

Q&A WITH ADAM CROW, JD, LL.M

MANAGING DIRECTOR OF WEALTH PLANNING & STRATEGY

Adam Crow recently joined Stephens as Managing Director of the Wealth Planning and Strategy Group, an extension of the Private Client Group division dedicated to highly sophisticated and complex financial planning. He has more than 15 years of legal and financial planning experience addressing the unique opportunities and issues raised by significant wealth. Here Adam answers a few essential questions for us about his new role, and his rare skill set.

Why did you decide to join Stephens?

During my long tenure as a member of Rose Law Firm here in Little Rock, Arkansas, I worked with Stephens and its clients on a wide range of matters. That allowed me to get to know the Company. I quickly developed tremendous respect for their sophistication, team approach and commitment to clients. We all worked so well together that, over time, it became a natural fit for me to join Stephens.

How will you be helping Stephens financial advisors and their wealth management clients with estate and tax planning goals?

I am helping advisors on a wide array of advanced solutions for the ultra-high-net-worth individuals, families, and privately held businesses they serve. Many of these solutions can benefit clients with investment accounts, or clients that are considering or are in the midst of a private banking transaction. They often involve taking advantage of historically low interest rates and leveraging high gift, estate and generation-skipping tax exemptions. How the rate environment and tax regime might change in the foreseeable future also comes into play.

What's the most important thing advisors should do when working on complex solutions for ultra-high-net-worth clients?

The most important thing for advisors is to understand the client's legacy and family goals, both in the immediate and over the course of many years. When those goals are understood, advisors can take them into account along with a client's risk tolerance and potential income needs to develop a personalized strategy.

Most of these strategies have long-term effects, which can be very beneficial from a tax and family planning standpoint. Due to these long-term effects, advisors should often attempt to include provisions that add flexibility and can be used if there is a change in client goals or tax law. The ability to modify a plan if necessary is something that clients often appreciate most and value over multiple generations.

Is the new presidential administration and change of control in Congress a major concern, from a wealth planning and strategy perspective? Why or why not?

Yes, it is. The current administration has proposed substantially lowering the tax exemption levels for gift, estate and generation-skipping purposes, and raising the tax rates. It has proposed raising income taxes to the extent that top marginal rates (combining federal, state and local taxes) would surpass 60% in certain locations.¹ In addition, some members of Congress have recently proposed broad changes to transfer tax

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and related income tax provisions, including an elimination of the step-up in basis for assets transferred at death and the taxation of unrealized capital gains above \$1 million per decedent.² It is possible that budget reconciliation could be used to enact legislation with a simple 51-vote majority in the Senate.

Furthermore, irrevocable trust strategies often utilize valuation discounts for tax purposes, based on longstanding cases establishing lack of control and lack of marketability for certain assets. The administration could move forward with the issuance of regulations under Section 2704 of the Internal Revenue Code to greatly reduce the ability to take valuation discounts on assets transferred into these trusts.³ These regulations were previously issued in proposed form but withdrawn in 2017.

Given that a massive transition of intergenerational wealth is likely to occur for many families over the next several years — during unknown tax consequences — ultra-high-net-worth clients might want to

lock in estate planning strategies now rather than later. Advisors would do well to explain to clients that evolving political factors could have serious financial consequences.

What concerns do these political factors present for business owner clients?

Assets used in planning strategies often include closely held business interests, so the potential loss of valuation discounts is a real concern. In addition to the transfer tax increases, there are proposed income tax increases that would raise the top federal individual income tax rate from the current maximum of 37% back to 39.6% and would tax long-term capital gains and qualified dividends at the ordinary rate of 39.6% on income above \$1 million.⁴ There is also a proposal to increase the federal corporate income tax rate from 21% to 28%.⁵

The personal income tax proposals would impact many privately held business owners, as it is common for those businesses to be structured as pass-through entities. Also, if these proposals become law they would impact the sale of business interests, which often are taxed in whole or in part at capital gains rates. In many cases, a higher rate of tax would be paid upon the sale. A related proposal would raise taxes on employers for highly paid individuals earning income over \$400,000.

