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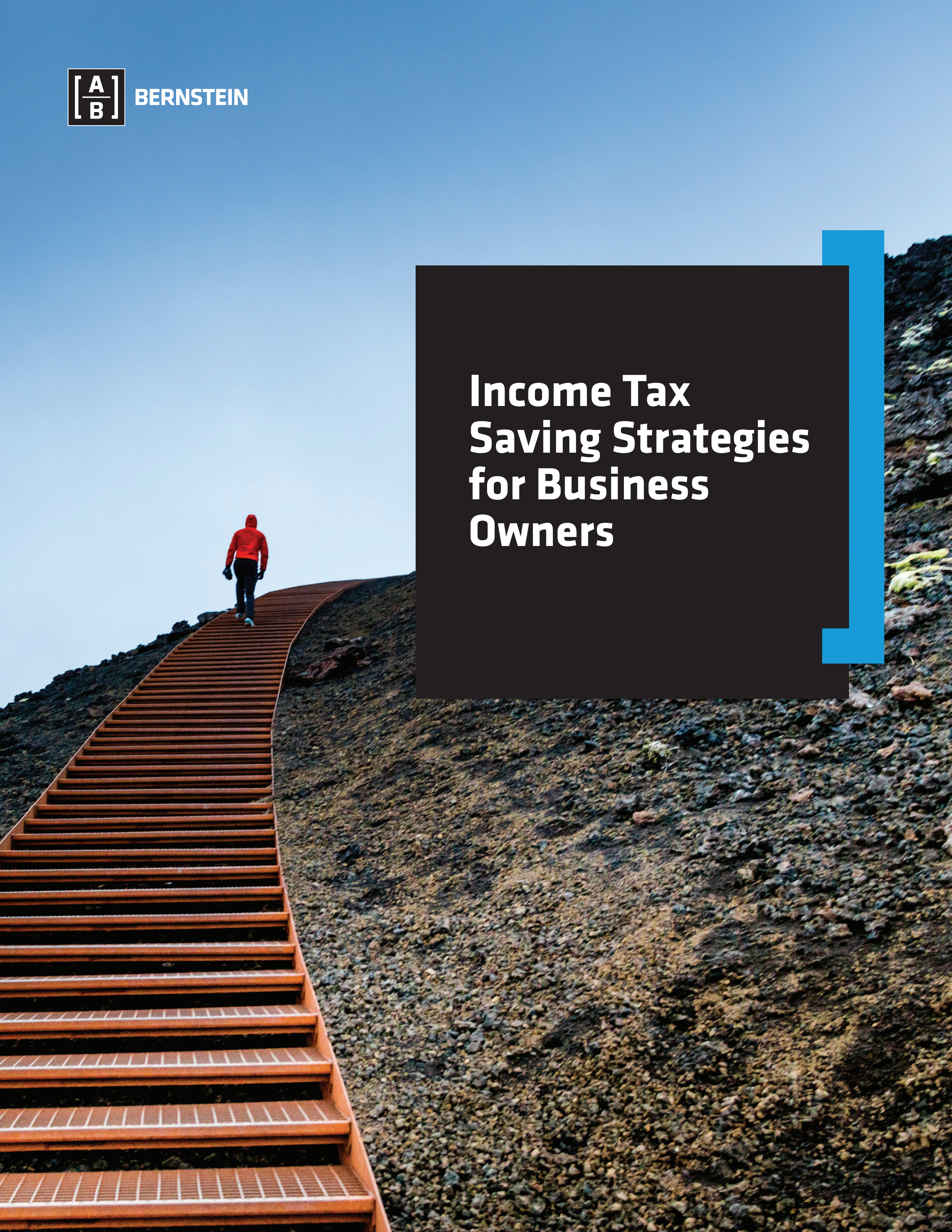
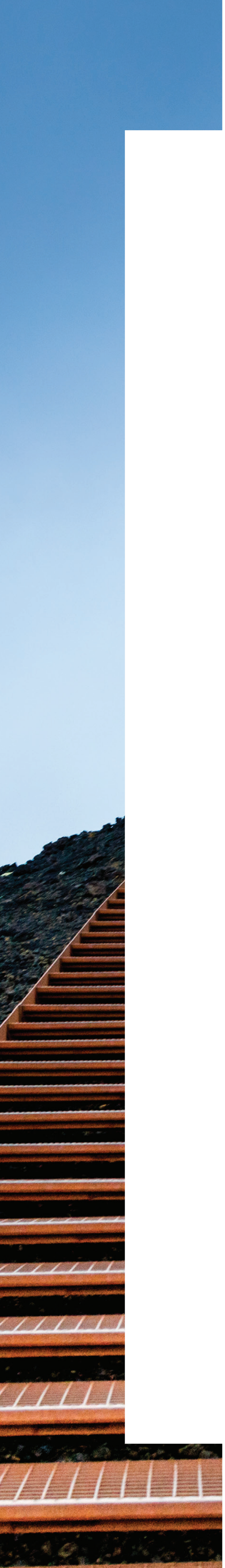


Income Tax Saving Strategies for Business Owners



A wide array of income tax saving options are available to business owners with the luxury and foresight to plan—provided they know where to look. The optimal strategy depends not only on the business owner's goals and objectives, but on obtaining expert advice well before a deal is on the table.

In part, the "right" approach depends on the circumstances. For instance, business owners who live in high-income-tax-rate states can avoid state tax by establishing a specialized trust in a jurisdiction with no income tax. What's more, business owners may sidestep $10 million or more of otherwise taxable gain for federal tax purposes (and potentially state income tax purposes as well[1]) if their ownership interest is qualified small business stock (QSBS) within the meaning of Section 1202 of the Internal Revenue Code.[2] In this paper, we'll explore both of these strategies in detail, as they tend to be underappreciated relative to their considerable tax-saving potential.

