# WEALTH TRANSFER PLANNING AFTER TRA 2010

## - 2011 and Beyond -

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# IMPORTANT DISCLAIMERS

# AND NOTICES

These materials are intended for educational purposes ***only***. They are designed to provide accurate and authoritative information in regard to the subject matter covered. However, Attorney Robert G. Alexander is not offering legal, accounting, or professional advice in these materials. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.

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# NAEPC Current Projects

- Providing the highest quality training, education, products and services to America's leading estate planning professionals.

- Increasing public awareness of estate planning and the advantages of using a "team" of qualified estate planning professionals.

I. Academic Programs
   A. LLM Programs
   B. Masters Programs
   C. CLE
   D. Conferences/Webinars/ Audio Broadcasts

II. National Estate Planning Conference-Annually Recognized as One of the Nation's Leading Estate Planning Conferences

III. Forms/Documents-Blattmachr's Wealth Transfer Planning

- Estate and Financial Planning Software

- Prestigious Publications-NAEPC Journal of Estate and Tax Planning

VI. Newsletters-CCH/Blattmachr/NAEPC

VII. Research Libraries and Technical Information-CCH Publishing

VIII. Leimberg Informational Services/LISI

- Nationally Recognized Experts-Speakers/Teachers

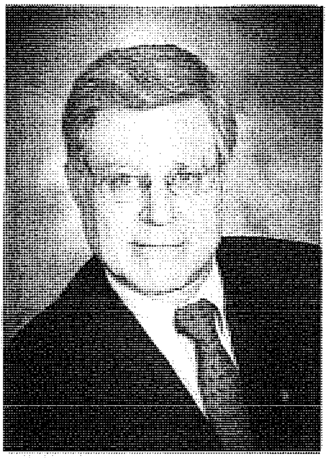
- Networking and Concurrent Projects Among the Nation's Leading Estate and Financial Planning Organizations

   A. NAEPC/Synergy Summit
      1. Society of Financial Service Professionals
      2. American Institute of Certified Public Accountants
   B. American Bar Association-Real Property, Probate and Trust Law Section
      1. American Bar Association-Tax Section/Gift and Estate Tax Committee
      2. NAEPC
      3. NAELA-National Academy of Elder Law Attorneys

XI. Referrals/Networking-Locally and Nationally

XII. Charitable Foundation-Public Awareness and Education Regarding Estate Planning

XIII. National Recognition of America's Most Distinguished Estate



# Robert G. Alexander, JD, LL.M., AEP, EPLS

## Professional Biography 2011

Attorney Robert G. Alexander is the President and majority shareholder of Alexander & Klemmer, S.C., located in Milwaukee, Wisconsin. He earned a B.A. in English from the University of Wisconsin-Madison, J.D. from the University of Wisconsin-Madison Law School, and an LL.M. in Taxation from DePaul University. Mr. Alexander entered into private practice in 1978 and concentrates his practice in the areas of wealth transfer, asset protection and family business planning, including discretionary dynasty trusts, asset protection trusts, life insurance planning, federal estate and gift taxation; trust and estate administration; fiduciary income taxation; charitable planning; business organization and succession planning and international tax planning. He has earned professional designations as a Board Certified Estate Planning Law Specialist (EPLS) as accredited by the American Bar Association, and as an Accredited Estate Planner (AEP) by the National Association of Estate Planners & Councils (NAEPC). He is AV rated by Martindale-Hubbell, its highest rating in legal ability and ethical standards, a Wisconsin Super-Lawyer and a Milwaukee Five Star Wealth Manager.

Mr. Alexander currently holds the office of treasurer for the National Association of Estate Planners & Councils and serves as the chairperson of the Estate Planning Law Specialist Board, (EPLS), Inc. as accredited by the American Bar Association. He is the chairperson of the NAEPC Foundation Committee, serves on the NAEPC Committee administering the Accredited Estate Planner (AEP) designation, and the Conference Committee. He is an NAEPC delegate to the Synergy Summit, a leading national estate, tax, and financial think tank, where he also served as the chairperson. He served on the editorial advising board of *Wealth Management Magazine* (2007-2009); and currently is on the professional advisors panel for *The Elite Advisor Forum.* Mr. Alexander served for two years as the original Publishing Editor of the NAEPC's academic journal, *The NAEPC Journal of Estate and Tax Planning*; and for three years on the board of directors of the Milwaukee Estate Planning Council. Currently he serves on the board of directors for the Milwaukee Chapter of the Society of Financial Service Professionals (SFSP).

He is a nationally known author and speaker who lectures and teaches extensively for both public and private organizations, including the National Association of Estate Planners & Councils (NAEPC), The Society of Financial Services Professionals (SFSP), CCH Wolters Kluwer, national continuing legal education providers, the Wisconsin Institute of CPA's, major insurance companies, brokerage firms, banks, trust companies, community foundations, charitable organizations, and various local colleges.

Mr. Alexander is a member of the American Bar Association sections on Real Property, Probate and Trust Law and Taxation; the State Bar of Wisconsin; the National Association of Estate Planners & Councils; the Milwaukee and Waukesha Estate Planning Councils; the Society of Financial Service Professionals (SFSP) and the Society of Trust and Estate Practitioners (STEP). Mr. Alexander is admitted to practice in Wisconsin, the U.S. District for the Eastern and Western Districts of Wisconsin, the Seventh Circuit Court of Appeals, and the U.S. Tax Court.

Significant Recent Speaking Engagements Include:

1. November 2009 - Inter-face Conference on Distressed Real Estate – Atlanta, Georgia. France Publications.
   - Asset Preservation & Protection Considerations.

2. September 2009 – Real Estate's Place in Wealth Management & Financial Planning Conference – Dallas, Texas. France Publications.
   – Estate, Tax and Asset Protection Strategies. Co-speaker: Atty. Stan Blend.

3. July 2009 – Northwestern Mutual Financial Network Annual Convention – Milwaukee, Wisconsin. Physicians Nationwide.
   - The Beneficiary Defective Inheritor's Trust – A Powerful New Wealth Planning Strategy

4. June 2009 - Real Estate's Place in Wealth Management and Financial Planning – Atlanta, Georgia. France Publications.
   - Legal & Tax Strategies for New Investments, Already Owned and To Be Passed-On Commercial and Residential Property

5. May 2009 - Spokane Estate Planning Council Annual Meeting. Gonzaga University Law School
   - Super-charging Wealth Transfer and Asset Protection Planning with Grantor Trusts
   - Selected Issues in Fiduciary Duties and Liabilities
   - Tax Disasters and Other Conundrums: What Can Be Done to Correct All These Problems

6. March 2009 – Northwestern Mutual Life Insurance Company. The Estate and Business Planning Specialists Conference; Milwaukee, WI
   - Beneficiary Defective Inheritor's Trust ("BDIT") – Finessing the Pipe Dream

7. January 2009 – Palm Beach Tax Institute; Palm Beach, FL.
   - Income Tax Issues With Respect to LLC and Partnership Interests Held In Trust

8. Society of Financial Services Professionals 2008 Forum – Las Vegas, Nevada;
   - Advanced Estate and Asset Protection Planning for Tax-Qualified Assets
   - Panelist: Family Business Succession Planning

9. 2008 Sid Kess-The Ultimate Estate and Retirement Conference - Las Vegas, NV.
   - What Every Practitioner Needs to Know About International Estate Planning.

