

# Death and Taxes for North Carolina Business Owners

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*Changing tax laws, political uncertainty, and the whole family at Thanksgiving can take us on a roller coaster ride of ups and downs. But savvy business owners (and their estate planning counsel) know that – in the end – current circumstances provide the opportunity for savvy wealth-*

## *transfer planning.*

The federal estate tax exemption is still at historically high levels, allowing an individual to transfer up to \$13,990,000 in 2025 (through transfers made during life or at death) without estate or gift tax. The exemption amount, however, is set to be reduced by approximately half in 2026.

Meanwhile, markets have been volatile (albeit mostly rising), and interest rates have begun to come back down.

These circumstances have inspired a new round of estate planning for those focused on efficient wealth transfer. Some of those planning techniques include:

### **Gifts to Utilize Exemption**

Many wealthy individuals recognize the "use it or lose it" nature of the current gift and estate exemption and are choosing to make large gifts before exemption amounts go back down. The utility of these gifts can be maximized by gifting assets likely to appreciate over time or subject to valuation discounts. These gifts often are made in trust for asset protection purposes and to achieve additional tax benefits.

### **Grantor Retained Annuity Trusts**

A grantor retained annuity trust ("GRAT") is a special kind of irrevocable trust. The person who creates and funds the trust – the "grantor" – retains the right to an annuity payment from the trust for a period of years. At the end of the term, the remaining trust property passes to other beneficiaries (such as the grantor's children) either outright or in further trust. Assuming the grantor survives the term, those remaining trust assets are removed from the grantor's taxable estate.

However, unlike a traditional gift of cash or gift in trust (which could trigger gift tax on the entire amount

contributed), only the value of the remainder interest in the GRAT is considered a gift. Because there is no precise way to assess the value of the remainder interest at the beginning of the trust term, the government simply assigns a present value based on interest rates in effect at the time of the transfer.

By setting the annuity payment at a sufficiently high level, the remainder interest can even effectively have a "zero" value, thus using little or none of the grantor's gift and estate tax exemption to affect the gift. These "zeroed-out" GRATs are especially appropriate for individuals who have already exhausted their lifetime gift tax credits and are already maximizing their annual exclusion gifts.

If the GRAT assets outperform the original interest rate over time (which is easier to do as rates decline), there is a windfall for the beneficiaries of the trust.

### **Sales to Grantor Trusts**

Closely-held business owners might consider completing an installment sale of discounted business interests to an irrevocable grantor trust in exchange for a promissory note. The note should employ the proper applicable federal rates ("AFR") depending on the repayment term. The trust can be designed as a separate entity for federal estate and gift tax purposes while still allowing for trust income to be taxed to the grantor for income tax purposes (thus increasing growth within the trust).

Post-sale appreciation in the value of transferred assets can pass to the trust beneficiaries outside the grantor's taxable estate free of federal estate or gift tax.

### **Intrafamily Loans**

Senior family members may also consider lending assets at a "frozen" value to junior family members at the appropriate AFR.

To pass muster, intrafamily loan payment terms must be honored as if the loan were between unrelated parties. If the assets appreciate in value significantly over the course of the intrafamily loan, then the return in excess of the "hurdle rate" benefits the junior family member borrower and is outside the senior family member lender's taxable estate.

Ward and Smith's trust and estates attorneys work with business owners, family offices, and financial advisors throughout North Carolina to structure complex tax-efficient estate plans. Let us know if we can assist.

***This is a part of our November series: "Family Matters." For more insights, [click here](#).***

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