

How to Find a Tax Shelter

Published in MDNetGuide September 2006

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Solid tax planning is almost always a worthwhile goal. While other business expenses, such as payroll, advertising and software, are intended to produce greater income and assets, money spent on taxes return zero economic benefit. Every dollar paid in taxes directly reduces, dollar for dollar, the amount you have available for savings and investment in your business. In these times, I have confidence that you can do a better job spending your money than the Government.

So what can you do to save taxes legally, without spending your life and your savings fighting with the IRS? Clearly, maneuvering through the Byzantine tax code is impractical for most and wisely choosing an advisor within the multibillion dollar tax “advice” industry can be equally daunting. In early August, several individuals-near billionaires-testified before a Senate committee about being duped out of tens of millions of dollars in legal and accounting fees by their “blue-chip” advisors who set up fraudulent and worthless tax evasion schemes for them.

Clearly then, having a great CPA or tax lawyer for honest guidance is the most important step. But the role you can play is to understand the language of tax shelters and how to evaluate different strategies which may be presented to you. In this month’s column I’ll show you one way to make sense of shelters and present an illustration of a popular tax savings technique that can be used in a variety of circumstances.

Classifying Tax Shelters

The most clearly aggressive tax shelters are those specific transactions which the IRS has designated and listed as “Abusive.” These activities are those which hold a high potential for non-reporting of income and may involve offshore tax plans in which accounts and true ownership of entities can be easily concealed. Abusive Shelters are required to be fully disclosed on your tax returns and are likely to be subjected to a high degree of scrutiny. Many of the employee “health and welfare benefits” programs are similarly regarded. Unless you are prepared for years of litigation to defend your position, your tax planning should avoid these types of shelters.

At the other end of the spectrum are “Favored” shelters which are investments or vehicles encouraged by the Government to promote particular economic or social policies. Home ownership, retirement savings, oil and gas exploration and equipment purchases are

certainly in this category. Many of these transactions require little or no reporting, the techniques are widely known and approved and it is often sensible to work within these plans to the extent they are available to you.

Somewhere between “Abusive” and “Favored “ is the netherworld known as the “Grey Area” where tax attorneys and CPA’s toil endlessly to squeeze out the greatest advantages and tax savings for their clients. Strategies which reach deeply or too aggressively into the “Grey Area” are sometimes challenged or litigated by the IRS and the taxpayer may win or lose depending on the skill of his attorney and facts of the case.

Tax Benefits with the CRT

One strategy that has worked very well for many of my clients is known as the Charitable Remainder Trust (“CRT”) which has been a part of the tax law since 1969. The intent of the law is to encourage charitable giving but the law is drawn broadly so that even if your charitable wishes are only a minimal part of your overall goals, the CRT can produce highly favored tax treatment in a variety of situations.

In a nutshell, Section 664 of the Internal Revenue Code states that if you create a trust, with a charity as the ultimate beneficiary, the trust will not be subject to taxes on its income. You are permitted to receive payments and distributions from the CRT and contributed property can be sold by the trust without any tax. You also receive a current income tax deduction for the value of the charitable contribution.

Here’s an example of a CRT we recently finished. A physician client with a high income owned a medical office building worth \$2 million. He had paid only \$300,000 for it about 10 years earlier. Instead of selling it and paying capital gains tax, we formed a CRT and transferred the property to the trust. Based on the way the CRT was structured, he accomplished these results:

- 1) An income tax deduction of \$400,000, producing a tax savings of about \$200,000;
- 2) When the CRT sold the property, there was no capital gains tax on the appreciation;
- 3) The \$2 million proceeds in the CRT is managed and invested by the client and there are no taxes on the earnings of the investment portfolio;
- 4) Within certain parameters, we have the freedom to designate when and how much of the trust is distributed to the client and/or his spouse (and kids);
- 5) Any remaining amount in the CRT at the time of death is not subject to estate taxes;
- 6) Excellent asset protection is accomplished and property in the CRT is shielded from lawsuit risk.

There are many rules, traps and explanations which apply to any CRT. On this particular plan we stayed squarely within the “Favored” territory but depending upon the size the income tax deduction which is claimed and the timing of the distributions, it’s easy to move into the “Grey Area” and create some possibility for a dispute at a point in the future. As always, we urge you to consult with your tax advisor to determine the impact which any planning may have on your particular circumstances.

*Robert J. Mintz, JD, is an attorney and the author of the book **Asset Protection for Physicians and High-Risk Business Owners**. To receive a complimentary copy of the book call 800-223-4291 or visit www.rjmintz.com*