10. Charles Schwab Impact 2008- Atlanta, GA.
    - Super-Charging Wealth Transfer and Asset Protection Planning with Grantor Trusts.

Significant Current Publications include:

1. The Cash Value Beneficiary Defective Inheritor's Trust (The "Cash Value BDIT") – Creating a More Flexible and Comprehensive Wealth Accumulation and Retirement Plan. NYU Review of

Employee Benefits and Executive Compensation; Matthew Bender & Company, Inc. November, 2009.

2. Enhancing the Planning Value of GRATs - Part 2 – CCH: Financial and Estate Planning Report No. 352, April 2009, and the Journal of Practical Estate Planning, Feb./Mar. 2009.

3. Enhancing the Planning Value of GRATs - Part I – CCH: Financial and Estate Planning Report No. 350, Feb. 2009, and the Journal of Practical Estate Planning, Nov./Dec. 2008.

4. The Beneficiary Defective Inheritor's Trust (BDIT) – Finessing the Pipe Dream. CCH Practitioner's Strategies, Nov. 2008. Co-authored with Attorney Richard A. Oshins.

5. Combining Cash value Life Insurance with the Beneficiary defective inheritor's Trust ("BDIT"), CCH Practitioner's Strategies, Nov. 2009. Co-authored with Attorney Kristen E. Simmons.

6. The Beneficiary Defective Inheritor's Trust: Creating the Idea Wealth Transfer and Asset Protection Plan. The Society of Financial Service Professionals. May 2010.

7. Creative Wealth Planning with Grantor Trusts, Family Limited Partnerships and Limited Liability Companies. Texas Tech Law School. Estate Planning and Community Property Law Journal. Volume 2, Book 2. Spring 2010.

8. The Cash Value BDIT – Modern Portfolio Theory and Life Insurance. The Society of Financial Service Professionals. August 2010.

Significant Books Include:

1. Trust Administration and Trustee Selection. Chicago: Guarantee Trust Company, 2003. Rev. Ed. Milwaukee: Wealth Planning Publishing International, LLC, 2009.

2. Succession Planning for Closely Held Businesses. Chicago: Guarantee Trust Company, 2003.

3. Wealth Planning with Domestic and Foreign Asset Protection Trusts: A Resource and Study Guide. Rev. Ed. Milwaukee: Wealth Planning Publishing International, LLC, 2010.

4. Lifetime and Testamentary Charitable Planning: A Resource and Study Guide. Milwaukee: Wealth Planning Publishing International, LLC, 2006.

5. Tax and Estate Planning Under the 2001 Tax Act. Chicago: Guarantee Trust Company, 2001. Rev. Ed. 2002.

Forthcoming Publications:

1. Modern Wealth Planning with Discretionary Dynasty Trusts: A Practitioner's Guide. Milwaukee: Wealth Planning Publishing International, LLC. Fall 2010.

2. The Cash Value Beneficiary Defective Inheritor's Trust (the Cash Value BDIT) – Part II. NYU Review of Employee Benefits and Executive Compensation; Matthew Bender & Company, Inc. November, 2010. Co-authored with Atty. Larry Brody and Gary Flotron, CLU, ChFC, AEP.

Upcoming Major Conferences:

1. Northwestern Mutual Life Insurance Company – Annual Conference, Milwaukee, Wis., July 2010.
2. South Dakota State Bar Association – Sioux Falls, S.D., September 2010.
3. Northwestern Mutual Life Insurance Company – Financial Advisor's Annual Conference, Milwaukee, Wis., October, 2010.
4. Society of Financial Service Professionals Forum – Orlando, Florida, October 2010.
5. Society of Financial Service Professionals Advanced Institute – Tucson, Arizona, February 2011.

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June, 2010

## Wealth Transfer Planning After TRA 2010 - 2011 and Beyond -

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## NAEPC - Your Professional Organization of Choice -

- Providing the highest quality training, education, products and services to America's leading estate and wealth planning professionals
- Increasing public awareness of estate and financial planning and the importance of using a "team" of qualified, credentialed planning professionals
- Credentialed professional networking
  - Locally
  - Nationally
  - Referrals

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## Introducing NAEPC & the NAEPC Education Foundation

- **The National Association of Estate Planners and Councils**
  - Formed over 49 years ago as a nonprofit membership league
  - Serves over 220 councils & 26,000 credentialed financial professionals
  - In 2005 we formed The NAEPC Education Foundation as a 501(c)(3) nonprofit organization

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## NAEPC Current Projects - Continued

- **High quality professional educational programs**
  - National conference
  - Webinars and teleconferences
  - Professional CE
  - Links to other professional organizations
  - NAEPC speakers bureau

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## NAEPC Current Projects - Continued

- **Publications, software and documents**
  - Newsletters
  - NAEPC Journal of Estate and Tax Planning
  - Estate and financial planning software
  - Blattmachr's Wealth Transfer Planning - ILS
  - CCH research libraries and technical information
  - NAEPC value partners
  - Leimberg Informational Services/LISI
  - Business Exit Planning – BEI
  - Many others

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## NAEPC Current Projects - Continued

- **Nationally recognized awards and designations**
  - National Estate Planning Hall of Fame – DAEP
  - The Accredited Estate Planner designation – AEP
  - ABA board certified Estate Planning Law Specialist
    - EPLS
  - Hart Axley Distinguished Service Award

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## Synergy Summit

- **National "think tank" comprised of the top professional wealth planning organizations in America**
  - NAEPC
  - American Association of Attorney - CPAs
  - American Bar Association - Real Property, Trust & Estate Law
  - American Bar Association - Tax Section (Estate & Gift Tax Committee)
  - American Institute of Certified Public Accountants
  - Society of Financial Service Professionals
  - National Academy of Elder Law Attorneys
  - Partnership for Philanthropic Planning
  - ACTEC

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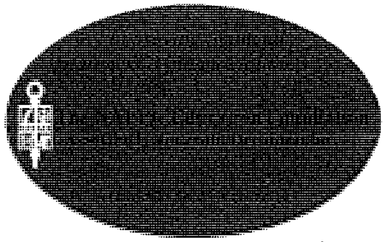
## The NAEPC Education Foundation

Your 501(c)(3) at Work!!!



