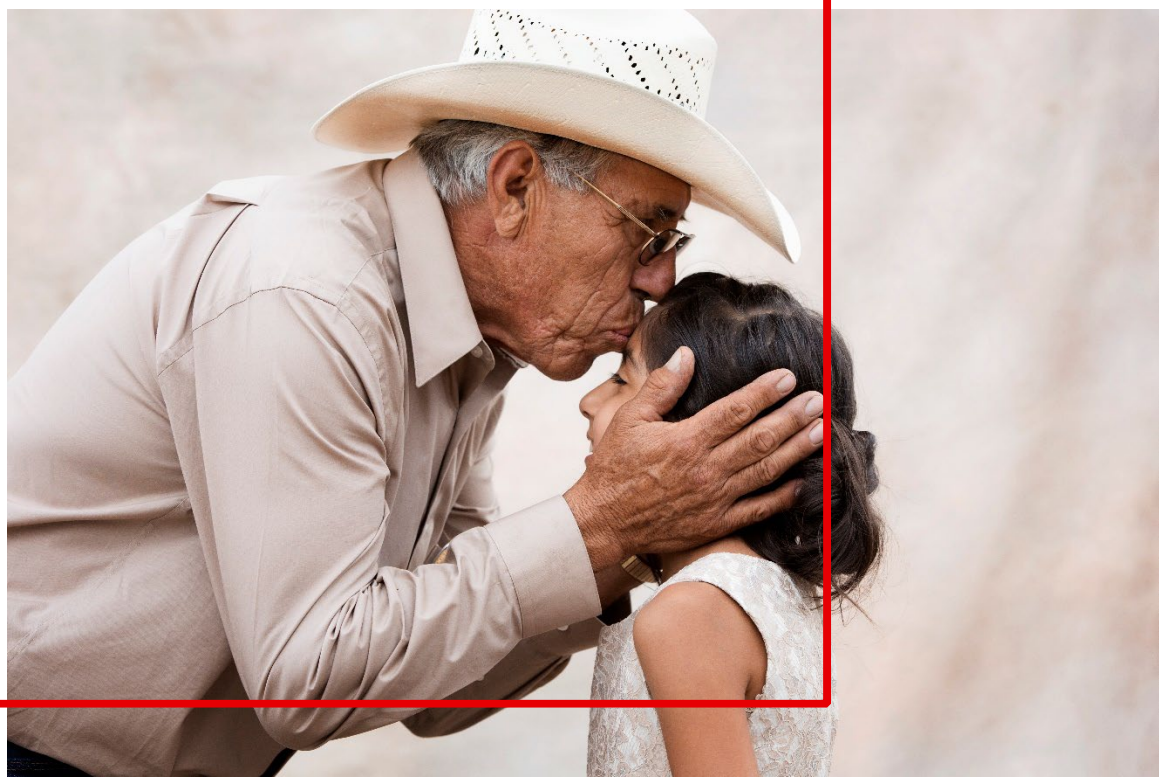
UBS

Advanced Planning

Planning for multicultural investors



Contents

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Introduction

Multicultural investors (MCIs) (represented in Invest to Advance: How Multicultural Families Build Generational Wealth (a publication of the UBS Multicultural Client Segment) as Black, Asian, and Hispanics and Latino American investors) have been financially excluded and underserved in the type and depth of research that can accurately reflect their aspirations and raise their visibility.[1] With more access to financial services, high net worth and ultra high net worth MCIs are positioned for the next stage in building, allocating, and preserving wealth. Even though the financial industry has made strides in serving MCIs, there is so much work to do. Raising visibility of this important investor segment will continue to help build tailored, inclusive wealth solutions.[2]

In an effort to provide more visibility and access as a complement to the MCI report, this whitepaper will serve as a roadmap and walk through the benefits of wealth transfer, tax minimization, and wealth preservation.

Basic estate planning

In some cultures death is not something that's discussed, much less planned for. However, if appropriate documentation is not in place, an individual's wishes relating to the management of financial affairs, healthcare-related decisions, and the distribution of their estate will not be carried out as desired.

Although many may not want to face it, MCIs will all pass away at some point, and planning ahead clearly has its benefits: (1) it is informative, (2) it provides peace of mind, and (3) it creates efficiency. Without any planning, an MCI's estate will pass pursuant to state intestacy laws. This is rarely a desired result as it generally consumes more time and money than if the time and effort had been put in during the MCI's lifetime.

Estate planning overview

A foundational estate plan will generally consist of a will, revocable living trust, financial durable power of attorney, and medical directive. Each state has laws that govern the drafting, interpretation, and validity of these documents. The state where an MCI is domiciled generally determines the applicable state law; however, assets in other states should be taken into account as well.

For more information on basic estate planning, see Christine Kolm, *Estate Planning: An Overview* (a publication of the UBS Advanced Planning Group). For more information on international estate planning, see Christine Kolm, Jacqueline Denton, and Cintia Jasminoy, *Estate Planning for International Individuals* (a publication of the UBS Advanced Planning Group).

