



Robert W. Wood

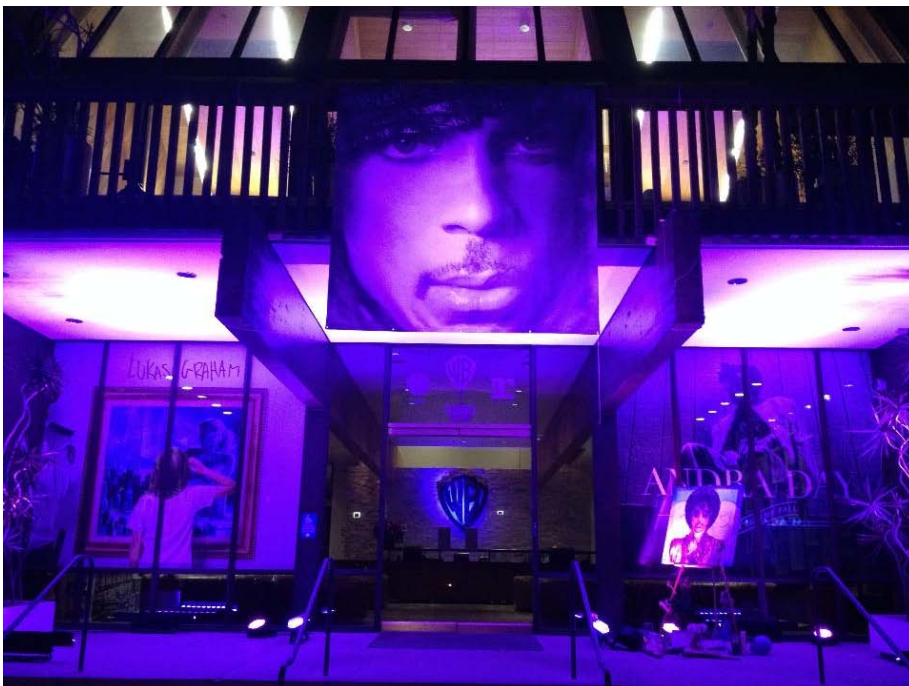
THE TAX LAWYER

TAXES 5/17/2016

Prince Estate Lawsuits Have Silver Lining: Tax Savings

Prince [died without a will](#). Among other things, that makes it even more likely that the estate will face lawsuits by claimants who hope to collect a piece of [Prince's vast estate](#). A well organized estate (with a trust to avoid probate) can usually be kept private. A simple will—or as in Prince's case, no will at all—means probate. The probate process is public and expensive. And it can invite disputes. Already, the first paternity lawsuit looms.

Carlin Q. Williams, a 39-year-old inmate in federal prison, claims to be Prince's son. He says his mother Marsha Henson, had sex with Prince in 1976 at a hotel in Kansas City. The claim says Ms. Henson gave birth to Prince's son on April 8, 1977. DNA tests might confirm it or rule it out. But depending on how this shakes out, there could be a legal settlement. And taxes could figure prominently. Already, it's clear that Prince's large estate will face major taxes.



Some observers criticize Prince for not planning ahead. But from a tax viewpoint, it may not matter. Prince was not married, and marriage is one of the biggest estate tax savings of all. The current federal estate tax law says that a person can (by will or intestacy) give \$5.45 million tax free to anyone. One can add to that gifts to qualified charities (Prince might have wanted to benefit the Jehovah's Witnesses).

But beyond that, Prince's estate will have to pay. The current federal estate tax rate is 40%. For every million dollars going to a half-sibling, for example, the IRS will get \$400,000. That would not have been helped by a will. Then, Minnesota also has an inheritance tax of 16%. Combining it with the federal estate tax of 40%, and the government collects more than half. Democratic candidates Hillary Clinton and [Bernie Sanders are promoting a big tax hike they call 'sensible'](#). They would hike the rate from 40% to 45% and cut the exemption from \$5.45 million down to \$3.5 million.

How much tax Prince's estate will ultimately bear will depend on the manner of payouts too. For example, if the estate pays the inmate who claims he is Prince's son, is it tax free to him? It depends, and the estate will have settlement tax issues to address too. For example, can Prince's estate deduct a settlement payment on its own tax return? That's where things get interesting.

Normally, an estate cannot deduct (for tax purposes) the distributions it makes to beneficiaries. Normally, that would include payments to putative heirs too, like the inmate who claims he is Prince's son. However, estates sometimes take the position that a settlement of a legal claim is a tax deduction that *reduces* estate tax. It ties into the question of whether the claimant has income. After all, if you receive a bequest from an estate, it is not subject to income tax.

What if you have to sue the estate to be recognized as an heir and to get your money? You might sign a legal settlement agreement, but the origin of your claim should be the same. Is it possible for both the claimant and the estate to win? In some cases, yes. It is must one of the many complex tax issues facing estates and their beneficiaries. And then there is the question of how Prince's image rights should be taxed!

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.