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## The NAEPC Education Foundation Mission

- **To provide the public with financial awareness programs & improve financial literacy**
- **To educate the public regarding the benefits of the multi-disciplinary team concept of estate & financial planning as espoused by the National Association of Estate Planners & Council**
- **To develop educational programs regarding estate & financial planning for financial professionals**
- **To develop & promote a community outreach program for the general public**
- **To hold educational conferences, seminars, forums, & meetings regarding estate & financial planning**

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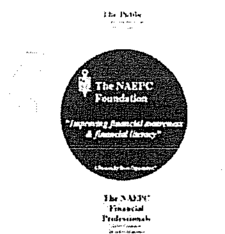
## The NAEPC Education Foundation

- **Is uniquely positioned to both understand & serve:**
  - The Public
  - Wealth Planning Professi
  - Helping to make this
  - a better world…






## One Big Challenge

Improving Financial Awareness & Literacy

- **Estate Planning is an element of financial planning**
  - 100 million Americans don't have a current estate plan
- **Half of Americans are unfamiliar with retirement tools**
- **Without a proper & well thought out estate & financial plans people waste big money and often ruin their financial futures**
- **85% of Americans over 65 are totally dependent on Social Security (EBRI-June 2010)**

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## Help Us by Being Part of the Solution

- **Goals**
  - Alert, educate, motivate & assist the American Public to cost effectively get & keep their estate & financial plans up-to-date.
- **Touch every American at least annually**
  - High quality educational content & tools
  - Our public estate & financial planning web portal, seminars, programs, media, & relationships.

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## 2011 Projects & Programs

- **Promote financial awareness & improve financial literacy through:**
  - National Estate Planning Awareness Week
  - Public & Professional Financial Portals
  - The launching of The NAEPC Education Foundation Publishing Division
  - To facilitate & hold educational conferences, seminars, forums, webinars and meetings regarding estate and financial planning for professionals and the public
  - Fund nationwide scholarships to advance the wealth planning professions

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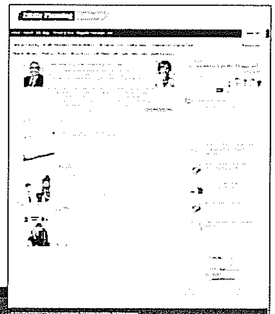
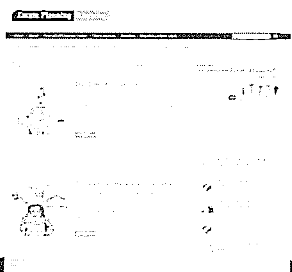
## Public Financial Portal

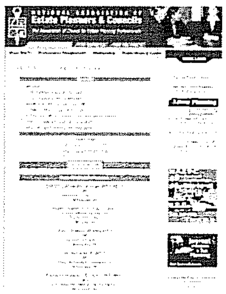




## Public Financial Portal - Continued

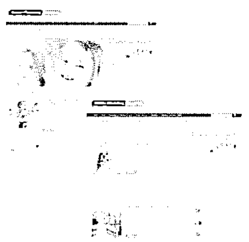
Find an AEP® or find councils easily







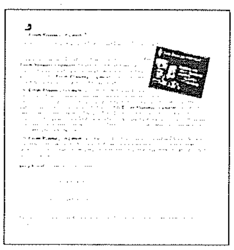
## Public Financial Portal - Continued



Timely content, great resource links, downloadable worksheets, forward to your social networks, ...



## Launching The NAEPC Education Foundation Publishing Division

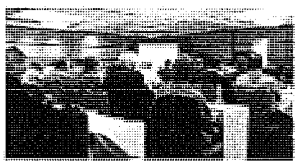




## Providing Education Programs

Be sure to mark you calendars for the NAEPC 48th Annual Conference Nov 16-18, 2011 in San Antonio, Texas





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## Key Benefits to the Public & Professionals

- **National Estate Planning Awareness Week**
  - Organized strategic contact plan
  - Community efforts
- **"Go To" Public Financial Portal**
  - Friendly, motivational, unbiased, up-to-date, empowers the public
- **Launching The NAEPC Education Foundation Publishing Division**
  - Cost effectively bring content and tools to the public & professionals
- **Educational Programs**
  - Helps create financial awareness amongst the professionals & the public

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## Endorsements & Organizational Support

- **Through the Synergy Summit:**
  - American Association of Attorney - CPAs
  - American Bar Association - Real Property, Trust & Estate Law
  - American Bar Association - Tax Section (Estate & Gift Tax Committee)
  - American Institute of Certified Public Accountants
  - Society of Financial Service Professionals
  - National Academy of Elder Law Attorneys
  - Partnership for Philanthropic Planning
  - ACTEC

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## Your 501(c)(3) at Work!

**Thanks for your Consideration!**

If you would like additional information on how you can make a difference, please contact:

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## Wealth Transfer Planning After TRA 2010 - 2011 and Beyond -

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## Our Study Goals

- **Understand the wealth transfer tax provisions of TRA 2010**
- **Review selected planning opportunities and specific techniques for practitioners to consider under TRA 2010**



## Special Thanks

- Good poets borrow from other poets...Great poets steal from other poets!
  - T.S. Elliot
- Disclaimer: no claim is made to original work herein. These PowerPoints include not only original material, but also a compilation, editing and revision of other source material, including the authors and sources cited on the following PowerPoint
  - See also the "Selected Additional Sources of Information" PowerPoints

## Special Thanks

- Steve Akers
- Jonathan Blattmachr
- Natalie Choate
- Robert Keebler
- Marty Shenkman
- NAEPC
- CCH Wolters Kluwer
- The ABA/RPTE Section
- AICPA
- Leimberg LISI




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## Wealth Transfer Planning After TRA 2010 – Introduction and Overview –

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## Introduction

- **Estate planning will be somewhat different, but it can never be ignored!**
  - Proper planning still is essential to all of our clients
- **Obviously - less emphasis on estate taxes for most people**
- **Instead, focus on the traditional personal, family, financial, retirement, long term care, income tax, asset protection, business succession, health, and other non-tax issues that always have been the cornerstone of estate planning**




## Introduction - Continued

- **So exactly what is TRA 2010?**
  - The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Action of 2010
  - P.L. 111-312
  - Signed into law: December 17, 2010
  - Effective date: January 1, 2011 for many provisions