Probate and asset titling

Administration of an MCI's estate, post-death, is also governed by state law. The location of the assets and where the MCI lived at the time of death are determinative. If an MCI dies without any foundational estate planning documents in place, state law will most likely control the state probate administration process and the distribution of the MCI's assets.

If an MCI created appropriately drafted foundational estate planning documents, then the terms of such documents reflecting the MCI's specific wishes will generally control the disposition of assets. However, depending upon the state, state law may still control some aspects of the administration. Therefore, not only is creating the estate plan important, but titling of the MCI's assets in conjunction with this planning is imperative.

This can include (1) funding a revocable living trust, (2) designating beneficiaries on life insurance policies and retirement and employee benefits, and (3) determining if applicable state law authorizes other non-probate

[1] Invest to Advance: How Multicultural Families Build Generational Wealth (a publication of the UBS Multicultural Client Segment)

[2] Id.

distribution of assets (such as transfer on death or payable on death designations).

For more information on probate and asset titling, see Christine Kolm, *Probate Primer*, and Catherine McDermott, *Asset Titling: Traps and Opportunities* (publications of UBS Advanced Planning Group).

Fiduciary appointments

While most people think of estate planning in the context of disposition of assets, what's also crucial is designating the appropriate individuals (or in some cases, banks or trust companies) to carry out these wishes, both at death and upon incapacity. Understanding the duties and liabilities of each role is essential.

An MCI's agent under financial and medical powers of attorney is tasked with making financial and medical decisions, respectively, for an incapacitated MCI. For financial decisions on behalf of an MCI, among other things, the agent has to pay bills, authorize transactions, and manage the MCI's overall financial affairs. For medical decisions on behalf of an MCI, it's important that the agent understands and is aligned with the MCI's wishes regarding medical procedures and life sustaining treatment.

A personal representative of a deceased individual's estate is in charge of carrying out the terms of the deceased individual's will.[3] Similarly, a trustee of a trust is in charge of carrying out the terms of the trust. A trustee must abide by and is governed by the terms of the trust document (and state and federal law). Each act as a fiduciary and are entrusted with control over assets which are to be managed and distributed for the benefit of someone else. As a fiduciary, the executor and trustee will be held to a very high standard.

For more information on fiduciary appointments and duties, see Christine Kolm, *Estate Planning: An Overview*, and Casey Verst, *Duties of a Trustee* (publications of the UBS Advanced Planning Group).

Legacy planning

Congress limits the ability to make lifetime gifts to heirs (e.g., children, grandchildren, other family members, and friends).[4] The Internal Revenue Service (IRS) enforces such limits. Generally, the two main tools are the annual exclusion and the lifetime exemption. In 2022, the annual exclusion allows an individual to give up to $16,000 to any number of individuals ($32,000 per married couple). Any gifts in excess of this amount count against an individual's $12.06 million lifetime gift tax exemption in 2022 ($24.12 million for married couples).[5]

Caring for family members and friends is a core cultural value and source of pride for many Hispanic and Latino individuals throughout their wealth journeys. The vast majority provide support directly or through an inheritance and note that they too benefited from such assistance.[6] There are various estate planning strategies that can be implemented in order to maximize such a transfer of wealth to desired beneficiaries while potentially mitigating transfer tax consequences.

Lifetime gifting

Currently, there are three types of wealth transfer taxes that may be imposed on the transfer of property during an individual's life or at death—gift tax, estate tax, and generation-skipping transfer (GST) tax.

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[3] The individual or institution nominated as personal representative under the terms of the deceased individual's will might not be the person ultimately appointed. The individual or institution will have to qualify and be formally appointed by the probate court in the respective jurisdiction.

[4] This whitepaper uses the term "heir" in the colloquial sense—referring to a person who receives property from a decedent—rather than its strict legal sense.

[5] This assumes that each spouse is a US citizen. For a discussion of the gift and estate taxation of non-US persons, see Carrie Larson, *Planning for Non-US Citizens* (a publication of the UBS Advanced Planning Group). For a US person, the gift and estate tax exemption is indexed annually for inflation and currently includes a temporary increase. This increase expires after 2025, at which time the gift and estate tax exemption will be cut roughly in half.

[6] Invest to Advance: How Multicultural Families Build Generational Wealth (a publication of the UBS Multicultural Client Segment)

In the most simplistic terms, the estate and gift tax are very similar. Each is a tax on transfers to individuals. The primary difference is timing (although there are other more nuanced differences that arise in some situations). The gift tax is levied on transfers in excess of the lifetime exemption made during the individual's life, while the estate tax is levied on transfers at death.

The transfer tax rate is 40%, but there is an unlimited deduction for transfers to qualified charities and U.S. citizen spouses.

In addition to the gift tax annual exclusion and the lifetime exemption discussed above, the tax code grants health care and education expense exclusions. Currently, there is an unlimited gift tax exclusion (in addition to the $16,000 current annual exclusion) for qualifying payments of tuition (does not include room and board or books) paid directly to an educational institution and an unlimited gift tax exclusion for the payment of medical expenses (including health insurance premiums) to qualified institutions.