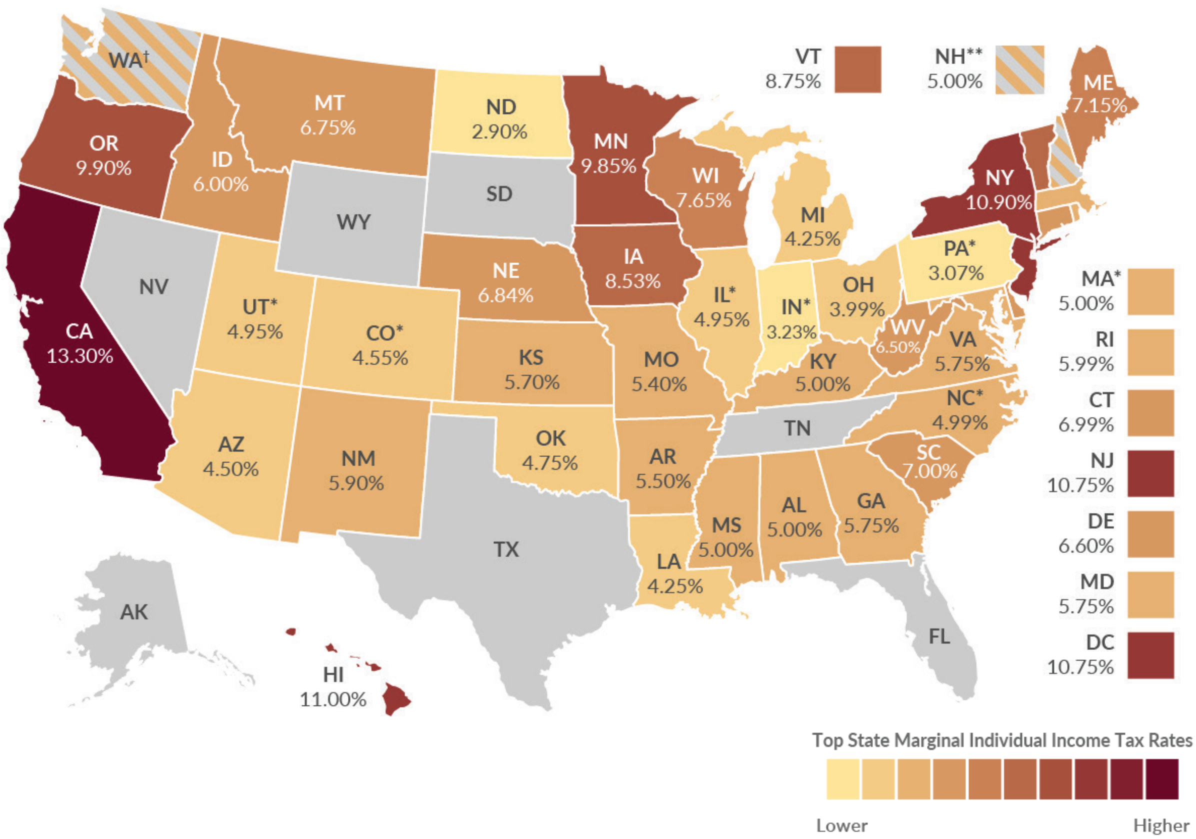
1 Not all states conform to Section 1202 which will still result in a state income tax liability on the sale of QSBS. As of this writing, California, Pennsylvania, New Jersey, Alabama, and Mississippi do not conform, while Hawaii and Massachusetts partially conform to Section 1202.
2 Within the meaning of Section 1202 of the Internal Revenue Code of 1986, as amended (hereinafter, "IRC").

Income Taxes: State of Play

Before diving in, note that income tax rates differ substantially from state to state. Some states—including Massachusetts, Utah, and Illinois—levy a flat income tax while others—Florida, Texas, and Nevada, for example—impose no state income tax at all. New Jersey and California, among others, have marginal percentage rates in the double digits, while others set their taxes at quite modest levels, comparatively speaking (**Display 1**).

DISPLAY 1: STATE INCOME TAXES DIFFER SIGNIFICANTLY FROM STATE TO STATE

Top Marginal State Individual Income Tax Rates (as of January 1, 2022)



Note: Map shows top marginal rates: the maximum statutory rate in each state. This map does not show effective marginal tax rates, which would include the effects of phase-outs of various tax preferences. Local income taxes are not included. Missouri's top marginal rate will be reduced to 5.3% if certain revenue triggers are met.
*State has flat income tax.
**State only taxes interest and dividend income.
Source: Bloomberg BNA; Tax Foundation; state tax statutes, forms, and constructions.

To mitigate state income taxes, some entrepreneurs may consider relocating to a lower-tax state. But changing one's tax domicile can be complicated, and the requirements vary state-by-state. And another option—qualified retirement plans or individual retirement accounts (IRAs)—generally disallow ownership interests in one's closely held business.

Instead, some entrepreneurs with deals in sight might consider an incomplete gift nongrantor (ING) trust. When properly implemented, this strategy eliminates state income taxes on sale proceeds, but it isn't for everyone. Ultimately, its appeal rests on careful structuring and a thorough understanding of the trade-offs. Let's explore in further detail.

DINGs, WINGs, and NINGs

Among the zero-income-tax states where an ING trust might be established are Delaware (DING), Nevada (NING), and Wyoming (WING). While these acronyms might sound like silverware hitting the floor, they're actually powerful tools for an eventual business exit. Whichever the jurisdiction, business owners can use these strategies to secure substantial state income tax savings—provided the trust is properly structured.[3]

How do ING trusts work? First, a business owner living in a high-tax-rate state (other than New York[4]) establishes a nongrantor trust—one that's treated as a separate taxpayer for income tax purposes—in a state that does not tax the trust's retained income (e.g., Delaware, Nevada, Wyoming, Tennessee). Notably, the trust must have two essential features:

- The gift must be "incomplete" so that the entrepreneur *is* treated as owning the trust assets for estate and gift tax purposes, and
- The trust must be a "nongrantor trust" so that the entrepreneur *isn't* treated as owning the trust assets for income tax purposes.

This combination allows the grantor to achieve a favorable state income tax outcome without making a taxable gift (**Display 2**).

DISPLAY 2: "INCOMPLETE" NONGRANTOR (ING) TRUSTS HINGE ON WHAT YOU OWN

"Incomplete"

Grantor owns trust assets for **estate and gift tax** purposes

"Nongrantor"

Grantor doesn't own trust assets for **income tax** purposes

Trust Powers: Knowing When to Hold or Fold

To ensure the transfer to the trust will be considered incomplete for **gift** tax purposes, the grantor must reserve sufficient power over the transferred assets. Typically, the grantor will retain a power to direct the trustee to distribute the trust's assets to others.[5] If properly structured, the mere existence of this "limited power of appointment" will make the grantor's gift to the trust incomplete. Relinquishment of the grantor's power of appointment would complete the gift; for that reason, in most cases, the power will remain in effect during the grantor's lifetime.

For **income** tax purposes, limitations on the grantor's ability to receive distributions of trust assets help ensure qualification as a nongrantor trust.[6] Among other provisions, the trust instrument typically will prohibit any distribution to the grantor without consent of a "distribution committee" consisting of a subset of, or all, current beneficiaries.