## Introduction - Continued

- **So exactly what is TRA 2010?**
  - The bottom line:
    - Extends the Bush tax cuts and the estate tax provisions for two (2) years
    - Basically all of the EGTRRA provisions are extended for two (2) years
    - The "sunset" provision is extended for two (2) years
    - Includes special estate, gift and GST provisions for 2010



## Historical Perspective on 2010 Estate Tax Relief

- **The Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"), made dramatic reductions in the estate tax**
- **Most of EGTRRA's provisions were repealed for one (1) year (2010) and "sunsetted" on December 1, 2010**
- **EGTRRA lowered the gift tax rate to 35% and increased the gift tax exemption to $1 million for 2010**
- **EGTRRA "sunset" provisions: in 2011 the estate, gift and generation skipping transfer ("GST") tax exclusion were scheduled to decline to $1 million and the estate, gift and GST tax rate was scheduled to rise to 55%**



## 2010 Tax Act – Summary and Key Changes –

- **For 2010:**
  - TRA generally sets the estate, gift and GST exemption at $5 million, indexed for inflation from 2010 beginning in 2012
    - The $5 million exemptions generally apply in 2010
      - ✓ Except the gift tax exemption which remains at $1 million for 2010
    - These exemptions apply for all of 2010
  - Executors can choose between:
    - Carryover basis and no estate tax, or
    - The estate tax with a $5M exclusion and a 35% rate



## 2010 Tax Act – Summary & Key Changes – Continued

- **For 2010:**
  - Estates for decedents dying in 2010 with gross estates under $5 million will not be required to file an estate tax return
    - Won't have to file the carryover basis report Form 8939
  - The estate tax return and payment date of the estate tax is extended to no earlier than nine (9) months after the date of enactment
    - Applies to estate of decedents dying from Jan. 1, 2010 to the day before the enactment
    - The extension is to September 19, 2011
      - ✓ (September 17, 2011 is a Saturday!)
  - The carryover basis report to be filed with the final income tax return is extended the same way.
    - Except the extension will likely be to at least Oct. 17, 2011



## 2010 Tax Act– Summary & Key Changes – Continued

- **GST tax returns for 2010**
  - As a general rule, for GST transfer made in 2010 before Dec. 17, 2010, the filing date is extended to September 19, 2011
  - This applies to direct skips, taxable distributions or taxable terminations
    - The transfer is reported but the tax rate is zero
    - Elect out of automatic allocations for direct skip transfers in 2010
  - NOTE: this rule does not appear to apply to filing a return to make timely allocations of GST exemption or to elect out of automatic allocations for "indirect skip" transfers to trusts which are not direct skips



## 2010 Tax Act– Summary & Key Changes – Continued

- **Disclaimers – IRC Sec. 2518(b)**
  - The time for making any disclaimer for property passing by by reason of the death of a decedent in 2010 is extended to September 19, 2011
  - Watch:
    - State law considerations
    - Accepting the benefits
  - Recite in the documents that your intention is to make a qualified disclaimer for federal tax law purposes
    - Other planning considerations
  - Disclaimer planning provides a great deal of flexibility in dealing with the new law

## 2010 Tax Act – Summary and Key Changes – Continued

- For 2011 – 2012:
  - $5M gift, estate and GST exclusions
  - 35% gift, estate and GST tax rate
  - Exemption inflation indexed beginning in 2012 (from 2010)
  - Portability of the estate tax exclusion
    - But not the GST exemption
    - Only applies to gifts made or decedents dying on or after January 1, 2011, and
      - ✓ Only with respect to previously deceased spouses who die on or after January 1, 2011
    - The election needs to be made on a timely filed estate tax return of the predeceased spouse!
  - These changes are dramatic and will change the face of estate planning at least for the next two (2) year



## 2010 Tax Act – Summary and Key Changes – Continued

- **For 2013:**
  - Absent action by Washington, TRA "sunsets" and we are back to:
    - The $1 million exclusion, 55% rate for estate and gift taxes, and
    - The $1 million GST exemption, 55% rate (indexed for inflation from 1997)
    - It is possible that gifts will be tossed back into the estate and be included in estate tax calculations with a $1 million exemption



## 2010 Tax Act – Summary and Key Changes – Continued

- **The EGTRAA Sec. 901 "sunset" is extend for two (2) years by TRA Sec. 101(a)**
- **Could 2013 be a repeat of year end 2010?**
- **Marty Shenkman says:**
  - The rollercoaster continues
  - Clients have to understand the risks of the 2012 sunset
    - Is it really safe to ignore 2013?



## Wealth Transfer Planning After TRA 2010

- Understanding the Terms Used Under TRA 2010 -

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## 2010 TRA – Terms You Need To Know – Continued

- **Basic Exclusion Amount:**
  - In 2011 and 2012 this amount will be $5 million
  - The exclusion previously was called the "applicable exclusion amount"
  - In 2009 this amount was $3.5 million
    - In 2013, absent yet another change in the law, this amount will be $1 million
  - Under TRA a new building block is required to address the concept of portability of a deceased spouse's unused exclusion to the surviving spouse
  - TRA new math/definitions are: [Basic Exclusion Amount + Portable Amount = New Applicable Exclusion Amount]



## 2010 TRA – Terms You Need To Know – Continued

- **The Applicable Exclusion Amount:**
  - From prior law, this term has been redefined to encompass the new estate tax concept of "portability"
    - The surviving spouse is permitted, under certain conditions, to use the remaining basic exclusion amount from his or her previously deceased spouse
  - [Your Basic Exclusion Amount + Portable Amount from your Last Deceased Spouse = New Applicable Exclusion Amount]
  - Query: A power of attorney that permits gifts up to the applicable exclusion
    - Does that now mean $5 or $10M instead of perhaps the $1M when signed?

## 2010 TRA – Terms You Need to Know – Continued

- **Deceased Spousal Unused Exclusion:**
  – TRA creates a new concept called "portability" which tries to simplify the estate tax system by avoiding the need for families to undertake complex planning to maximize the use of both spouse's exclusions
    - e.g. marital deduction and credit shelter trust planning
  – Under prior law a couple might have divided assets 50/50 and had each will include a bypass trust to benefit the surviving spouse while still avoiding inclusion of those assets in the surviving spouse's estate
  – Under TRA if a spouse dies with none of this planning, on the later death of the surviving spouse, he/she may be able to utilize the prior deceased spouse's unused estate tax exclusion
  – Caution: this new planning is not as simple as it sounds!