The GST tax is a separate and additional layer of tax on transfers to recipients who generally are two or more generations younger than the donor (known as "skip-persons"). It is important to note that the tax may be imposed on transfers that may or may not also be subject to gift or estate tax. Simply stated, the GST tax is a flat tax applied at the highest estate tax rate in effect at the time of the transfer (40% in 2022) and applies to both direct transfers and transfers in trust.

Every individual currently has an $12.06 million exemption from GST tax that they may use over their lifetime (or if unused during the individual's lifetime, at death).[7] The GST tax exemption can shelter transfers made directly to "skip persons" from GST tax (i.e., a gift to a grandchild), or it can be allocated to a properly structured trust, which enables the trust and all appreciation on its assets to pass to future generations free of tax.

Leaving an inheritance

There are several planning options when it comes to tax efficient transfers to desired beneficiaries. The simplest form, whether made during life or at death, is an outright gift. However, simplicity doesn't necessarily provide tax efficiency or creditor protection. An alternative approach often involves making gifts via a trust.

Trust Basics

What is a trust?

A trust is a three-party arrangement among: (1) the creator of a trust (generally called donor, grantor, settlor, or trustor), (2) the manager of a trust (trustee), and (3) the trust's beneficiary, which may include more than one person or organization.

A trust's creator may form a trust during their lifetime or upon death. A trust can incur federal income tax liability that is separate from that of the grantor (but, as discussed below, there are circumstances when the trust may not be separate for federal income tax purposes). Trusts may be organized in different ways and serve a variety of grantor motives. Funds placed in trust can provide advantages for estate, financial, personal, or business purposes.

Trustees

The trustee is the individual or entity responsible for holding and managing the trust property for the benefit of the beneficiary. Trustees can be an institutional fiduciary or any competent individual who isn't a minor. The trustee holds the legal title to the trust property. As such, the trustee has a fiduciary duty to the beneficiaries with respect to the trust property. In the event of a breach of fiduciary duty, a trustee may be held personally liable. Typically, a trustee must pay more attention to the investments and management of trust assets than such individual would for their own personal accounts. The

[7] Like the estate and gift tax exemption, this exemption is indexed for inflation and scheduled to revert to the prior exemption amount of $5,000,000 (indexed for inflation) on January 1, 2026.

trustees generally also have to coordinate the preparation, verification, and submission of all required state and federal tax forms and legal documents.

In addition to trustees, the roles of trust protectors and trust advisors are becoming more common. Trust protectors and trust advisors can provide additional oversight and support for a trustee. These roles can also provide additional flexibility to the trust structure and potentially facilitate unforeseen circumstances that may arise in the future.

Beneficiaries

The beneficiaries of a trust are the persons or entities who have the beneficial interest in the trust assets. The terms of the trust agreement will outline when and to what extent the beneficiary is entitled to distributions of the trust's income or principal (either currently or in the future).

The type of trust structure will often be determined based on the intended beneficiaries. Different trust vehicles are often used for charitable beneficiaries versus non-charitable beneficiaries. Not only will the intended beneficiaries impact the trust structure, but so will the donor's intent as to distributions, assets contributed to the trust, creditor protection, fiduciary appointments, and so much more.

For more information on trust basics and terminology, see Carrie J. Larson, *Trust Basics for Beneficiaries*, and Casey Verst, *Duties of a Trustee* (publications of the UBS Advanced Planning Group).

Trust structures

Assets can be transferred using various wealth transfer techniques. The following are some of the methods most widely used by estate planners, any one of which may be used to transfer various types of assets.

Grantor versus nongrantor trust

Many irrevocable trusts are characterized as nongrantor trusts. This simply means that the trustee of the trust is responsible for filing a trust income tax return, and that the trustee will use trust assets to pay any income taxes due.

In contrast, a grantor trust is a trust for which the grantor generally is held responsible for reporting and paying the income generated by the trust. All such income is reported on the grantor's personal income tax return.[8] This tax treatment generally is the result of the grantor or the grantor's spouse having certain interests, rights, or powers in the trust (such as being eligible to receive distributions of income or the power to substitute trust property for other property of equivalent value). These trusts are sometimes called "defective" for income tax purposes.

There are many different types of trusts that are considered grantor trusts (such as revocable trusts, which are the basis for many estate plans). However, our focus in this section is on those trusts that are used for the purposes of wealth transfer during the grantor's life. These grantor trusts should be drafted such that the assets are not includable in the estate of the grantor at the grantor's death and are irrevocable.

In addition, there are many different types of trusts that are considered nongrantor trusts (such as incomplete nongrantor (ING) trusts, which are often used to avoid state income taxes). Nongrantor trusts can be drafted to be includable or excludable from the grantor's estate; however, nongrantor trusts generally incur federal income tax liability that is separate from that of the grantor.

For more information on the differences between grantor and nongrantor trusts, see Casey Verst, *Using Irrevocable Grantor Trusts to Transfer Wealth*, and for more information on nongrantor-ING trusts, see Ann Bjerke and Todd D. Mayo, *ING Trusts* (publications of the UBS Advanced Planning Group).

