	0	0	5,000,000
20	98	312,228	0	0	5,000,000
21	99	312,228	0	0	5,000,000
22	100	312,228	0	0	5,000,000
23	101	0	0	0	5,000,000
24	102	0	0	0	5,000,000
25	103	0	0	0	5,000,000



# Kai's Current UL Policy

Death Benefit	\$5m
Current Cash Value	\$463,610
Planned Premium*	\$153,000
Required Premium**	\$332,000

\* Projected to Lapse in 1 year

\*\* Projected to remain in force 8 years



# 15 Year Term – Female - 67

## Tabular Values

Guaranteed Values					
Year	Age End Year	Annual Premium for Basic Policy	Total Annual Premium	Cumulative Total Annual Premium	Total Death Benefit End Year
1	68	62,375	62,375	62,375	10,000,000
2	69	62,375	62,375	124,750	10,000,000
3	70	62,375	62,375	187,125	10,000,000
4	71	62,375	62,375	249,500	10,000,000
5	72	62,375	62,375	311,875	10,000,000
6	73	62,375	62,375	374,250	10,000,000
7	74	62,375	62,375	436,625	10,000,000
8	75	62,375	62,375	499,000	10,000,000
9	76	62,375	62,375	561,375	10,000,000
10	77	62,375	62,375	623,750	10,000,000
11	78	62,375	62,375	686,125	10,000,000
12	79	62,375	62,375	748,500	10,000,000
13	80	62,375	62,375	810,875	10,000,000
14	81	62,375	62,375	873,250	10,000,000
15	82	62,375	62,375	935,625	10,000,000
16	83	1,214,475	1,214,475	2,150,100	10,000,000
17	84	1,368,975	1,368,975	3,519,075	10,000,000
18	85	1,554,675	1,554,675	5,073,750	10,000,000
19	86	1,839,375	1,839,375	6,913,125	10,000,000
20	87	2,091,975	2,091,975	9,005,100	10,000,000

# ULG – Female - 67

Values shown do not reflect loans and/or withdrawals.

Year	Age End Year	Annual Premium Outlay*	1.00% Guaranteed Interest Rate		
			Account Value End Year	Net Surrender Value End Year	Death Benefit End Year
1	68	294,727	146,209	0	10,000,000
2	69	294,727	288,662	0	10,000,000
3	70	294,727	426,617	54,779	10,000,000
4	71	294,727	559,156	208,688	10,000,000
5	72	294,727	684,909	360,085	10,000,000
6	73	294,727	802,246	498,792	10,000,000
7	74	294,727	909,543	623,185	10,000,000
8	75	294,727	1,004,894	739,906	10,000,000
9	76	294,727	1,085,999	838,107	10,000,000
10	77	294,727	1,150,580	915,510	10,000,000
11	78	294,727	1,195,366	985,940	10,000,000
12	79	294,727	1,216,462	1,028,406	10,000,000
13	80	294,727	1,208,359	1,041,673	10,000,000
14	81	294,727	1,163,477	1,022,435	10,000,000
15	82	294,727	1,074,209	954,537	10,000,000
16	83	294,727	938,171	844,143	10,000,000
17	84	294,727	747,677	675,019	10,000,000
18	85	294,727	487,765	440,751	10,000,000
19	86	294,727	118,293	96,923	10,000,000
20	87	294,727	0	0	10,000,000
21	88	294,727	0	0	10,000,000
22	89	294,727	0	0	10,000,000
23	90	294,727	0	0	10,000,000
24	91	294,727	0	0	10,000,000
25	92	294,727	0	0	10,000,000