If the trust meets both requirements—the gift to the trust is incomplete, but the trust is not a grantor trust—then **undistributed** trust income should avoid state income tax, while distributed income will be subject to income tax in the beneficiary's home state. Either way, an ING trust is still subject to federal income tax (whether income is accumulated in the trust or distributed to beneficiaries). And, if income is accumulated, the trust must pay those federal income taxes under highly compressed trust tax brackets.

3 Trust income tax laws vary from state to state, so state income tax savings may not be achieved in every situation. For example, some states assert the right to tax a trust forever if the grantor was a resident of that state at the time the trust became irrevocable.
4 New York treats an ING trust established by a resident as a grantor trust for state income tax purposes; other states, including California, are considering similar legislation.
5 Treas. Reg. Sec. 25.2511-2(b).
6 See Sections 671-679 of the Internal Revenue Code.

Case Study: Exploring Exit Options

Consider the Riveras, a 60-year-old couple planning to sell their business for $30 million. For our purposes, we'll assume they live in a (fictional) state that imposes an income tax at a flat rate of 10%. Like many entrepreneurs, most of their wealth is tied up in their business. However, they have set aside $2.5 million in marketable investments, including a $1.5 million retirement account. While they enjoy living in their current state, the prospect of losing 10% (i.e., $3 million) of their sale proceeds to state and local taxes concerns them. The Riveras want to maximize their after-tax proceeds since they'll rely on those funds to sustain their annual living expenses of $250,000, adjusted for inflation, over their lifetimes. Could an ING trust provide a meaningful tax benefit? Or would forgoing that income tax benefit and establishing a spousal lifetime access trust (SLAT) instead prove more effective?

To answer these questions, let's analyze four different scenarios:

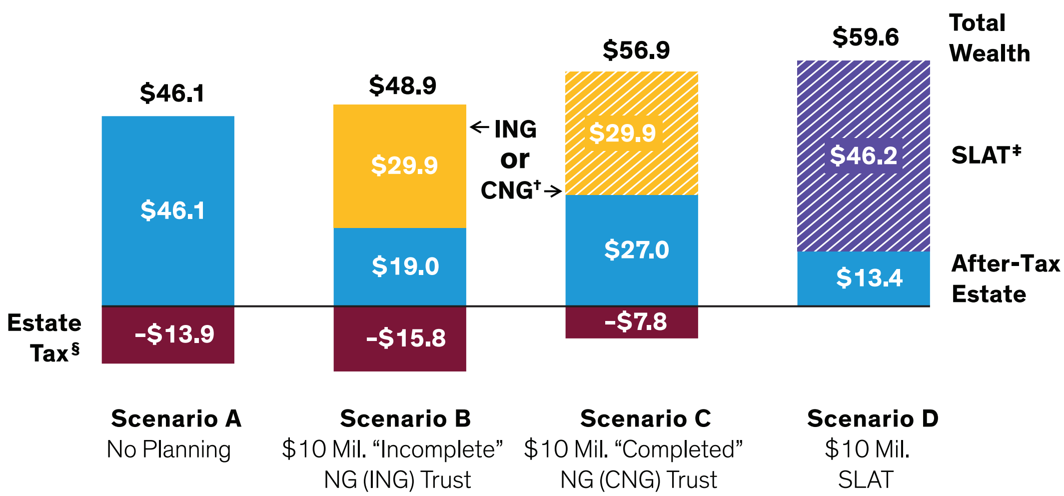
	Scenario A	Scenario B	Scenario C	Scenario D
Assumptions	• No tax planning prior to the sale	• One spouse gives $10 million of their business interest to an ING trust prior to the sale	• One spouse gives $10 million of their business interest to nongrantor trust, in a tax-favored state, prior to the sale as a completed gift	• One spouse gives $10 million of their business interest to a SLAT for the benefit of the other spouse and their descendants
Strategy	• Sell the business for $30 million • Pay a $9 million income tax liability* • Reinvest the remaining $21 million in an 80%/20% portfolio of global stocks and bonds	• Riveras personally receive $14 million, net of federal, state, and local tax • ING Trust receives $7.63 million, net of just federal tax† • Saves $620,000 in state and local income taxes	• Riveras personally receive $14 million, net of federal, state, and local tax • Nongrantor trust receives $7.63 million, net of just federal tax† • Saves $620,000 in state and local income taxes • Trust assets will be excluded from the Riveras' taxable estate as neither spouse is a beneficiary of the trust	• The SLAT essentially reverses the tax effects of the ING trust • Grantor is treated as owner for federal, state, and local income tax purposes, but **not** for estate and gift tax purposes • Riveras pay the entire $9 million tax liability from the sale • Receive $11 million personally and $10 million in the SLAT

*Taxes were calculated assuming all $30 million will be subject to a 30% tax rate (20% federal long-term capital gain plus a 10% state rate). As the Riveras were active owners, they were not subject to the 3.8% net investment income tax.
†As the trustee of the ING would not generally be an active owner of the business, we assumed that the proceeds the ING received would be subject to the 3.8% net investment income tax, in addition to a 20% long-term capital gains tax.

The results of our model surprised the Riveras (**Display 3**). They can clearly sustain their lifestyle for 30 years, but in the absence of any planning, will likely owe significant estate taxes at the second death (Scenario A). Giving $10 million to an ING (Scenario B) achieves a somewhat better outcome by generating an immediate state income tax savings of $620,000. But that extra savings increases the size of their taxable estate, which drives their future estate tax liability higher. Conversely, a $10 million completed gift to a non-ING trust (Scenario C) not only saves them $620,000 in income taxes but also removes future growth of the trust's assets from their estate for federal estate tax purposes.