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[8] In some cases, a trust can be a grantor trust with respect to a beneficiary, and the beneficiary must report the trust's income, deductions, and credits on the beneficiary's personal income tax return. In this whitepaper, however, we will focus on grantor trusts that are grantor trusts with respect to the grantor (and not with respect to a beneficiary).

Gifts to grantor trusts

Assets may be given to a trust for an intended recipient, rather than outright. The trust can be structured as a grantor trust for income tax purposes. With a grantor trust, all items of income, deduction, credit, and loss will flow through to the grantor's personal income tax return, as opposed to the trust paying its own taxes from the trust's own assets. By paying the income tax liability of the trust from the grantor's own assets, the grantor allows the trust assets to grow free from income tax liability.[9] Since significant cash flow (and potentially, taxable income) may be generated from assets in the trust, a grantor trust provides a way to enhance the wealth transfer impact of the gift.

Additionally, the trust may provide protection from the beneficiary's creditors (including divorcing spouses) if certain provisions and restrictions are included in the trust agreement. This allows an individual to transfer assets to trusts for the grantor's children, or to the grantor's spouse, while maintaining a measure of asset protection for the beneficiary.

Grantor retained annuity trust

A grantor retained annuity trust (GRAT) is an irrevocable trust designed to transfer future appreciation on an asset with little or no gift tax cost. This wealth transfer strategy may appeal if an individual has an asset expected to appreciate significantly in a short time period, and wants to hold onto the asset itself, but is willing to transfer potential growth. It can also be useful in situations where an individual would like to transfer wealth, but has already exhausted their lifetime gift tax exemption.

The grantor creates a GRAT and funds it with assets that are expected to appreciate. The trustee of the GRAT distributes an annuity (a fixed annual amount determined at the outset) to the grantor for a term of years. At the end of the GRAT term, any assets remaining in the trust pass to the remainder beneficiaries—often the grantor's children or trusts for their benefit.

For more information on GRATs, see Jennifer Lan, *Grantor Retained Annuity Trusts* (a publication of the UBS Advanced Planning Group).

Spousal lifetime access trust

The primary beneficiaries of most trusts are the children and more distant descendants of the grantor. The distinguishing feature of a spousal lifetime access trust (SLAT) is that it benefits the grantor's spouse as well as the grantor's descendants (and possibly others). Naming a spouse as a discretionary beneficiary provides a simple way for assets to be returned to the couple if their economic situation changes at some point in the future and they want some or all of the transferred funds back. The intention in creating a SLAT is that the grantor will never need the transferred funds, but naming a spouse as a beneficiary creates a "Plan B" for the family.

Since the grantor's spouse, and not the grantor, is a trust beneficiary, the grantor only has indirect access to SLAT funds. If the trustee makes a distribution to the beneficiary-spouse, then the beneficiary-spouse may be expected to spend that distribution in a way that benefits the married couple, but they are under no legal obligation to do so. A SLAT, therefore, may also benefit a family.

While a SLAT is a very popular and often useful planning strategy, there are several traps that need to be considered when drafting and funding a SLAT. For example, additional considerations must be made if an individual lives in a community property state. Assets transferred to the trust should be made from the grantor's separate property and not from jointly titled or community property. Additionally, consideration must be given to (1) divorce, (2) death of the beneficiary spouse, and the (3) reciprocal trust doctrine.[10]

For more information on SLATs, see Catherine McDermott, *Spousal Lifetime Access Trusts* (a publication of the UBS Advanced Planning Group).

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[9] MCIs should consider their ability to pay income tax from their other assets.

[10] If both spouses create identical trusts for the benefit of the other and fund them with identical assets they will be in the same position as if each had created a trust for their own benefit and the trusts will be uncrossed, resulting in full estate tax inclusion.

Dynasty trusts

Dynasty trusts are trusts that are established for the benefit of multiple generations and structured to remove assets from the transfer tax system for multiple generations. A dynasty trust therefore enables a grantor to "leverage" the grantor's gift and GST tax exemptions by removing from the grantor's estate all future income and appreciation on the assets transferred to the trust.

Dynasty trusts can be designed as grantor trusts or as nongrantor trust. SLATs, and many other types of trusts can all be designed as dynasty trusts as well.

Dynasty trusts are designed to continue for as long as the applicable governing law allows. In certain jurisdictions, the trust may theoretically continue forever. The structure of the dynasty trust can be as flexible as the grantor of the trust wishes to allow for future unanticipated issues.

For more information on structuring the terms of trusts, see Rebecca Sterling, *Creating Flexibility in Trust Agreements* (a publication of the UBS Advanced Planning Group). For an overview of the various techniques discussed in this section, see Casey Verst, *Planning Opportunities When Asset Values Decline* (a publication of the UBS Advanced Planning Group).

Generational support

Trusts are not the only option when it comes to providing generational support or inheritance. While a trust could satisfy the need for loans to family members, education expenses, and providing support to elder family members, there are other options to consider as well. The strategy that may work best for an MCI will depend on the MCI's individual and particular circumstances.