## 2010 TRA – Terms You Need to Know – Continued

- **Last Deceased Spouse:**
  – On the later death of the surviving spouse, if his/her previously deceased spouse did not use all of his/her estate tax exclusion
    - Under the new "portability" concept, the surviving spouse may be permitted to take advantage of that unused exclusion
  – To assure that the estate of the surviving spouse will only benefit from one such prior unused exclusion, and to provide clarity as to which exclusion can be used
    - It is the exclusion of the last deceased spouse that governs



## 2010 TRA – Terms You Need to Know – Continued

- **Indexing:**
  – The estate tax "Basis Exclusion Amount" is indexed for inflation beginning in 2012
  – If the estate tax relief provisions are not extended, 2012 will be the only year of increase since the law reverts back to pre-2001 law after that point (i.e., in 2013)
  – On the death of the first spouse to die, "portability" allows the executor either to utilize the decedent's $5M exemption amount or to transfer it to the surviving spouse
    - The decedent spouse's unused exemptions transferred to the surviving spouse does not get indexed for inflation



## Wealth Transfer Planning After TRA 2010 – The Tax Act Provisions –

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## TRA 2010 – Analysis of the Law –

- **Sec. 301(a):**
  – Each provision of law amended by subtitle A or E of title V of EGTRRA 2001 is amended to read as such provision would read if such subtitle had never been enacted
- **The repeal is repealed…but only for 2 years**
- **Subtitle A includes Sec. 2210 which repealed the estate tax and Sec. 2664 which repealed the GST tax**
- **Subtitle E is the carryover basis rules**



## TRA 2010 – Analysis of the Law – Continued

- **Sec. 301. Reinstatement of Estate Tax; Repeal of Carryover Basis**
  – (c) Special Election with Respect to Estates of Decedents Dying in 2010
    - Such election shall be made at such time and in such manner as the Secretary of the Treasury or the Secretary's delegate shall provide. Such an election once made shall be revocable only with the consent of the Secretary
    - Special rules make 2010 probates unique and potentially complex and adversarial with an option to choose carryover basis treatment in lieu of estate tax treatment. No guidance yet exists. It is irrevocable.
  – (d) Extension of Time for Performing Certain Acts: The gives some time leniency nine (9) months after enactment – but watch disclaimers and state law
  – (e) Effective Date: January 1, 2010 for many provisions. Surprising, generous and complicated

## TRA 2010 – Analysis of the Law – Continued

- 302(a)(1) and (2) "Modifications to estate, gift, and generation-skipping transfer taxes. "$5,000,000 Applicable Exclusion Amount
- 2010: Caution – For 2010 there is only a $1M gift exclusion, but a $5M exclusion for estate and GST tax purposes
- 2011-12: $5M gift, estate and GST exclusion in 2011 and 2012
  - Tax rate is 35%
- 2013: $1M exclusion unless Congress acts
  - Tax rate is 55%




## TRA 2010 – Analysis of the Law – Continued

- "(B) Inflation adjustment.—In the case of any decedent dying in a calendar year after 2011, the dollar amount in subparagraph (A) shall be increased by an amount equal to—"(i) such dollar amount, multiplied by "(ii) the cost-of-living adjustment determined ...
- Inflation adjustment will, in part, keep the exclusion paced with inflation
  - But there are issues to consider
- The adjustment only applies in 2012 unless Congress extends the law in 2013 and/or later years
- Portability – unused exclusion from first spouse is not inflation adjusted from the death of the 1st spouse to the death of the 2nd spouse




## TRA 2010 – Analysis of the Law – Continued

- 302 (c) Modification of Generation-Skipping Transfer Tax
- Applicable rate for 2010 is zero
- Note: there are several complex year end GST planning opportunities for 2010




## TRA 2010 – Analysis of the Law – Continued

- 303(a):"(4) Deceased spousal unused exclusion amount.—For purposes of this subsection, with respect to a surviving spouse of a deceased spouse dying after December 31, 2010, the term 'deceased spousal unused exclusion amount' means the lesser of— "(A) the basic exclusion amount, or "(B) the excess of— "(i) the basic exclusion amount of the last such deceased spouse of such surviving spouse, over "(ii) the amount with respect to which the tentative tax is determined under section 2001(b)(1) on the estate of such deceased spouse.
- This is not simple:
  - There is no inflation adjustment
  - No asset protection
  - No state estate tax minimization
  - No GST portability
  - Only applies in 2011 and 2012
  - There are many complex issues




## TRA 2010 – Analysis of the Law – Continued

- 303(a)(5): "(a) a deceased spousal unused exclusion amount may not be taken into account by a surviving spouse under paragraph (2) unless the executor of the estate of the deceased spouse files an estate tax return on which such amount is computed and makes an election ...No election may be made ...if such return is filed after the time prescribed by law ...(B) Examination of prior returns after expiration of period of limitations with respect to deceased spousal unused exclusion amount
- Portability is not simple
  - The executor must elect it on the estate tax return of the first spouse to die
  - The election must be on time
  - The period to audit doesn't end for purposes of determining the unused exclusion amount
  - This is not the "slam dunk" advertised
  - Key an eye on the "sunset": if the first souse dies in 2011 and the surviving souse dies in 2014 and portability has sunsetted what happens?




## TRA 2010 – Analysis of the Law – Continued

- 2011 and 2012 – "Portability"
  - The Applicable Exclusion Amount (AEA):
    - Defined as the sum of (1) the "Basic Exclusion Amount" and (2) the "Deceased Spousal Unused Exclusion Amount"
    - The "Basis Exclusion Amount" (BEA) is what used to be called the AEA and is $5 million for 2011
      - ✓ Adjusted for inflation after 2011
      - ✓ Currently estimated to be $5,210,000 for 2012
    - The "Deceased Spousal Unused Exclusion Amount" (DSUEA) is the difference between the decedent's last predeceased spouse's BEA and the taxable estate of the last predeceased spouse
      - ✓ Congress did it this way to avoid "stacking" of unused exclusion amounts

## TRA 2010 – Analysis of the Law – Continued

- **2011 and 2011 – "Portability"**
  - Election for portability needs to be made on a timely filed estate tax return of the predeceased spouse
    - Executor will need to determine if it is appropriate to file and preserve the election
      - ✓ Prudence would seem to suggest to do so
    - Likely will result in lots of estate tax return filings for 2011 and 2012
      - ✓ Although many without tax due
  - Lots of questions as to what may happen after 2012
  - Note: Credit Shelter Trusts may still be the best way to go to try and preserve the full BEA beyond 2012

 

## Wealth Transfer Planning After TRA 2010

What Our Client's Will Be Most Concerned About

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## What Our Clients Will Be Concerned About Most