DISPLAY 3: THE NONGRANTOR TRUSTS CREATE AN IMMEDIATE INCOME TAX SAVINGS WHILE THE "COMPLETED" GIFT AND SLAT CREATE ESTATE TAX SAVINGS

Projected Wealth—Year 30 (Nominal, USD Million)*
Assuming Current Estate Tax Laws



Increase in Total Wealth	**$2.8**	**$10.8**	**$13.5**

In Estate **Out of Estate**

*Values assume initial assets of $2.5 million, pretax sale proceeds of $30 million in year 1 with a cost basis of zero and annual spending of $250,000, adjusted for inflation. All scenarios assume the assets are invested with an asset allocation of 80% global stocks and 20% bonds, and that all assets with the exception of the assets in the nongrantor trusts are subject to a state tax rate of 10%. Projections assumed the transaction was structured as a stock sale, not an asset sale, and that no state-sourced income from grantors home state was realized.
†Assumes $10 million is transferred to an "incomplete" nongrantor trust (ING) or a "completed" nongrantor trust (CNG). In both cases, the trust will be structured where it will only pay federal taxes on the income generated by the trust. The CNG is a completed gift and is out of the grantor's estate for estate tax purposes.
‡The SLAT is assumed to be funded with $10 million and that the grantor will pay the taxes on the trust for the first 20 years of the analysis, thereafter the trust will pay its own taxes.
§Estate taxes were calculated assuming a federal rate of 40% and that the lifetime exemption sunsets back to $6.03 million per person, adjusted for inflation. It is assumed that one spouse used $10 million of their lifetime exemption to make the completed gift or to fund the SLAT in scenarios C and D. The values do not account for any benefit from a step-up in cost basis.
Projections based on AB's estimates of the range of returns for the applicable capital markets over the periods analyzed. **Data do not represent past performance and are not a promise of actual future results or a range of future results.** Bernstein does not provide tax or legal advice; investors should consult tax and legal professionals before making any decisions. See Notes on the Bernstein Wealth Forecasting System in Appendix for further details.

Lastly, and perhaps unexpectedly, the SLAT (Scenario D) confers the greatest benefit of all: While the SLAT yields no income tax savings, the family's wealth is significantly enhanced by shifting federal, state, and local income taxes from the trust to the Riveras personally. This depletes their estate and, in this case, completely eliminates their potential estate tax liability. The savings is mainly due to the grantor's ability to pay the SLAT's income taxes without those payments being treated as additional gifts to the trust for federal gift tax purposes.[7] Without this income tax burden, the SLAT accumulates $16.3 million more wealth than the taxable trusts (Scenarios B and C) over a 30-year period. All in all, the family is better off by $13.5 million (29% more wealth) after 30 years compared to the "no planning" scenario.

7 Rev. Rul. 2004-64, 2004-2 C.B. 7, 2004.

An Optimal Solution?

In general, establishing an ING trust makes the most sense when the grantor:

- Lives in a high-income-tax-rate state;
- Is in the top-marginal-income-tax bracket for federal income tax purposes;
- Has already used her or his full federal gift and estate tax exclusion ($12.92 million in 2023); and
- Has appreciated assets (like business interests) to contribute that would benefit from a step-up in cost basis at the grantor's death.

Before proceeding, there are several considerations that business owners and their professional advisors must weigh, including:

1. **Availability**: This strategy may not be legally available in the entrepreneur's state of residence. Some states assert the right to tax tangible assets (e.g., real estate, businesses), notwithstanding ownership by an out-of-state trust. As mentioned previously, at least one state (New York) treats an ING trust established by a resident as a grantor trust for state income tax purposes. Other states may follow.
2. **Trade-Offs**: As the case study shows, an ING trust can provide substantial income tax savings on an initial sale, but (i) will require the trust to be taxed at extremely condensed federal income tax brackets on undistributed income; and (ii) will not provide any estate tax relief.
3. **Oversight**: An ING trust requires an individual or corporate trustee domiciled in the tax-favored state. A corporate trustee charges administration fees, which must be factored into the strategy's net value. After sale of the business, the ING trust's future federal income taxes may be mitigated by (i) distributing, rather than retaining, trust accounting income; and (ii) adopting tax-efficient investment strategies, such as tax-loss harvesting, and "wrapping" high-returning, tax-inefficient investments in one or more low-cost private placement life insurance (PPLI) policies.

QSBS Can Also Lead to Big Savings

Most entrepreneurs—whether they live in a high-state-income-tax-rate jurisdiction or not—place a high priority on reducing the tax burden of an eventual business sale. Yet, tax planning prior to a business sale can be complicated. The more lead time owners have before closing, the more options they can preserve. Those who own stock in a closely held C corporation should determine, at a minimum, whether their ownership interest meets the statutory definition of QSBS under Section 1202 of the Internal Revenue Code.

Qualifying for QSBS: An "Exclusive" Club

For stock to be considered QSBS (**Display**), it must be or have been:

1. Issued by a domestic C corporation
2. Granted by a company that conducts an "active" business for substantially all the owner's holding period
3. Received when the aggregate value of the company's gross assets was less than $50 million
4. Held for more than five years
5. Granted by a company that conducts a "qualified" business within the meaning of the statute.

QSBS Eligibility at a Glance

Corporate Structure	Domestic C corporation only
Active Trade or Business	Any trade or business other than: • Service Business • Banking/Insurance/Leasing • Investment Management • Farming/Mining/Oil & Gas Extraction • Hotels/Motels/Restaurants
Gross Assets	Less than $50 million in gross assets between business formation and immediately after stock issuance
Issuance	• Stock must be issued when corporation is deemed a qualified small business • Stock must be issued directly from the company and received by a non-corporate taxpayer (e.g., individuals, pass-through entities, trusts)

Source: AllianceBernstein (AB)

8 See IRC § 1202(h)(1), (2)(A),(B).

Even those with a working knowledge of QSBS may not fully appreciate its potential. For instance, with appropriate pre-transaction planning, exiting owners may qualify for additional $10 million exclusions. How? If a gift of QSBS is made to another taxpayer—such as a family member or perhaps a nongrantor trust—that stock retains its "original issuance" status and is therefore eligible for its own $10 million exclusion, assuming all other statutory requirements are met.[8] As you are about to see, this ability to "stack" multiple QSBS exclusions can be a very powerful strategy.

Multiplying the QSBS Exclusion

Let's revisit the Riveras, who "winged" their way to considerable state tax savings earlier. They still plan to sell their business for $30 million, but this time we'll assume their company was structured as a C corporation—rather than a limited liability company taxable as a partnership—when it was first established. As they contemplate their goals, the couple remains intent on securing $250,000 of annual, inflation-adjusted spending while minimizing income and estate taxes.

Since the Riveras structured their business as a C corporation, held their shares for more than five years, and met all other requirements of Section 1202, their stock qualifies as QSBS. That means they can exclude $10 million of gain from the sale of their business, netting them $3.4 million[9] in tax savings.