Intra-family loans

Lending between family members is a common occurrence. Intra-family loans are more predominant among high net worth and ultra high net worth families, in part because these families have greater lending capacity. Unlike commercial loans, intra-family loans are usually motivated by a desire to benefit the borrower in some way rather than maximizing the return on the loan.

While loans between family members seem relatively simple at first glance, there are a number of income, gift, and estate tax traps of which both lenders and borrowers should be aware. Fortunately most of these traps can easily be avoided by proper loan structure and administration.

Perhaps the most common form of intra-family lending is a loan from a parent to a child to help the child purchase or invest in a specific asset, such as to assist a child with the purchase of a home or with the purchase or start-up of a business.

Intra-family lending can itself be an efficient and relatively simple estate tax planning strategy, especially in low interest rate environments. With this type of lending, the senior generation lends funds to the junior generation at the lowest permissible interest rate, and hopes that during the term of the loan the junior generation can invest these funds and earn a return in excess of the interest rate on the loan. Any "excess return" belongs to the junior generation with no gift tax consequences, and avoids potential estate tax in the senior generation's estate.

There are a variety of ways to structure intra-family loans, including use of a trust or outright, depending on the lender and the borrower's respective circumstances. The transfer must be a bona fide loan with a real expectation of repayment and an intention to enforce the debt. It should always be evidenced by a promissory note signed by both the lender and borrower and which sets forth all the applicable terms of repayment.

For more information on intra-family loans, see Christine Kolm, *Intra-Family Loans* (a publication of the UBS Advanced Planning Group).

529 accounts

Families who want to reduce their estate tax exposure and save for education costs may wish to consider funding 529 accounts as an option. A contribution to a 529 account for children, grandchildren, or other family members or friends takes advantage of tax-deferred growth and tax-free withdrawals for qualified education expenses. An individual can pre-fund up to five years of annual gift exclusions in one year for this purpose, so a married couple together can contribute $160,000 to a 529 account for each beneficiary in 2022, less any

contemplated or actual annual exclusion gifts made to those beneficiaries in the same year.

While 529 accounts have grown in popularity, there are limitations on use, size, and investment parameters which should be taken into account.

For more information on 529 accounts, see Brad Dillon, *Funding Education: 529 Accounts and Annual Giving Trusts* (a publication of the UBS Advanced Planning Group).

Power of appointment support trust

Traditionally, long-term trusts (like the ones discussed above) are commonly used by wealth families to benefit downstream generations—the grantor's children and grandchildren. But these days, many wealthy families also support their own parents or in-laws (the upstream generation), who may well be one of these individuals who will not fully use their federal estate tax exemption. If that is the case, this upstream generation may present an opportunity to do some basis planning.

An example of an upstream trust is the power of appointment support trust (POAST) which is an irrevocable trust established by a grantor to provide support for a senior generation family member and the descendants of the grantor. The POAST then captures the senior beneficiary's unused federal estate tax exemption and GST tax exemption (usually by granting such senior beneficiary a general power of appointment) that would otherwise not be used on the senior beneficiary's later death. With a general power of appointment, the holder of the power of appointment (called the power holder) can direct assets to anyone, but must include one of these four classes of appointees—the power holder, the power holder's estate, creditors of the power holder, or creditors of the estate of the power holder. A general power of appointment will cause the trust assets to be included in a power holder's estate for estate tax purposes, even if the power is not exercised.

When properly set up, the senior beneficiary's GST tax exemption may be used to protect POAST assets from future transfer tax for multiple generations of the grantor's family. The POAST also provides for a date of death basis adjustment of all or most the assets in the POAST at the senior beneficiary's death, thereby reducing or eliminating the potential income tax on appreciated assets later sold by the trust. Therefore, the grantor will generally use low basis assets (generally with high appreciation potential) to fund a POAST.

While the POAST can provide support to a senior beneficiary and income tax basis adjustment for trust assets at the death of the senior beneficiary, the general power of appointment should be carefully drafted. There is no guarantee that the power will not be exercised by the senior beneficiary, which could potentially divert assets away from the grantor's intended beneficiaries and result in the loss of grantor trust status (if initially set up as a grantor trust). Finally, with the general power of appointment, the assets of the POAST may be reachable by the senior beneficiary's creditors.

For more information on POAST, see Christine Kolm, *Power of Appointment Support Trusts* (a publication of the UBS Advanced Planning Group).

Asset types and growing wealth

Planning strategies are often driven by assets (1) what type of asset the individual wants to gift and (2) the intend use of such asset by the beneficiary. The type of asset can affect what planning strategy might make the most sense, and, thus, an individual should be certain of exactly what they own in order to assess what and how much may be transferred, and how best to do so.

Overview

First and foremost, it is critical to determine how assets are legally owned and held. But this an often-overlooked component of financial and estate planning. It's important to examine asset titling both at the time the strategy is implemented and periodically thereafter as changes to the balance sheet or estate plan occur.

