

## CASE STUDY

### AVOIDING BIG TAX BILL FOR LOW-COST-BASIS STOCKS

#### PROBLEM

The five Marks siblings inherit a complex estate from their father, Edward Marks. The estate includes a trust that owns 60% of the Marks Company, a 40% stake in the Marks Company that goes directly to the siblings and an expensive mansion in Weston, Mass. With few liquid assets, the estate has to take out a loan from Marks Company to pay estate taxes. Some of the siblings want to cash out the trust's holdings. The issue is how to end the trust, so the siblings can get money out and pay off the loan. An additional complication: the mansion has been sold at a sizeable gain.

#### SOLUTION

Have the Marks Company redeem—in essence, buy back—the trust's shares, which triggers a capital loss to offset the gain on the mansion. Convert the company to an S corporation, which pays no company-level taxes, so income flows directly to the Marks siblings.

#### DISCUSSION

The process involved:

- Recognizing that the stocks in the trust had declined in value since Edward Marks died at the top of the technology stock bubble, so redemption would trigger a capital loss that could be used to offset the gain on the Weston mansion
- Changing the tax status of Marks Company to an S corporation so cash could flow tax-free to the Marks siblings
- Recognizing that the Marks Company could ultimately be sold to a company that has loss carryforwards and wants to buy its stock to utilize its appreciated assets to absorb its losses, thus allowing the siblings to cash out for an amount representing the fair value of the company without incurring capital gains taxes on the appreciated securities in the company.

The Marks siblings gain access to cash flows from the Marks Company without paying capital gains taxes.