Could they do better? Our analysis explores several scenarios:

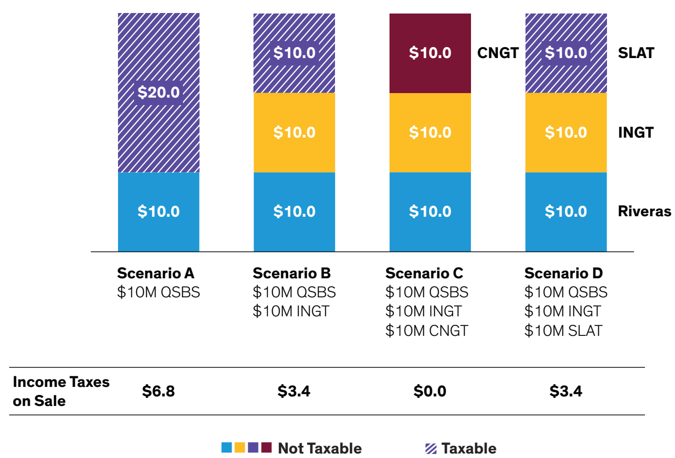
- **Scenario A**: No additional planning; the Riveras exclude only $10 million of gain.
- **Scenario B**: The couple gives a $10 million stake in their business to an ING trust. As a separate taxpayer, the ING trust should be entitled to its own $10 million QSBS exclusion, saving an additional $3.4 million in income taxes. Yet the "incomplete" nature of the gift means that the assets held in trust will still be subject to estate tax at the grantor's death.
- **Scenario C**: Mirrors Scenario B, except prior to the sale, the couple also makes a "completed" gift of $10 million worth of shares in the business to a separate nongrantor (CNG) trust. This hybrid strategy should shield all $30 million of gain from income tax. In addition, assets held in the CNG trust at the grantor's death should avoid estate tax.
- **Scenario D**: Mirrors Scenario B, except the Riveras also give $10 million to a SLAT. Because a SLAT is almost always a grantor trust, the grantor must pay all income taxes attributable to the SLAT's assets—including any gain recognized on the sale of the business. As a result, the SLAT is not entitled to a separate $10 million QSBS exclusion. However, assets held in the SLAT will not be subject to estate tax at the grantor's death, and the continuing obligation to pay income taxes on behalf of the trust and its beneficiaries will deplete the Riveras' estate for estate tax purposes.

Quantifying the Outcomes

Upon seeing our analysis, the Riveras were taken aback when they compared the amount of sale proceeds subject to income tax under each scenario (**Display 4**, top section of each bar). Scenario C, in particular, stood out. Multiplying the QSBS exclusion through nongrantor trusts provides immediate income tax savings on the sale—but Scenario C layered on an even more significant estate tax benefit by structuring the second nongrantor trust as a CNG trust. Essentially, by making both completed and incomplete gifts to nongrantor trusts, the couple can avoid all income tax arising from their exit.

DISPLAY 4: HOW THE QSBS WILL BE "STACKED" WITH VARIOUS TRUSTS

Based on a $30.0 Million Sale*



*Values assume that the sale qualifies for QSBS tax treatment where the Riveras can exclude $10 million of gains. All non-eligible QSBS are subject to a 33.8% tax rate (23.8% federal + 10% state). It is assumed that the incomplete nongrantor trusts (INGT) and the completed nongrantor trust (CNGT) will also be able to exclude $10 million of proceeds from taxation but the spousal lifetime access trust (SLAT) will not avoid any income taxes.

9 For purposes of this analysis, we assume that the Riveras reside in a state that conforms to IRC Section 1202 and that eligible gain avoids state income tax at a "flat" rate of 10%.
10 On several occasions, most recently in the Biden administration's "greenbook" of Fiscal Year 2023 tax reform proposals, the Democrats have proposed to curtail or eliminate many of the estate planning benefits of grantor trusts, including, for example, a proposal to treat the grantor's payment of income taxes on behalf of the trust and its beneficiaries as taxable transfers for federal gift tax purposes. See Department of the Treasury, General Explanations of the Administration's Fiscal Year 2023 Revenue Proposals, at 42 (March 2022); cf. Rev. Rul. 2004-64, 2004-27 I.R.B. 7 (treating such payments as true obligations, not gifts).

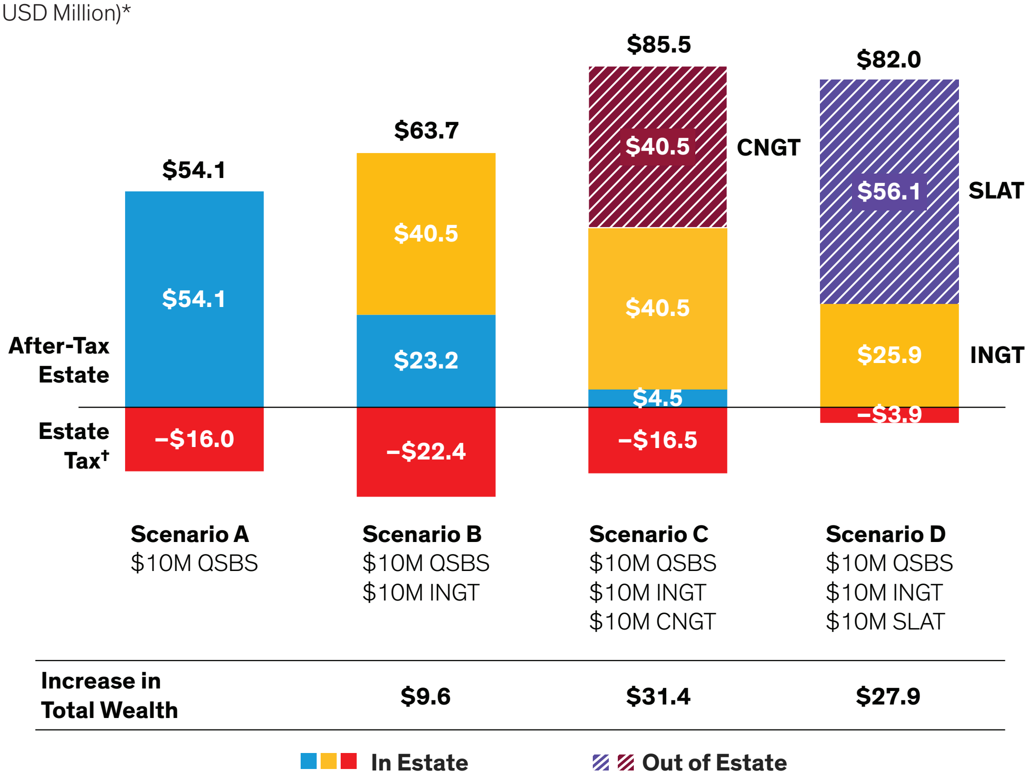
Did the SLAT (Scenario D) add any value? Perhaps surprisingly, not as much as the CNG trust (**Display 5**). That's because a SLAT provides no separate QSBS benefit. And at $85.5 million, the net assets the couple would have accumulated in 30 years under Scenario C exceed the $82.0 million in the SLAT (Scenario D) by about 4%—without having to rely on another three decades of favorable grantor trust laws.[10]

CRUTs Help Overcome the Loss of Control

Although the prospect of completely sidestepping income taxes appealed to the Riveras, they were uncomfortable making irrevocable gifts that could considerably restrict their use and enjoyment of the assets. Could these entrepreneurs capture an additional $10 million QSBS exclusion without forgoing future access?