Additionally, if an asset is determined to be held within an entity (like a partnership, corporation, or limited liability company) there may be transfer restrictions within the governing documents. These would need to be assessed and dealt with prior to implementation of any strategy.

Asset titling has far-reaching implications, impacting not only estate planning but also creditor protection, income tax planning, and incapacity planning. Deciding how to title assets can be a complex proposition and every individual's strategy depends on their own unique circumstances, goals, and state of residency.
For more information on asset titling, see Catherine McDermott, *Asset Titling: Traps and Opportunities* (a publication of the UBS Advanced Planning Group).

Real estate

Purchase of real estate

Real estate is a common path to wealth for many individuals. Half of Black investors grew up in households that emphasized real estate investing. Nearly six in 10 currently invest in real estate, income properties, or vacation rentals.[11]

Investing in real estate can often require a substantial amount of funds upfront. Often wealthy individuals will therefore assist family members (often the younger generation) with the purchase of a home or other real estate investment. This assistance can take a variety of forms.

An individual can co-sign a loan, make a loan to the intended beneficiary, or make a cash gift to help with a home or other real estate purchase. Each approach has its own benefits and drawbacks in terms of the effects on the donor and the beneficiary.

This type of assistance often allows the younger generation to enter into the real estate market on more favorable terms than they may otherwise receive through conventional mortgage standards. These structures can be invaluable to a child who lacks credit history or is unable or unwilling to provide collateral associated with other types of financing.

Each option is not without its risks. The financial resources of the donor need to be taken into account, and the donor needs to be cognizant of their own cash flow needs and desires. If the beneficiary defaults on the loan, the donor will be liable, so they should also consider the ability of the beneficiary to repay any form of loan.

For more information on help with the purchase of real estate, see Christine Kolm, *Intra-Family Loans*, and Jennifer Lan, *Help with a Home* (publications of the UBS Advanced Planning Group).

Vacation home

As an individual continues to build wealth, the acquisition of secondary or vacation home becomes a priority. These retreats are often some of the most cherished family assets, not only because of the economic value of the property, but also because of an emotional attachment to these places. Therefore, many family members have a heightened focus and interest in ensuring that the family vacation home is preserved for the next generation and that it passes in a fair and equitable manner. Planning for the use and transfer of the family vacation home is challenging, because it must not only navigate the legal and tax aspects of wealth transfer, but also the emotional considerations of the family's various members.

Not only can a secondary or vacation home have sentimental value, it can also be a source of revenue from rental activity. Whether used for personal enjoyment or investment purposes, a secondary or vacation home can also cause family drama. Care should be taken to set clear boundaries and guidelines around use, maintenance, and upkeep. Family members may wish to formalize rules and responsibilities related to such occupancy and expenses. Creating a plan that navigates these complexities is challenging, but creating such a structure can provide enjoyment of the family vacation home for generations to come.

For more information on secondary and vacation homes, see Joanna Morrison, *Family Vacation Homes* (a publication of the UBS Advanced Planning Group).

Investment assets

Asian American investors prioritize growing their wealth rather than preserving it. Their primary source of wealth is employment income which is then deployed into

[11] Invest to Advance: How Multicultural Families Build Generational Wealth (a publication of the UBS Multicultural Client Segment)

stocks.[12] Salaries and bonuses are not the only source of employment income, especially for founders and early employees. Often, these founders and early employees are provided with equity compensation which generally takes the form of grants of stock options or restricted stock.

There are various gifting strategies around such equity compensation, often times unknown to these founders and early employees. While complex in nature, equity compensation is a significant source of wealth creation for many individuals and worth exploration in the appropriate circumstance.

While stocks are a frequent source of wealth for many, MCIs should be careful when holding large, concentrated stock positions. Certain strategies can help individuals preserve or diversity out of a concentrated position depending on their goals. Individuals can implement a strategy to allow for continued participation in the growth potential of a stock or to simultaneously support their charitable goals.

For more information on equity compensation, see Todd D. Mayo, *Equity Compensation*; for more information on concentrated stock, see Christine Kolm, *Concentrated Stock Positions*; and, for more information on investing trust assets, see Todd D. Mayo, *Investing for Trusts*. (Each of these is a publication of the UBS Advanced Planning Group.)

Business ownership

MCIs tend to attribute more of their wealth to business interests than other high net worth or ultra high net worth investors overall.[13] One of the most fascinating business stories in the United States of the past couple of decades has been the growth of minority-owned small businesses and their contribution to our country's present and future economic health. It is important for MCIs to understand the barriers and opportunities surrounding minority small business owners to fully unlock the segment's economic power.[14]

Business succession planning

Some families who have built their wealth through business ownership wish for their business to pass intact to their children. After working many years to grow a business, many owners wish to exit the business and transfer the reigns to other family members. In such situations effective business succession planning is critical for the long-term success of a family business.

In order to accomplish a smooth transition between generations, MCIs should put a business succession plan in place that may include the establishment of a management committee to make decisions during any period of incapacity and during the transition period following death and until another family member is ready to run the company on their own.