- **Wealthy Clients:**
  - TRA 2010 is a golden opportunity for wealth transfer and asset protection planning!
    - Why:
      - ✓ Large exemptions - $5 million
      - ✓ Low tax rates – 35%
      - ✓ Continued availability of:
        - » GRATs
        - » QPRTs
        - » Valuation discounts
      - ✓ Low interest rate environment
      - ✓ Less IRS audit risk?
      - ✓ GST relief provisions are still in place
    - These opportunities may disappear in 2013

 

## What Our Clients Will Be Concerned About Most

- **Mid-range clients:**
  - It is estimated that fewer than 5,600 estate tax returns will be filed and pay a tax each year for 2011-2012
    - The estate tax will affect very few people
  - Even for the mid-range clients, 2011-2012 is a golden opportunity to do wealth transfer and asset protection planning
    - Own everything in trust forever!
    - The benefits of portability and the other TRA provisions may be short-lived
      - ✓ "Sunset" at the end of 2012

 

## What Our Clients Will Be Concerned About Most

- **Mid-range clients:**
  - Major planning concerns:
    - State estate and gift taxes in decoupled states
      - ✓ e.g. on a $1 million exemption in New York
    - Inflation and investment returns may push the estate above the threshold for taxation
    - The 2013 return of the $1 million exemption
      - ✓ Gifts tossed back into the estate tax calculation
    - Creative and flexible planning
    - Shenkman: "wait and see" may result in "wait and pay"

 

## What Our Clients Will Be Concerned About Most

- **Most taxpayers:**
  - Tax issues in decoupled states
  - Planning costs and complexities
  - Uncertainty continues
  - Income tax planning:
    - Minimizing income tax basis step-up
    - Planning for residency and domicile to minimize income and estate taxes
  - Traditional family and personal matters
  - Multi-jurisdictional planning
  - Corporate/entity and business succession planning
  - Asset protection planning
  - Retirement and long-term care planning

 

## Estate Planning for Estates of Up to Ten Million Dollars

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## Introduction

- **The new "modest wealth" – special hurdles**
- **Estates less than $5 million, and/or estates for married couples between $5 million and $10 million**
- **Clients cannot afford or want to gift significant amounts of wealth during lifetimes**
  - This is the most useful way to transfer wealth



## Introduction - Continued

- **Real tension between opportunities to reduce taxes and maintaining current standard of living**
  - After tax
  - Inflation adjusted
  - Asset protected
  - Maintain control
- **Planning uncertainties**
  - Estate taxes?
  - Income taxes?



## Assign Life Insurance & Other Non-Income Producing Assets

- **Goals**
  - Reduce taxes
  - Consume income but not principal
  - Retention of income does not reduce estate taxes or protect from creditors
- **Generally, life insurance does not produce income**
  - Investment component



## Life Insurance - Continued

- **Assign the policies and all incidents of ownership**
- **Outright**
- **Life insurance trusts**
  - New policies
  - Existing policies
    - Sell to a grantor trust (ILIT)
    - No gain recognition
    - No three year inclusion rule



## Life Insurance - Continued

- **Draft trust so it can qualify for the "back-up" marital deduction by a QTIP election**
- **GST provisions?**
- **Multiple Crummey powers**
- **Excellent use of annual exclusions**
- **Draft ILIT to allow flexibility in structuring and restructuring the lifetime insurance plan**

## Other Lifetime Gifts

- **Annual exclusion gift of tangible personal property**
  - Must be a completed gift
  - Watch retained use or control
  - Donee pays insurance on the property
- **Recreational real estate**
  - Undivided interests – tenants in common
  - Valuation discounts
  - Be sure to split costs and use proportionately
  - Perhaps a second QPRT?




## Estate Building & Income Tax Sheltering With Life Insurance

- **Generally, internal build-up is income tax free – Sec. 7702**
- **Variable insurance allows owner to direct investments**
- **Withdrawals up to the extent of basis may be free of income tax**
  - Watch modified endowment rules – Sec. 7702A




## Estate Building & Income Tax Sheltering With Life Insurance - Continued

- **Income can be borrowed without income tax effect**
- **Cash build up allows future term premiums to be paid with the income earned under the policy using pre-tax dollars that will never be subject to tax**
  - Even if the policy lapses




## Estate Building & Income Tax Sheltering With Life Insurance - Continued

- **Watch insured's direct access to cash or investment components**
  - Causes estate tax inclusion
- **Split-dollar arrangements may allow access (at least indirectly) to policy's cash without the term component being included in the estate**
- **Corporate, LLC or partnership ownership**
  - Properly structured, no ownership in estate of insured
  - Entity has access to cash values without income tax
  - Distributions to insured/owner – income tax




## Estate Building & Income Tax Sheltering With Life Insurance - Continued

- **Avoiding income tax on withdrawals**
  - Self-settled trusts
    - Alaska
    - Delaware
    - South Dakota
    - Nevada
  - Trust structured so that insured has no incidents of ownership attributed to him/her
  - Insured may be eligible to receive distributions from the trust
    - Even from cash values of insurance




## Estate Building & Income Tax Sheltering With Life Insurance - Continued

- **Insured cannot have direct access to cash value without estate tax inclusion**
- **Ownership with a split-dollar arrangement may allow insured to benefit (at least indirectly) from cash values without estate tax inclusion**
  - ILIT owns the term component
  - Entity owns the cash component
  - Corporations – no more than 50% voting stock
  - Partnerships

Estate Building & Income Tax Sheltering With Life Insurance - Continued

- Entity can access cash values without tax
  - Withdrawals
  - Borrow
- Distributions to insured/owner may be subject to income tax
- Self-settled trusts in Alaska, Delaware, South Dakota or Nevada owns the policy
  - Insured grantor can be eligible or distributions



## Qualified Personal Residence Trust

- Sec. 2702 split interest trust
- Value interest under Sec. 7520 rates
- Grantor retains the exclusive right to occupy the property as a personal residence for a term of years
- End of term
  - Passes to remaindermen
    - Another trust?
  - Grantor purchases or rents at FMV



Qualified Personal Residence Trust - Continued

- Split-purchase trust
  - Parents purchase a life estate
  - A grantor trust (generation skipping trust) purchases the remainder interest
- Parents occupy residence for life
  - Do not need to pay rent
  - No required survival period required
- Leverage the GST exemption for the parents, unlike a QPRT



Effective Use of the Balance of the Annual Exclusions

- Make annual gift tax exclusion gifts over a period of time
- Use one or both spouse's annual exclusions over time
- Removes the asset, appreciation and income on the assets from the Donor's estate