DISPLAY 5: CONTINUING TO PAY TAXES ON THE SLAT DOES NOT OVERCOME THE BENEFIT OF MULTIPLYING THE QSBS EXCLUSION

Projected Wealth After Estate Taxes—Year 30
(Nominal, USD Million)*



*Values assume initial assets of $2.5 million, pretax sale proceeds of $30 million in year 1 with a cost basis of zero, and annual spending of $250,000, adjusted for inflation. All scenarios assume the assets are invested with an allocation of 80% global stocks and 20% bonds, and that all portfolio income would be subject to top marginal federal taxes and a state rate of 10%. "$10M QSBS" assumed the owner's business qualifies for the IRS Section 1202 Qualified Small Business Stock (QSBS) election where $10 million of the gains can be excluded from federal taxes. In scenarios B, C, and D, we assumed the owner gave $10 million worth of the stock to an incomplete nongrantor trust (INGT) that would receive its QSBS exclusion. In scenario C, we assumed the owners gave $10 million to a completed nongrantor trust (CNGT) that would receive its own $10 million exclusion. In scenario D, we assumed the $10 million gift to the SLAT would not receive any income tax benefit from the sale, but we assumed the grantor will pay taxes on the trust each year of the analysis from their assets and if depleted, then INGT.
†Estate taxes were calculated assuming a federal rate of 40% and that the lifetime exemption sunsets back to $6.03 million per person, adjusted for inflation. It is assumed that one spouse used $10 million of their lifetime exemption to fund the SLAT and the CNGT. The values do not account for any benefit from a step-up in cost basis.
Projections based on AB's estimates of the range of returns for the applicable capital markets over the periods analyzed. **Data do not represent past performance and are not a promise of actual future results or a range of future results.** Bernstein does not provide tax or legal advice; investors should consult tax and legal professionals before making any decisions. See Notes on the Bernstein Wealth Forecasting System in Appendix for further details.

11 The income tax charitable deduction is not the total amount contributed, but rather the present value of what is expected to pass to charity at the end of the noncharitable term of the trust. The present value calculation takes into account the value of the contributed assets, the discount rate (based on the applicable "Section 7520 rate"), and the noncharitable term of the trust (either a fixed term of years, or for lifetime trusts, a life expectancy table is used). See IRC §§ 664, 7520, and the applicable Treasury regulations thereunder.

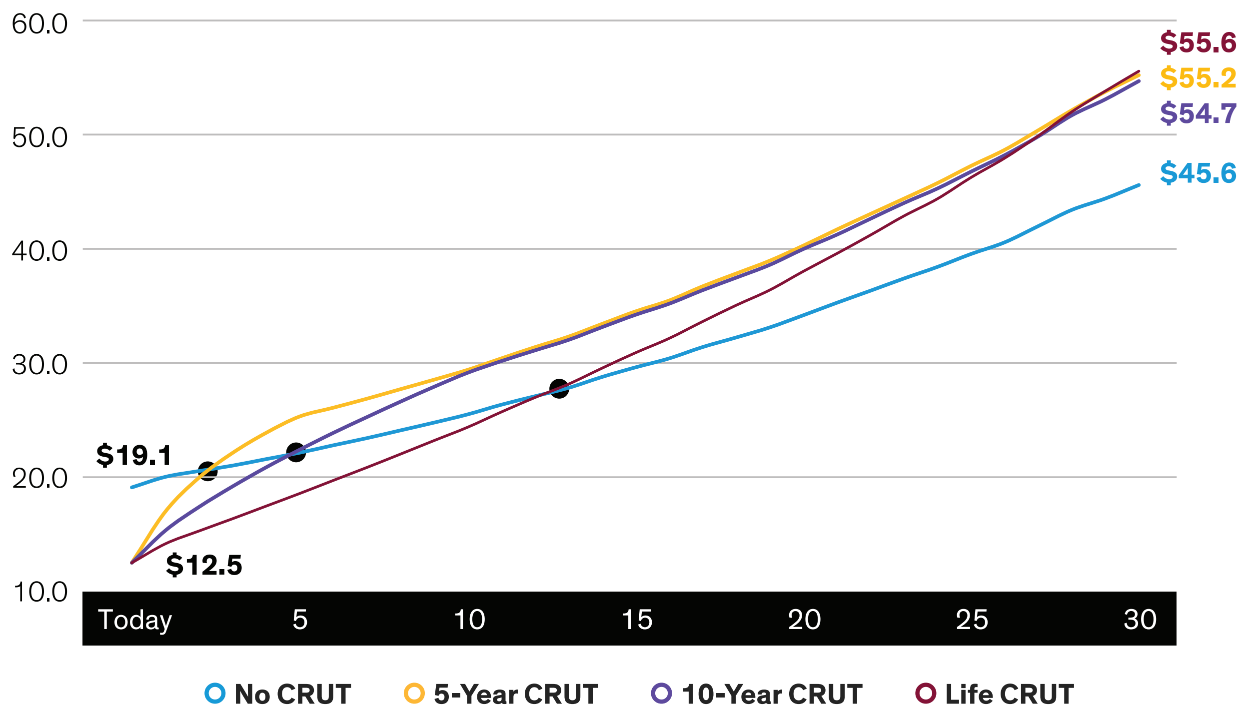
One potential solution may be contributing $10 million of shares to a charitable remainder unitrust (CRUT). In exchange, the couple would receive an upfront income tax charitable deduction for a portion of the value contributed.[11] They would also retain the right to receive a fixed percentage of the fair market value of the CRUT's assets each year (a "unitrust" distribution) for a set term or for life.

Since a CRUT is tax-exempt, the sale proceeds should not be taxed immediately. Instead, periodic distributions will be taxed to the Riveras based on certain "tiered" rules of accounting[12] where the highest-taxed tranches are deemed to be paid out first. If the CRUT qualifies for a separate QSBS exclusion, $10 million of gain should avoid taxation. On the other hand, if the CRUT is not treated as a separate taxpayer for QSBS purposes, then that $10 million of deferred gain will be taxable to the Riveras over the noncharitable term, which could stretch over their joint lifetimes.