For more information on business succession planning, see *Business Succession Planning* and *Business Succession Planning with Non-Active Family Members* (publications of the UBS Advanced Planning Group).

Sale of a business

Sometimes, the business is the glue that keeps the family together. As such, a business owner should first make a comprehensive analysis of the alternatives to sale. For example, are there family members who could step into the shoes of current family management? If not, could professional management be brought in to avoid a sale?

If appropriate succession planning isn't possible, consideration of a sale may become the primary objective. Transparency and proper communication among relevant family members are necessary to maintain trust after the sale. If family dynamics issues are properly managed and the transaction is handled in a way sensitive to both the needs and feelings of family members, a sale may be the best solution and may actually improve family relations over time.

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[12] Id.

[13] Id.

[14] Isaac Mizrahi, *The Minority-Majority Shift. Two Decades That Will Change America. The Large Role of Multicultural Small Businesses.* Forbes, October 22, 2020 (https://www.forbes.com/sites/isaacmizrahi/2020/10/22/the-minority-majority-shift-two-decades-that-will-change-america-the-large-role-of-multicultural-small-businesses/?sh=2451eca162d6)

A truly efficient sale incorporates tax planning opportunities that can result in significant income, gift, and estate tax savings that may be lost once the deal is closed. Business owners may engage in pre-sale tax planning strategies to minimize income tax on the sale. Gift and estate tax savings can be achieved by transferring part of the value of the owner's business to family members, trusts, or other entities at a lower valuation prior to the close. When contemplating the sale of a business, owners should make sure that the transaction structure complements their family's financial goals and objectives.

The structure of the sale itself and the corresponding tax minimization strategies are dependent on the type of entity (for example, S corporation, C corporation, partnership, limited liability company) contemplated for sale and the families' overall financial goals and intentions. In conjunction with income, gift and estate minimization strategies, the MCI should also consider what portion of the business the MCI wishes to retain for their benefit versus gifting to family members and charitable organizations.

For more information on selling a business, see David Leibell, *Planning for the Sale of a Closely Held Business* (a publication of the UBS Advanced Planning Group in collaboration with Family Office Solutions) Ann Bjerke, *Pre-Sale Planning*, David Leibell, *Personal Planning for Start-Up Founders*, and Todd D. Mayo, *Qualified Small Business Stock* (publications of the UBS Advanced Planning Group).

For more information on income, gift, and estate tax minimization strategies, see Legacy Planning above and Philanthropic Planning below.

Philanthropic planning

MCIs are generally charitably inclined and are driven by a desire to give to culturally-aligned institutions. MCIs want to help people with the same background succeed, narrow the wealth gap among difference race and ethnic groups, and pay forward the opportunities they were given.[15]

The tax code imposes limitations on charitable income tax deductions based on an individual's adjusted gross income (AGI).[16] Contributions of qualified appreciated property to a public charity (including a donor advised fund) can be deducted up to 30% of AGI while contributions of cash to a public charity can be deducted up to 60% of AGI. For contributions to a private foundation, the AGI limits are 20% and 30%, respectively. Excess charitable contributions carry over for five years.

Outright giving

The simplest form of charitable giving is making outright gifts of cash to a public charity. While gifts of cash are quick and easy, they are often suboptimal from a tax perspective. Appreciated property held long-term is typically the most attractive form of property to give to charity during a donor's lifetime. The type of asset an MCI chooses to donate will depend on the MCI's financial status and their ultimate charitable and tax minimization goals.

When donating to a public charity, especially on an on-going basis or when large donations are anticipated, charities strive to accommodate and properly recognize their donors but their ability to honor the donor's request or intent may be limited by federal or state law or the charity's internal governance documents. Ideally a donor and charity will openly discuss their objectives and priorities in order to understand the parameters and expectations surrounding the gift and come up with a mutually satisfactory gift agreement.

For more information on making strategic charitable gifts, see Ann Bjerke, *Negotiating Charitable Gifts* (a publication of the UBS Advanced Planning Group).

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[15] Invest to Advance: How Multicultural Families Build Generational Wealth (a publication of the UBS Multicultural Client Segment)

[16] More precisely, these limits are based on the donor's contribution base, which is the donor's adjusted gross income calculated without regard to any net operating loss carrybacks.

Donor advised funds versus private foundations

Rather than write a check to a favored charity, many donors who make significant gifts prefer to set and implement a strategic giving plan to help ensure that their charitable contributions have the maximum impact. Those donors are also inclined to involve their family members in their charitable planning in the hope that they will pass their values and philanthropic legacy on to the next generation.

Two common charitable vehicles permit a donor to make a charitable contribution in a particular year and deploy the gifted funds over a longer period in accordance with the donor's charitable plan. One such vehicle is a *private foundation*, and the other is a *donor advised fund* (DAF). Private foundations and DAFs operate in a similar manner—both vehicles permit the donor to make a charitable contribution, receive an immediate income tax deduction, and make decisions regarding the distribution of the contributed funds over time. However, a donor should consider the important distinctions between these two vehicles before choosing one over the other.