Effective Use of the Balance of the Annual Exclusion - Continued

- Annual exclusion gifts to a trust which permits the spouse to receive distributions
  - Income tax planning – grantor trust
  - Estate tax exclusion
- Each spouse creates a trust
  - Avoid the reciprocal trust doctrine
- Non-donor spouse gift splitting to trusts that may benefit the non-donor spouse
  -



## Self-Settled Trust Options

- States where creditors cannot reach assets transferred to a trust in which the grantor is a permissible distributee in the discretion of the trustee
  - Cannot be a transfer to defraud creditors
- Not included in the estate of the grantor
- Grantor cannot retain all the income
- Watch regular distributions to grantor

## Potential use of the Gift & GST Exemptions

- Transferor can indirectly benefit through his/her spouse from distributions to the spouse
  - No grantor estate inclusion
  - Use lifetime gift tax exemption?
- Allows the use of life-time QTIP trusts coupled with an upfront GST allocation
  - Also, you can draft to qualify for not qualify for the marital deduction
  - Allocate life-time exemption
- Don't retain a secondary income interest following the death of the spouse




## Accessing Income Tax Free States

- Seven states do not have income taxes
- No income tax on income not distributed to beneficiaries living in states that have income tax
- Specific state laws also may beneficiaries to avoid or reduce state income tax




## Using Charitable Remainder Trusts to Build & Generate Income

- Benefits
  - Charitable income, gift and estate tax deductions
  - Trust is exempt from income tax if it does not have unrelated business taxable income
- Trust can sell assets without imposition of income tax
  - Builds up additional wealth in the trust




## Using Charitable Remainder Trusts to Build & Generate Income - Continued

- If grantor's spouse and descendants are beneficiaries, there can be some estate tax inclusion
- However, trust can continue for benefit of spouse, children etc. subject to certain qualification rules
- Use NIMCRUTs, FLIPCRUTs and other planning to build up additional wealth in the trust




## Medical Care & Tuition Payments

- Direct payments are not subject to gift tax
- Combine with annual exclusion gifts
- Set up joint accounts with beneficiary of payments, so payments are made as you go/as needed
  - Gifts completed only when made




## Limited Liability Companies

- Asset protection
  - Creditor protection
  - Charging orders
- Tax planning
  - Income allocations
  - Valuation discounts
    - But watch lower income tax basis step up

Special Care in Handling Qualified Plans, IRAs & Other IRD

- **Watch exposure to estate tax and income tax**
- **Properly design the beneficiary designations**
- **Trust designations**
- **New PPA rules**
- **Charitable designations**



## TRA 2010 and Retirement Assets

- **The double whammy**
  - Estate taxes
  - Income taxes
- **Spousal rollover vs. estate tax and asset protection planning**



## TRA 2010 and Retirement Assets - Continued

- **Planning with trusts is difficult**
  - "See through" trust rules
  - Single life tables vs. uniform lifetime tables
    - 17 years vs. 27 years payout
  - Drafting with formulas is tricky
- **Spouse can rollover and name his/her own beneficiaries to continue deferral**



## TRA 2010 and Retirement Assets - Continued

- **Three (3) case studies**
  - Poor (?) clients with less than $5 million
  - Wealthy clients with over $10 million
  - Middle of the road clients (?) with estates of $5-10 million
- **Maybe the best answer is to buy life insurance and own it in an ILIT**
  - Preferably a dynasty trust



# Wealth Transfer Planning After TRA 2010

- Wealth Transfer and Asset Protection Planning For 2010 -

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## 2010 Wealth Transfer Planning - Gift Tax Planning -

- **There is only a $1M gift tax exclusion for 2010**
  - Reunification starts in 2011
- **$5M gift tax exclusion begins only in 2011**
  - Caution – the $5M exclusion for estate and GST is effective as of January 1, 2010
- **Planning Consideration:**
  - Do clients stop making annual exclusion gifts ($13,000 per donee, and unlimited tuition and medical) because the $5M exclusion means the estate tax will never apply to them? Or do they gift aggressively because in 2013 the law is a $1M estate exemption and 55% rate?

## 2010 Wealth Transfer Planning – GST Planning –

- You may be able to make unlimited gifts to grandchildren, or even to trusts for grandchildren (this had been doubtful until very recently), and not trigger any GST tax
- In 2011 and 2012 transfers to grandchildren (and other "skip persons" in GST terms) will be limited to the $5 million GST exemption
- Unless Congress acts in 2013, the GST exemption drops to $1 million (inflation indexed) and the rate increases to 55%.
- This is a free pass for GST planning but not for gift tax planning
  - If you gift more than $1 million (or what remains of your gift exclusion) in 2010 you will pay a gift tax
- Gift tax returns for 2010 will have to address many aspects if this issue
  - e.g. electing out of automatic GST exemption allocation for direct skip gifts

 

## 2010 Wealth Transfer Planning – Trust Distributions to Grandchildren –

- Trustees of certain trusts might be able to distribute to grandchildren
- Trusts not structured to avoid GST: GRATs, CLATs, QPRTs and certain ILITs (they did not have GST exemption allocated to protect them from GST tax; or the ETIP rules prevented allocation)
- Trustees of these trusts might be able to make distributions to grandchildren (or other skip persons) free of any GST tax, if these distributions are made before the end of 2010
- Caution: The terms of trust agreement or will must permit distributions. If not, it may be possible that state law could facilitate such tax advantaged distributions.

 

## Wealth Transfer Planning After TRA 2010
### – 2010 Probates and Administrations –

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## 2010 Probates – Key Changes –

- **$5M estate and GST exclusions**
  - If prior taxable gifts were made, the $5M figure will be lower
- **35% rate**
- **The executor can elect (choose) for the estate to be subject to the carry-over basis rules instead of the estate tax**

 

## 2010 Probates – Key Changes –

- **Section 301(d)(1) (C) making any disclaimer described in section 2518(b) of such Code of an interest in property passing by reason of the death of such decedent, shall not be earlier than the date which is 9 months after the date of the enactment of this Act.**
  - Query: will state law or beneficiary accepting benefits taint the ability to disclaim in spite of the extension?
  - 9 month federal extension to September 19, 2011 to file estate and GST returns or carryover basis reports
  - Extension addresses deadline in the tax law – IRC Sec. 2518
    - Query: does this really resolve issues of state disclaimer statutes that may embody a similar deadline?
    - Will states have to patch their disclaimer statutes
      - ✓ This may not be required by Sec. 2518(c)(3)
  - What about the risk of beneficiaries accepting benefits from property during this extended period thereby tainting the ability to disclaim
  - If a beneficiary disclaims to avoid a creditor and the disclaimer is valid under the federal extension but not under state law, what is the impact on creditor protection
  - Does a trustee have the authority to disclaim under the federal extension if the time period extends beyond what state law permits