# Whole Life w/ LISR – Female 67

Year	Age End Year	Annual Net Outlay	Cumulative Net Outlay	Net Cash Value End Year	Net Annual Cash Value Increase	Net Death Benefit Beg Year
1	68	302,852	302,852	29,729	29,729	10,000,000
2	69	302,852	605,704	132,657	102,927	10,000,000
3	70	302,852	908,556	365,142	232,485	10,000,000
4	71	302,852	1,211,408	607,603	242,462	10,000,000
5	72	302,852	1,514,260	858,582	250,979	10,000,000
6	73	302,852	1,817,112	1,116,700	258,119	10,000,000
7	74	302,852	2,119,964	1,384,868	268,168	10,000,000
8	75	302,852	2,422,816	1,662,463	277,594	10,000,000
9	76	302,852	2,725,668	1,948,386	285,924	10,000,000
10	77	302,852	3,028,520	2,241,471	293,085	10,000,000
11	78	302,852	3,331,372	2,543,663	302,193	10,000,000
12	79	302,852	3,634,224	2,854,621	310,957	10,000,000
13	80	302,852	3,937,075	3,175,138	320,517	10,000,000
14	81	302,852	4,239,927	3,501,813	326,675	10,000,000
15	82	302,852	4,542,779	3,830,643	328,830	10,000,000
16	83	302,852	4,845,631	4,159,450	328,807	10,000,000
17	84	302,852	5,148,483	4,484,938	325,488	10,000,000
18	85	302,852	5,451,335	4,814,918	329,980	10,000,000
19	86	302,852	5,754,187	5,139,059	324,141	10,000,000
20	87	302,852	6,057,039	5,464,112	325,052	10,000,000
21	88	302,852	6,359,891	5,771,829	307,717	10,000,000
22	89	302,852	6,662,743	6,071,643	299,814	10,000,000
23	90	302,852	6,965,595	6,363,622	291,979	10,000,000
24	91	302,852	7,268,447	6,648,909	285,287	10,000,000
25	92	302,852	7,571,299	6,930,436	281,527	10,000,000

# Pre-fund Estate Tax

Kai/Jade



Insured

\$10,000,000



LIFE INSURANCE  
TRUST

Life Insurance\*

- Transfer to Trust
- Potential Gift Tax
- Three year look back
- Estate equalization for Child 3
- Potential income and estate tax free

# Potential Buy/Sell Agreement

- Insured – Melvin and Maria
- They split partial ownership of company
- Agreement that children will use life insurance proceeds to buy the deceased sibling's ownership (Child 1 and Child 2)
- Buyout price will be based upon valuation
- Surviving sibling becomes 100% Owner after buyout of other sibling's interest



# Buyout of Sibling's Business Ownership

- Protect own estate and tax liability
- Retirement Planning
- Include Illustration for siblings
  - 2.5m each - term

## Permanent Insurance

- Lifetime death benefit
- Cash value accumulation
- Guaranteed Death Benefit, premiums and cash value
- Income tax advantages
- FLEXIBILITY

# Whole Life L100 - \$2.5m Death Benefit

The following information is a general summary of the values of the whole life policy being illustrated and reflect non-guaranteed values. You should review the policy's Basic Illustration for greater detail about the product's guarantees, features, and values.

Year	Age End Year	Annual Net Outlay	Cumulative Net Outlay	Net Cash Value End Year	Net Annual Cash Value Increase	Net Death Benefit End Year
1	43	36,000	36,000	0	0	2,500,000
2	44	36,000	72,000	1,525	1,525	2,506,029
3	45	36,000	108,000	25,826	24,301	2,512,245
4	46	36,000	144,000	58,035	32,209	2,518,451
5	47	36,000	180,000	91,458	33,422	2,525,185
6	48	36,000	216,000	126,206	34,749	2,532,859
7	49	36,000	252,000	163,250	37,044	2,544,532
8	50	36,000	288,000	202,581	39,331	2,559,687
9	51	36,000	324,000	244,313	41,732	2,578,242
10	52	36,000	360,000	288,512	44,199	2,600,035
11	53	36,000	396,000	336,299	47,787	2,628,015
12	54	36,000	432,000	387,825	51,526	2,661,908
13	55	36,000	468,000	443,247	55,422	2,701,455
14	56	36,000	504,000	502,730	59,483	2,746,629
15	57	36,000	540,000	566,509	63,779	2,797,307
16	58	36,000	576,000	633,535	67,027	2,850,305
17	59	36,000	612,000	703,645	70,110	2,904,963
18	60	36,000	648,000	777,029	73,383	2,961,445
19	61	36,000	684,000	853,737	76,708	3,019,838
20	62	36,000	720,000	933,906	80,170	3,080,124
21	63	36,000	756,000	1,015,673	81,767	3,143,946
22	64	36,000	792,000	1,101,684	86,011	3,211,218
23	65	36,000	828,000	1,192,136	90,452	3,282,007
24	66	36,000	864,000	1,287,192	95,056	3,356,511
25	67	36,000	900,000	1,387,058	99,866	3,434,793