A DAF is a separate identified fund or account that is maintained and operated by a public charity, which is called a "sponsoring organization." Much like a private foundation, a DAF generally permits a donor to make a charitable contribution, receive an immediate income tax deduction, and advise the sponsoring organization on investment of the assets. The donor may also recommend grants to other charities over time.

A private foundation is a charitable organization that typically receives support only from a single donor or family. It usually is organized as a corporation or a trust. Although a private foundation can directly engage in charitable activities, many private foundations are grantmaking organizations, meaning that they distribute their funds to support the activities of other charitable organizations. One significant benefit of a private foundation is that it generally permits the donor to make a charitable contribution (and receive an income tax deduction) in one year, and then invest and distribute the foundation's funds for charitable purposes over time.

For more information on these charitable planning vehicles and the distinctions between them, see Rebecca Sterling, *Donor Advised Funds and Private Foundations* (a publication of the UBS Advanced Planning Group).

Charitable lead annuity trust

For those individuals who are philanthropic and have taxable estates, a charitable lead annuity trust (CLAT) deserves consideration. A CLAT is an irrevocable trust that first makes a series of fixed payments to charity (usually for 10 to 20 years), after which any remaining assets in the trust typically will benefit non-charitable beneficiaries (usually the grantor's children) without triggering any gift or estate taxes. Wealth will only pass to a grantor's children if the CLAT assets earn more than an IRS prescribed interest rate. As a result, this is a strategy that generally works best when interest rates are low.

That said, there are a number of important decisions to be made in establishing a CLAT. Should the CLAT be a grantor trust or a nongrantor trust? Should the CLAT be creating during the grantor's lifetime or at death? Will the annuity be constant or will it increase over time? What assets should be used to fund the CLAT? Should the charity be fixed or can the trustees choose different charities over time? When implementing this type of strategy, it is important to consider these issues.

For more information on charitable lead trusts, see Jennifer Lan, *Charitable Lead Annuity Trusts* (a publication of the UBS Advanced Planning Team).

Charitable remainder trust

For MCIs looking for ways to generate a tax-efficient income stream and to pursue their charitable goals a charitable remainder trust (CRT) may be an option to consider. A CRT is a technique that can provide: (1) diversification of a concentrated stock position (or other appreciated asset) in a tax-deferred manner, (2) creation of an income distribution stream for the grantor, and (3) a current charitable income tax deduction.

A CRT is an irrevocable trust that provides distributions to individuals during their lives (or for a term of not more than 20 years), with the remainder passing to charity at the end of the trust's term. Because a CRT generally is tax-exempt, it's ideal for the tax-efficient diversification of highly appreciated assets. Although the trust itself is generally not taxable, payments to the non-charitable beneficiaries are taxable under a system of taxation unique to CRTs known as the four-tier system. There are two basic types of CRTs, the unitrust (which provides for variable payments) and the annuity trust (which provides

for fixed payments). Finally, the donor receives an income tax deduction in the year the trust is funded for the present value of the charitable remainder interest (which must be at least 10% of the amount contributed).

Whether a CRT is a good planning strategy will depend on many factors, including (1) is the individual charitably inclined, (2) does the individual have appreciated assets they are willing to sell, and (3) can the individual use the charitable income tax deduction. The benefit of the ability to diversify without current tax should be weighed against the remaining trust assets passing to charity rather than staying in the grantor's family.

For more information on charitable remainder trusts, see Benjamin Trayes, *Charitable Remainder Trusts* (a publication of the UBS Advanced Planning Group).For a comprehensive guide to charitable giving, see David Leibell, *Charitable Giving: The Rules of the Road* (a publication of the a publication of the UBS Advanced Planning Group in collaboration with Family Office Solutions).

Conclusion

MCIs have historically faced financial exclusion in the US, from systemic barriers and discrimination to lack of access to financial institutions and their resources.[17] It's important for MCIs and their advisors to engage in meaningful multicultural wealth dialogue, whether related to investments, planning opportunities, or overall goals. We need to continue to remove barriers and increase access for all MCIs through persistence and vigilance. Representation is important and crucial in order to bridge the trust gap. "It's time to tailor an American dream that includes each and every one of us."[18]

[17] Invest to Advance: How Multicultural Families Build Generational Wealth (a publication of the UBS Multicultural Client Segment)

[18] Dorothy A. Brown, *The Whiteness of Wealth: How the Tax System Impoverishes Black American – And How We Can Fix It* (Penguin Random House 2021)

About the Advanced Planning Group

The Advanced Planning Group consists of former practicing estate planning and tax attorneys with extensive private practice experience and diverse areas of specialization, including estate planning strategies, income and transfer tax planning, family office structuring, business succession planning, charitable planning, and family governance.

The Advanced Planning Group provides comprehensive planning and sophisticated advice and education to ultra-high net worth (UHNW) clients of the firm. The Advanced Planning Group also serves as a think tank for the firm, providing thought leadership and creating a robust intellectual capital library on estate planning, tax, and related topics of interest to UHNW families.

Thank you

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