Are there any other wealth planning and strategy issues that business owners should begin addressing?

Beyond the tax situation, owners of privately held businesses need to look at the big picture. They should consider wealth planning strategies years in advance of transactions such as a sale or other liquidity event, which tend to become their main priority once underway. Many of these strategies can involve the next generation of the client's family as well as the next generation of the business. Working with them early in the process helps ensure maximum success.

How do trusts factor into helping wealth management clients with their estate and tax planning goals?

There are three types of irrevocable trusts that may prove highly useful. These of course are all dependent upon a client's circumstances, but often can be very powerful and facilitate the tax efficient transfer of assets and the preservation of intergenerational wealth. Advisors that pay close attention to Grantor Retained Annuity Trusts, or GRATs, Intentionally Defective Grantor Trusts, or IDGTs, and Spousal Lifetime Access Trusts, or SLATs, are poised to add great value.

Can you shed a little light on how these structures work, and why a client might want to use each of them? Let's begin with GRATs.

GRATs can work well for a client who wishes to transfer appreciating assets to beneficiaries or trusts for their benefit. The grantor transfers assets to the GRAT and retains payments, and if the assets transferred to the GRAT appreciate over their initial fair market value plus an IRS hurdle rate based on prevailing interest rates, at the end of the GRAT period the remaining assets can transfer to beneficiaries free of estate and gift taxes. Without GRATs or IDGTs, it is difficult for a client to retain a desirable payment stream and transfer assets without depleting tax exemptions.

What is the difference between GRATs and IDGTs?

IDGTs are somewhat similar to GRATs but they do have key differences, particularly regarding the structure of the sale to the intentionally defective grantor trusts, payments to the grantor, and the amount of existing law in regard to the strategy. For example, unlike GRATs, they allow for a balloon payment at the end of the term of the promissory note, with interest-only payments along the way.

IDGTs are often the preferred vehicle for clients that wish to benefit grandchildren or more remote descendants and minimize generation-skipping transfer taxes. Generation-skipping trusts are often considered in connection with this planning technique, and clients that utilize these trusts can often extend and maximize family tax savings.

Why might clients want to use SLATs, and how do they relate to the other trusts?

SLATs enable clients to pass along wealth for the benefit of their spouse by using gift, estate and generation-skipping exemptions. This strategy allows the assets transferred to the trust to appreciate free of such taxes after the date of the gift while the beneficiary maintains access to those assets. SLATs have become more prevalent in recent years due to historically high exemption levels, which facilitate gifting a large amount of assets to trusts for spouses.

All three of these strategies utilize the grantor trust rules, which cause the assets of the trust to be treated as owned by the grantor for income tax purposes but excluded from the grantor's estate for estate tax purposes if structured correctly. As a result of the grantor trust treatment, the payments to a grantor from a GRAT or IDGT are not subject to income tax.

Besides the Private Client Group, do you anticipate working with any other business lines at Stephens?

Very much so. Business sales or mergers can call for the expertise of Stephens Investment Banking, and executive benefits or risk management strategies might lead to working with Stephens Insurance. Both of these teams and the other divisions at Stephens are invaluable resources to the firm and our clients. We can seamlessly incorporate them into business owner and personal estate planning strategies as needed to accomplish client goals.

When you're not focused on creating solutions that meet your clients' needs, what do you enjoy doing in your time off?

Right now I am focused on Stephens and our clients. When I do have time, I enjoy most outdoor activities. One thing in particular my family and I really enjoy is skiing. It is great exercise, and I appreciate the beautiful natural landscapes and wide open space.

¹ <https://taxfoundation.org/top-tax-rates-under-biden-tax-plan/>
² <https://www.vanhollen.senate.gov/imo/media/doc/One%20pacer%20-%20STEP%20Act.pdf>
³ <https://money.usnews.com/financial-advisors/articles/financial-advisors-eye-bidens-plan-for-estate-taxes>
⁴ https://taxfoundation.org/joe-biden-tax-plan-2020/#_ftnref2
⁵ <https://www.whitehouse.gov/briefing-room/statements-releases/2021/03/31/fact-sheet-the-american-jobs-plan/>