This sounded compelling to the Riveras. They would retain access to the sale proceeds via distributions from the CRUT, while the CRUT may be eligible for its own $10 million exclusion. But since the CRUT pays only a fixed percentage each year, it will take time for those accumulated distributions to exceed the amount the couple would have amassed otherwise. How long? The answer depends on the trust term and payout percentage.

DISPLAY 6: HOW LONG DOES IT TAKE FOR THE CRUT TO PROVIDE A BENEFIT?

Accumulated Personal Wealth (USD Million, Nominal)*
Current Tax Law—$10 million QSBS Contributed to CRUT



*Crossover is defined as the point at which one accumulates more personal wealth by creating the CRUT than by selling and diversifying without the CRT. It is assumed that all payouts received from the CRUT are reinvested in a taxable portfolio with an asset allocation of 80% global stocks and 20% bonds. All portfolio income is assumed to be subject to top marginal federal tax rates. The values above do not reflect the assets inside the nongrantor trust. The 5-year CRUT is modeled with a payout of 37.5%, the 10-year CRUT is modeled with a payout of 20.9%, and the Life CRUT is modeled with a payout of 9.3%. Values assume the CRUT is eligible to receive a $10.0 million QSBS exclusion. Based on Bernstein's estimates of the range of long-term returns for the applicable capital markets. **Data does not represent past performance and is not a promise of actual or range of future results.** See Notes on the Bernstein Wealth Forecasting System in Appendix for further details.

12 IRC § 664(b); Treas. Reg. Section 1.664-1(d)(1)

If the CRUT qualifies as a separate taxpayer for QSBS purposes, we project that it will take roughly three years for a CRUT with a five-year term and a 37.5% unitrust payout to generate more personal wealth than our "No CRUT" base case (**Display 6**). By comparison, it would take 13 years for a joint-life CRUT with a unitrust payout of 9.3% to surpass the personal wealth generated in our base scenario. Interestingly, the Riveras end up with nearly the same amount of wealth in 30 years—irrespective of the term—and nearly $10 million more than not using the CRUT at all.

Clearly, the CRUT creates more wealth if it captures an additional $10 million exclusion that will be paid out over time. Although CRUTs are typically designed to stretch the payouts to maximize tax deferral, the opposite may hold true for QSBS-funded CRUTs since there is no (or substantially lower) realized gain to be deferred. The Riveras aim to qualify the recipient trust as a separate taxpayer for QSBS purposes, while receiving $10 million of tax-free income as quickly as possible.

A note of caution: If the CRUT fails to qualify for a separate QSBS exclusion—or if future tax laws eliminate or reduce the QSBS benefit—a longer noncharitable term generally will prove more protective of the Riveras' personal wealth. A needs-based analysis can help quantify the trade-offs, and thereby mitigate those risks.

Entrepreneurs Have Options—If They Know Where to Look

Business owners have multiple tax-saving alternatives available to them in advance of a sale, but most strategies require considerable lead time to analyze and put into effect. The best advice for any business owner contemplating an eventual sale is to involve professional advisors early in the process. Once those advisors gain a better understanding of the owner's hopes and aspirations, they can build a custom plan that maximizes the proceeds of sale.

Notes on the Bernstein Wealth Forecasting System℠

1. Purpose and Description of the Bernstein Wealth Forecasting System

AB's Wealth Forecasting Analysis is designed to assist investors in making their long-term investment decisions as to their allocation of investments among categories of financial assets. Our planning tool consists of a four-step process: (1) Client-Profile Input: the client's asset allocation, income, expenses, cash withdrawals, tax rate, risk-tolerance level, goals and other factors; (2) Client Scenarios: in effect, questions the client would like our guidance on, which may touch on issues such as when to retire, what his/her cash-flow stream is likely to be, whether his/her portfolio can beat inflation long-term, and how different asset allocations might impact his/her long-term security; (3) The Capital-Markets Engine: our proprietary model that uses our research and historical data to create a vast range of hypothetical market returns, which takes into account the linkages within and among the capital markets, as well as their unpredictability; and finally (4) A Probability Distribution of Outcomes: based on the assets invested pursuant to the stated asset allocation, 90% of the estimated ranges of probable returns and asset values the client could experience are represented within the range established by the 5th and 95th percentiles on "box-and-whiskers" graphs. However, outcomes outside this range are expected to occur 10% of the time; thus, the range does not guarantee results or establish the boundaries for all outcomes. Estimated market returns on bonds are derived taking into account yield and other criteria. An important assumption is that stocks will, over time, outperform long bonds by a reasonable amount, although this is in no way a certainty. Moreover, actual future results may not meet AB's estimates of the range of market returns, as these results are subject to a variety of economic, market and other variables. Accordingly, the analysis should not be construed as a promise of actual future results, the actual range of future results or the actual probability that these results will be realized. The information provided here is not intended for public use or distribution beyond our private meeting. Of course, no investment strategy or allocation can eliminate risk or guarantee returns.

2. Retirement Vehicles

Each retirement plan is modeled as one of the following vehicles: Traditional IRA, 401(k), 403(b), Keogh, or Roth IRA/401(k). One of the significant differences among these vehicle types is the date at which mandatory distributions commence. For traditional IRA vehicles, mandatory distributions are assumed to commence during the year in which the investor reaches the age of 70.5. For 401(k), 403(b), and Keogh vehicles, mandatory distributions are assumed to commence at the later of (i) the year in which the investor reaches the age of 70.5 or (ii) the year in which the investor retires. In the case of a married couple, these dates are based on the date of birth of the older spouse. The minimum mandatory withdrawal is estimated using the Minimum Distribution Incidental Benefit tables as published on www.irs.gov. For Roth IRA/401(k) vehicles, there are no mandatory distributions. Distributions from Roth IRA/401(k) that exceed principal will be taxed and/or penalized if the distributed assets are less than five years old and the contributor is less than 59.5 years old. All Roth 401(k) plans will be rolled into a Roth IRA plan when the investor turns 59.5 years old to avoid Minimum Distribution requirements.