# Whole Life L100 - \$2.5m Death Benefit

Year	Age End Year	Annual Net Outlay	Cumulative Net Outlay	Net Cash Value End Year	Net Annual Cash Value Increase	Net Death Benefit End Year
26	68	36,000	936,000	1,491,948	104,890	3,516,903
27	69	36,000	972,000	1,602,034	110,086	3,603,037
28	70	36,000	1,008,000	1,717,638	115,604	3,693,325
29	71	36,000	1,044,000	1,838,799	121,161	3,787,685
30	72	36,000	1,080,000	1,965,761	126,962	3,886,036
31	73	36,000	1,116,000	2,098,340	132,579	3,987,908
32	74	36,000	1,152,000	2,236,821	138,481	4,093,423
33	75	36,000	1,188,000	2,381,171	144,350	4,202,406
34	76	36,000	1,224,000	2,531,565	150,394	4,315,036
35	77	36,000	1,260,000	2,688,035	156,470	4,431,286
36	78	36,000	1,296,000	2,850,534	162,499	4,551,230
37	79	36,000	1,332,000	3,019,055	168,521	4,674,714
38	80	36,000	1,368,000	3,193,410	174,356	4,801,572
39	81	36,000	1,404,000	3,373,370	179,959	4,931,508
40	82	36,000	1,440,000	3,558,566	185,196	5,064,907
41	83	36,000	1,476,000	3,748,237	189,671	5,201,019
42	84	36,000	1,512,000	3,943,533	195,296	5,341,656
43	85	36,000	1,548,000	4,143,885	200,352	5,486,698
44	86	36,000	1,584,000	4,346,958	203,074	5,633,663
45	87	36,000	1,620,000	4,554,117	207,159	5,785,067
46	88	36,000	1,656,000	4,764,949	210,831	5,940,287
47	89	36,000	1,692,000	4,978,963	214,014	6,098,851
48	90	36,000	1,728,000	5,196,044	217,081	6,260,618
49	91	36,000	1,764,000	5,416,716	220,671	6,425,763
50	92	36,000	1,800,000	5,641,570	224,855	6,593,874
51	93	36,000	1,836,000	5,869,883	228,313	6,762,916
52	94	36,000	1,872,000	6,104,609	234,726	6,934,356
53	95	36,000	1,908,000	6,348,654	244,045	7,106,852
54	96	36,000	1,944,000	6,605,268	256,615	7,279,092
55	97	36,000	1,980,000	6,876,822	271,554	7,448,855

# Whole Life L100 - \$2.5m Death Benefit

Year	Age End Year	Annual Net Outlay	Cumulative Net Outlay	Net Cash Value End Year	Net Annual Cash Value Increase	Net Death Benefit End Year
56	98	36,000	2,016,000	7,171,691	294,869	7,613,413
57	99	36,000	2,052,000	7,505,093	333,403	7,768,114
58	100	36,000	2,088,000	7,905,451	400,357	7,905,451
59	101	0	2,088,000	8,325,441	419,990	8,325,441
60	102	0	2,088,000	8,768,195	442,754	8,768,195
61	103	0	2,088,000	9,234,946	466,751	9,234,946
62	104	0	2,088,000	9,726,995	492,049	9,726,995
63	105	0	2,088,000	10,245,714	518,718	10,245,714
64	106	0	2,088,000	10,792,546	546,833	10,792,546
65	107	0	2,088,000	11,369,017	576,471	11,369,017
66	108	0	2,088,000	11,976,733	607,716	11,976,733
67	109	0	2,088,000	12,617,387	640,654	12,617,387
68	110	0	2,088,000	13,292,764	675,377	13,292,764
69	111	0	2,088,000	14,004,747	711,983	14,004,747
70	112	0	2,088,000	14,755,319	750,572	14,755,319
71	113	0	2,088,000	15,546,573	791,253	15,546,573
72	114	0	2,088,000	16,380,712	834,139	16,380,712
73	115	0	2,088,000	17,260,062	879,350	17,260,062
74	116	0	2,088,000	18,187,072	927,010	18,187,072
75	117	0	2,088,000	19,164,326	977,254	19,164,326
76	118	0	2,088,000	20,194,548	1,030,221	20,194,548
77	119	0	2,088,000	21,280,607	1,086,059	21,280,607
78	120	0	2,088,000	22,425,531	1,144,924	22,425,531
79	121	0	2,088,000	23,632,510	1,206,979	23,632,510

# Whole Life – 10 Pay - \$2.5m Death Benefit

## Supplemental Values

Non-Guaranteed Values*												
Year	Age End Year	Annual Outlay	Annual Loan	Annual Surrender	Annual Net Outlay	Annual Dividend End Year	Basic Policy Cash Value End Year	Total Cash Value of Additions End Year	Total Outstanding Loan End Year	Net Cash Value End Year	Total Paid-Up Additions End Year	Net Death Benefit End Year
1	43	158,800	0	0	158,800	6,775	52,400	6,775	0	59,175	14,814	2,514,814
2	44	158,800	0	0	158,800	12,462	144,125	19,362	0	163,487	41,569	2,541,569
3	45	158,800	0	0	158,800	18,452	284,075	38,172	0	322,247	80,465	2,580,465
4	46	158,800	0	0	158,800	24,732	426,875	63,608	0	490,483	131,654	2,631,654
5	47	158,800	0	0	158,800	31,417	572,525	96,196	0	668,721	195,504	2,695,504
6	48	158,800	0	0	158,800	36,657	721,075	134,616	0	855,691	268,663	2,768,663
7	49	158,800	0	0	158,800	42,307	872,650	179,384	0	1,052,034	351,582	2,851,582
8	50	158,800	0	0	158,800	48,201	1,027,300	230,851	0	1,258,151	444,363	2,944,363
9	51	158,800	0	0	158,800	54,333	1,185,100	289,370	0	1,474,470	547,085	3,047,085
10	52	158,800	0	0	158,800	60,893	1,346,175	355,482	0	1,701,657	660,171	3,160,171
11	53	0	0	0	0	63,279	1,370,350	425,145	0	1,795,495	775,614	3,275,614
12	54	0	0	0	0	66,761	1,394,850	499,507	0	1,894,357	895,270	3,395,270
13	55	0	0	0	0	70,389	1,419,625	578,768	0	1,998,393	1,019,227	3,519,227
14	56	0	0	0	0	74,245	1,444,675	663,226	0	2,107,901	1,147,708	3,647,708
15	57	0	0	0	0	78,278	1,470,025	753,142	0	2,223,167	1,280,832	3,780,832
16	58	0	0	0	0	82,581	1,495,625	848,839	0	2,344,464	1,418,870	3,918,870
17	59	0	0	0	0	87,134	1,521,475	950,644	0	2,472,119	1,562,044	4,062,044
18	60	0	0	0	0	91,911	1,547,550	1,058,848	0	2,606,398	1,710,523	4,210,523
19	61	0	0	0	0	96,973	1,573,800	1,173,781	0	2,747,581	1,864,565	4,364,565
20	62	0	0	0	0	102,268	1,600,225	1,295,758	0	2,895,983	2,024,337	4,524,337
21	63	0	0	0	0	107,927	1,626,800	1,425,203	0	3,052,003	2,190,194	4,690,194
22	64	0	0	0	0	113,956	1,653,475	1,562,529	0	3,216,004	2,362,492	4,862,492
23	65	0	0	0	0	120,316	1,680,250	1,708,147	0	3,388,397	2,541,507	5,041,507
24	66	-287,342	0	287,342	-287,342	116,667	1,707,050	1,560,134	0	3,267,184	2,284,839	4,784,839
25	67	-287,342	0	287,342	-287,342	112,787	1,733,875	1,405,579	0	3,139,454	2,026,644	4,526,644
26	68	-287,342	0	287,342	-287,342	108,652	1,760,725	1,244,205	0	3,004,930	1,766,608	4,266,608
27	69	-287,342	0	287,342	-287,342	104,263	1,787,525	1,075,690	0	2,863,215	1,504,440	4,004,440
28	70	-287,342	0	287,342	-287,342	99,568	1,814,275	899,713	0	2,713,988	1,239,769	3,739,769
29	71	-287,342	136,055	151,288	-287,342	99,552	1,840,950	858,982	136,055	2,556,679	1,166,492	3,523,240
30	72	-287,342	294,540	0	-287,342	104,992	1,867,550	976,385	430,595	2,390,562	1,307,040	3,353,667