3. Rebalancing

Another important planning assumption is how the asset allocation varies over time. We attempt to model how the portfolio would actually be managed. Cash flows and cash generated from portfolio turnover are used to maintain the selected asset allocation between cash, bonds, stocks, REITs and hedge funds over the period of the analysis. Where this is not sufficient, an optimization program is run to trade off the mismatch between the actual allocation and targets against the cost of trading to rebalance. In general, the portfolio allocation will be maintained reasonably close to its target. In addition, in later years, there may be contention between the total relationship's allocation and those of the separate portfolios. For example, suppose an investor (in the top marginal federal tax bracket) begins with an asset mix consisting entirely of municipal bonds in his/her personal portfolio and entirely of stocks in his/her retirement portfolio. If personal assets are spent, the mix between stocks and bonds will be pulled away from targets. We put primary weight on maintaining the overall allocation near target, which may result in an allocation to taxable bonds in the retirement portfolio as the personal assets decrease in value relative to the retirement portfolio's value.

4. Expenses and Spending Plans (Withdrawals)

All results are generally shown after applicable taxes and after anticipated withdrawals and/or additions, unless otherwise noted. Liquidations may result in realized gains or losses, which will have capital-gains tax implications.

5. Modeled Asset Classes

The following assets or indexes were used in this analysis to represent the various model classes:

Asset Class	Modeled as:	Annual Turnover Rate
Municipal Cash	Municipal money-market securities	100%
Cash Equivalents	3-month Treasury bills	100%
Intermediate-Term Diversified Municipals	AA-rated diversified municipal bonds of 7-year maturity	30%
Intermediate-Term Taxables	Taxable bonds with maturity of 7 years	30%
US Diversified	S&P 500 Index	15%
US Value	S&P/Barra Value Index	15%
US Growth	S&P/Barra Growth Index	15%
US Low Vol Equity	MSCI US Minimum Volatility Index	15%
Developed International	MSCI EAFE Unhedged	15%
Emerging Markets	MSCI Emerging Markets Index	20%
US SMID	Russell 2500	15%
High-Risk Intl	Country Fund	15%
Global Intermediate Taxable Bonds Hedged	7-year 50% Sovereign and 50% Investment Grade Corporate Debt of Developed Countries	30%

6. Volatility

Volatility is a measure of dispersion of expected returns around the average. The greater the volatility, the more likely it is that returns in any one period will be substantially above or below the expected result. The volatility for each asset class used in this analysis is listed on the Capital-Market Projections page at the end of these Notes. In general, two-thirds of the returns will be within one standard deviation. For example, assuming that stocks are expected to return 8.0% on a compounded basis and the volatility of returns on stocks is 17.0%, in any one year it is likely that two-thirds of the projected returns will be between (8.9)% and 28.8%. With intermediate government bonds, if the expected compound return is assumed to be 5.0% and the volatility is assumed to be 6.0%, two-thirds of the outcomes will typically be between (1.1)% and 11.5%. AB's forecast of volatility is based on historical data and incorporates AB's judgment that the volatility of fixed-income assets is different for different time periods.

7. Technical Assumptions

AB's Wealth Forecasting System is based on a number of technical assumptions regarding the future behavior of financial markets. AB's Capital Markets Engine is the module responsible for creating simulations of returns in the capital markets. These simulations are based on inputs that summarize the current condition of the capital markets as of December 31, 2020. Therefore, the first 12-month period of simulated returns represents the period from December 31, 2020, through December 31, 2021, and not necessarily the calendar year of 2020. A description of these technical assumptions is available on request.

8. Tax Implication

Before making any asset allocation decisions, an investor should review with his/her tax advisor the tax liabilities incurred by the different investment alternatives presented herein including any capital gains that would be incurred as a result of liquidating all or part of his/her portfolio, retirement-plan distributions, investments in municipal or taxable bonds, etc. AB does not provide tax, legal, or accounting advice. In considering this material, you should discuss your individual circumstances with professionals in those areas before making any decisions.

9. Tax Rates

The federal income tax rate represents AB's estimate of either the top marginal tax bracket or an "average" rate calculated based upon the marginal rate schedule. The federal capital gains tax rate is represented by the lesser of the top marginal income tax bracket or the current cap on capital gains for an individual or corporation, as applicable. Federal tax rates are blended with applicable state tax rates by including, among other things, federal deductions for state income and capital gains taxes. The state income tax rate represents AB's estimate of the "average" rate calculated based upon the applicable state's marginal tax schedule. Where an applicable state tax code permits the exclusion of a portion of capital gain income from gross income for purposes of calculating state income tax such exclusions have been included in the calculation.

10. Intentionally Defective Grantor Trusts (IDGTs)

The Intentionally Defective Grantor Trust (IDGT) is modeled as an irrevocable trust whose assets are treated as the grantor's for income tax purposes, but not for gift or estate tax purposes. Some income and transfer-tax consequences associated with transfers to and the operation of an IDGT remain uncertain, and the strategy may be subject to challenge by the IRS. Hence, this technique requires substantial guidance from tax and legal advisors. The grantor may give assets to the trust, which will require using gift tax exemptions or exclusions, or paying gift taxes. The IDGT is modeled with one or more current beneficiaries, and one or more remainder beneficiaries. Distributions to the current beneficiaries are not required, but the system permits the user to structure annual distributions in a number of different ways, including 1) an amount or a percentage of fiduciary accounting income (FAI) (which may be defined to include some or all realized capital gains); 2) FAI plus some principal, expressed either as a percentage of trust assets or as a dollar amount; 3) an annuity, or fixed-dollar amount, which may be increased annually by inflation, or by a fixed percentage; 4) a unitrust, or annual payment of a percentage of trust assets, based on the trust's value at the beginning of the year, or average over multiple years; or 5) any combination of the above four payout methods. Because the IDGT is modeled as a grantor trust, the system calculates all taxes on income and realized capital gains that occur in the IDGT portfolio each year, based on the grantor's tax rates and other income, and pays them from the grantor's personal portfolio. The IDGT may continue for the duration of the analysis, or the trust assets may be distributed in cash or in kind at a specific point in time or periodically to (1) a non-modeled recipient, (2) a taxable trust, or (3) a taxable portfolio for someone other than the grantor. If applicable, an installment sale to an IDGT may be modeled as a user-entered initial "seed" gift followed by a sale of additional assets to the trust. The system will use one of two methods to repay the value of the sale assets plus interest (less any user-specified discount to the grantor): 1) user-defined payback schedule, or 2) annual interest-only payments at the applicable federal rate (AFR) appropriate for the month of sale and the term of the installment note, with a balloon payment of principal plus any unpaid interest at the end of the specified term.

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BPWM-331817-2022-12-22
BER-1985-0123
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