# Whole Life – 10 Pay - \$2.5m Death Benefit

## Supplemental Values

Non-Guaranteed Values*												
Year	Age End Year	Annual Outlay	Annual Loan	Annual Surrender	Annual Net Outlay	Annual Dividend End Year	Basic Policy Cash Value End Year	Total Cash Value of Additions End Year	Total Outstanding Loan End Year	Net Cash Value End Year	Total Paid-Up Additions End Year	Net Death Benefit End Year
31	73	-287,342	310,121	0	-287,342	110,631	1,894,075	1,100,884	740,716	2,215,059	1,453,062	3,173,163
32	74	-287,342	326,526	0	-287,342	116,536	1,920,500	1,232,778	1,067,242	2,029,579	1,604,762	2,981,063
33	75	-287,342	343,800	0	-287,342	122,624	1,946,775	1,372,268	1,411,042	1,833,357	1,762,232	2,776,547
34	76	-287,342	361,987	0	-287,342	129,014	1,972,875	1,519,680	1,773,028	1,625,733	1,925,717	2,558,896
35	77	-287,342	381,136	0	-287,342	135,666	1,998,750	1,675,276	2,154,164	1,405,907	2,095,405	2,327,286
36	78	-287,342	401,298	0	-287,342	142,607	2,024,350	1,839,341	2,555,462	1,173,045	2,271,520	2,080,874
37	79	-287,342	422,526	0	-287,342	149,783	2,049,650	2,012,112	2,977,988	926,238	2,454,214	1,818,690
38	80	-287,342	444,878	0	-287,342	157,071	2,074,575	2,193,651	3,422,866	664,291	2,643,495	1,539,559
39	81	0	181,070	0	0	164,551	2,099,075	2,384,109	3,603,936	688,600	2,839,475	1,544,891
40	82	0	190,648	0	0	172,406	2,123,025	2,583,716	3,794,584	711,424	3,042,494	1,547,177
41	83	0	200,733	0	0	180,780	2,146,325	2,792,852	3,995,317	732,508	3,253,063	1,546,393
42	84	0	211,352	0	0	189,697	2,168,950	3,011,990	4,206,670	751,737	3,471,714	1,542,512
43	85	0	222,533	0	0	198,757	2,190,775	3,241,055	4,429,203	768,323	3,698,526	1,535,018
44	86	0	234,305	0	0	206,933	2,211,750	3,479,018	4,663,507	780,561	3,932,427	1,522,220
45	87	0	246,700	0	0	216,426	2,231,725	3,726,864	4,910,207	788,632	4,174,869	1,504,912
46	88	0	259,750	0	0	226,041	2,250,800	3,984,760	5,169,957	792,112	4,425,937	1,482,490
47	89	0	273,491	0	0	235,626	2,269,000	4,252,607	5,443,448	790,201	4,685,552	1,454,146
48	90	0	287,958	0	0	245,554	2,286,325	4,530,632	5,731,406	782,359	4,954,055	1,419,457
49	91	0	303,191	0	0	255,890	2,302,925	4,819,416	6,034,597	768,514	5,231,842	1,378,015
50	92	0	319,230	0	0	266,474	2,319,000	5,119,531	6,353,828	748,586	5,519,115	1,329,170
51	93	0	336,117	0	0	277,506	2,334,775	5,431,863	6,689,945	722,795	5,816,260	1,272,417
52	94	0	353,898	0	0	288,997	2,350,550	5,757,561	7,043,843	691,649	6,123,632	1,207,169
53	95	0	372,619	0	0	300,289	2,367,050	6,098,266	7,416,462	656,523	6,440,787	1,131,994
54	96	0	392,331	0	0	311,547	2,384,950	6,455,929	7,808,793	619,000	6,767,363	1,045,484
55	97	0	413,085	0	0	322,083	2,404,875	6,831,948	8,221,878	580,007	7,102,186	945,370
56	98	0	434,937	0	0	332,260	2,428,425	7,231,110	8,656,816	544,774	7,444,239	829,477
57	99	0	457,946	0	0	341,195	2,458,425	7,661,636	9,114,761	523,128	7,791,203	694,271
58	100	0	482,171	0	0	347,940	2,500,000	8,139,144	9,596,932	534,534	8,139,144	534,534
59	101	0	507,678	0	0	578,337	2,500,000	8,717,481	10,104,610	578,337	8,717,481	578,337
60	102	0	534,534	0	0	609,394	2,500,000	9,326,875	10,639,144	624,920	9,326,875	624,920



# Whole Life – 10 Pay - \$2.5m Death Benefit

	Retirement Supplement
Initial Death Benefit: \$2,500,000	Initial Premium: \$158,800.00
Owner Tax Bracket: 28%	
Dividend Option(s): Paid-Up Additions	

## Benefit Summary

### Retirement Supplement Using Whole Life Insurance

Initial Premium Payment of \$158,800

\$1,588,000 In Total up to Age 65

Can Provide

#### Pre-Retirement Death Benefits

\$3,395,270 at Age 54

\$5,041,507 at Age 65

#### Supplemental Retirement Income at Age 65

\$287,342 Initial Annual Retirement Income (after-tax)

Cumulative After-Tax Retirement Income of \$4,310,137 is paid over 15 years

#### Death Benefit at End of Specified Retirement Income Period

\$1,539,559 at Age 80

# What is Split Dollar?

Split Dollar is an arrangement for funding a life insurance need where the premiums are paid by one party, and the benefits are shared with a second party.

- Split dollar brings together the party with the need (employee, trust or family member) and the party with the ability to pay
- One party is the premium payor and owns all cash value, or is entitled to repayment of its premiums (loan arrangement)
- The other party is typically entitled to policy benefits in excess of these belonging to the premium payor.

# Economic Benefit Split Dollar (Endorsement)

- Premium payor (Business) owns all policy cash value, and typically receives a death benefit equal to greater of premiums or cash value.
  - Premium payor could receive larger death benefit, such as one-half of total death benefit, for key person benefit purposes.
- Other (benefited) party is entitled to death benefits in excess of premium payor's interest
  - Economic benefit of term value of benefited party's interest treated as compensation (or as a gift with "Private Split Dollar")
- Policy premiums are NOT deductible
- Insured taxed annually on "Economic Benefit" of Insured's share of death benefit (Table 2001 rates)
  - Second-to-die policies (adjusted for two lives)

# Loan Regime Split Dollar

Loan Arrangements (Equity Collateral Assignment):

- Executive, trust, or other third party owns policy
- Owner collaterally assigns policy to premium payor
- Premium payor pays premiums (not deductible) – treated as loans
- Premium payor has right to call demand loan at any time; parties could also use a term loan
- Policyowner owns cash value, but owes loan amount; cash value in excess of loan is policyowner's "equity"
- Policy beneficiary receives income tax-free death benefit in excess of loan
- Employee reports/pays interest – applicable federal rate
- Each premium treated as a new loan for tax purposes

# Premium Financing Plan

- In premium financial arrangements, insured or a trust owns the policy and borrows money from a bank.
- Each year the premiums are funded by a loan, and loan interest has to be paid and increases annually.
- In prior year low interest rate environment, premium financing had become more popular (3-4%).
- Today more difficult but can still work for high growth business (7-8%)

# Premium Finance Plan



Bank

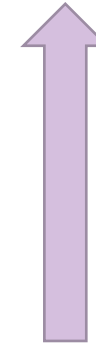
Premium - \$



Interest - \$

INSURED

LIFE INSURANCE



Gift - \$

Insured





# Summary

## Term

- Cheaper out of pocket cost
- Only for a set number of years (10, 20, 30)
- Payout % is very low – have to die within the term
- Death benefit typically income tax free
- Can be very expensive when you really need it
- Convertible

GUL – No cash value – lifetime premiums

## Permanent

- Premiums higher – won't increase
- Higher out of pocket cost, but for set number of years
- Builds cash value
- Guaranteed to pay out
- Cash value build up tax-deferred
- Dividend earnings
- Flexible
- Death benefit typically income tax free

# Thank You!

Gary Sancilio  
The Affinity Group, LLC  
4 Tower Place, Fl. 1  
Albany, NY 12203  
[Gsancilio@affinityadvs.com](mailto:Gsancilio@affinityadvs.com)  
518-776-1268





# INTERGEN

Wrap Up and Questions





# THANK YOU!

Please complete the brief survey with your feedback.

*See you next year for the*

19<sup>th</sup> ANNUAL

**INTERGENERATIONAL  
ESTATE PLANNING  
CONFERENCE**