 

## 2010 Probates – Carryover Basis –

- If the executor elects to have carryover basis rules apply will a state tax patch for repeal result in a bequest to children being limited to the 2009 exclusion of $3.5 million?
  - Might the result be a $5 million bequest to the children if the carryover basis rules are not elected?
  - Could the choice of which tax system to apply result in an additional $1.5 M swing in actual distributions?
- How can any executor address and resolve an issue like this?
- Note: no guidance on allocating $1.35M/$3M basis adjustments has been issued
  - The IRS has issued a draft form with no instructions
  - Many issues remain unanswered

 

## 2010 Probates – Carryover Basis –

- **Carryover basis vs. estate tax on estates over $5 million is difficult**
  - The beneficiaries who bear the estate tax may be different than the beneficiaries who will bear the burden of the capital gains tax
- **The election is irrevocable**
  - What sign-off does an executor want
  - What should go into a receipt and release
  - When should court approval be sought
  - What about the cost of the proceeding and the time factors
- **Carryover basis does not affect the GST application**
  - Therefore 2010 testamentary trusts won't get a "Get out of GST Free" card
- **What other unexpected results are lurking in the 2010 estate tax law?**




## Wealth Transfer Planning After TRA 2010

### – Reviewing Existing Plans and Documents –

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## Wills and Revocable Living Trusts

- **Review every will/revocable trust**
- **Do pecuniary bequests, percentage allocations and formula clauses still work?**
- **State patches – defaulting to 2009 law may only apply if there is no estate tax**
  - Now there is an estate tax
- **Testamentary CLT not needed, or is it?**
- **Continue Bypass/credit shelter trusts:**
  - Risk of 2013 and $1M exemption
  - State estate tax savings
  - Asset protection
  - Portability may not protect post-death appreciation
    - Technicalities to qualify for portability make it uncertain
- **Formulas should consider floors, caps and statements of intent**




## Wills and Revocable Trusts - Continued

- **Review formula provisions carefully**
  - Drafting based on "what-if" scenarios
  - The impact of the formula on the overall estate plan
    - The client's intentions as to the amount of the bequests
  - "One-lung" QTIP trust planning
  - Flexibility in the by-pass trust
    - Discretionary distribution in an independent trustee
    - Independent person has the power to grant a general power of appointment to the surviving spouse over some or all of the bypass trust
    - POA exercisable only with the consent of a non-adverse party
    - Independent trustee has the power to remove the POA over all or some of the trust property
    - Surviving spouse can exercise the POA in a way that causes the assets (all or part) to be included in the spouse's gross estate
      - ✓ Spring the Delaware tax trap
    - Others




## Wills and Revocable Trusts - Continued

- **Watch the wording of the formula**
  - Applicable credit amount – $5 million?
  - The maximum amount that can pass free of estate tax
  - Values as finally determined for federal estate tax purposes
    - What does this mean if no return is filed
- **GST formulas have the same problems**




## Wills and Revocable Trusts - Continued

- **State death tax planning**
  - Planning for domicile
  - Location of assets in more than one state
    - LLC and trust planning to centralize situs?
  - Examine formula and tax allocation clauses
  - Fund the by-pass trust with only the state exemption amount?
    - Typically $1 million
  - State only QTIP election
  - Gift planning
    - Gifts usually are not included in the state gross estate base

## Powers of Attorney

- Gifting provisions:
  - Should gifts now be prohibited because there never will be an estate tax if net worth is safely under $5M
  - Should the gifting provision be expanded along with broad rights to create and fund a trust in the event the grantor becomes incompetent in 2012
  - Consider the risk of a $1M exclusion and an increase to a 55% rate in 2013
- What about:
  - Inflation and investment rates of return
  - State estate tax in a decoupled state
  - 2013 and the risk of a $1M exclusion




## Pre-marital Agreements

- **Portability should be addressed**
- **Include representations and warranties as to intended use of the exclusion**
  - (e.g., should the new spouse count on it)
- **Consider representations as to gift tax returns and attach all prior returns as exhibits**
- **Many pre-marital agreements undoubtedly included formula clauses that were never addressed in 2009 or early 2010 to plan for repeal**
  - These agreements should be reviewed to ascertain whether the $5M exclusions undermines this intent




## Wealth Transfer Planning After TRA 2010

- Wealth Transfer and Asset Protection Planning After TRA 2010 -

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## General Considerations

- **Draft wills and trusts for flexibility**
  - React to new tax laws
  - React to changed circumstances
  - Just like we did after EGTRRA
- **Patching up trusts and plans already in place**
  - Modifications and reformations
  - Decanting
  - Sales and exchanges to new trusts
  - Disclaimers
  - Organization of new entities and reorganizations of existing entities
  - Change situs of plans




## General Considerations - Continued

- **Keep in mind the axioms of modern wealth transfer and asset protection planning**
  - Own everything in trust forever
  - Make transfer to trusts using:
    - Discountable entities
    - Leveraged gifts and sales
    - Income tax defective trusts
    - Select the most advantageous situs
- **TRA can make all of this planning much easier, efficient and effective**
  - So get it done now!




## Planning After TRA 2010 – Existing Gifts/Sales –

- **Review existing IDITs and Note sales**
  - Can additional seed gifts be infused into the trust using the new $5M exclusion and therefore reduce or eliminate the need for guarantees?
- **Should grantor trust status be toggled off if new outright gifts are made or the estate is well below the $5M exclusion?**
  - Properly plan the "tax burn"
- **Should you keep rolling GRATs or just make outright gifts?**

## Planning After TRA 2010 – New Gifts/Sales –

- GRAT while you can and while interest rates are low
- Discount gifts/sales while you can
  - Assets discounted to $5M and used as "seed money" can support a sale up to $45 million (assuming a 9:1 debt-to-equity ratio)
    - At a 40% discount that's a total of $83.33 million transferred!
    - If each spouse does this – that's a total of $166.66 million transferred!
  - Remember two (2) of the axioms of modern wealth planning
    - Own everything in trust forever
    - Use leverage gifts/sales

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## Planning After TRA 2010 – New Gifts/Sales – Continued

- IDIT and Note Sales with less seed money/guarantee issues because of funding flexibility
- 2013 and the $1M exclusion should be a real problem
- Gift/GST using $5M exclusion
  - Use it while you can and before it is taken away in 2013
    - Also, what happens if it is reduced in 2013?
- Wealth transfer and asset protection planning with disregarded entities
  - Grantor income tax defective trusts and single person LLCs
    - The Pierre case
    - The "double" LLC

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## Planning After TRA 2010 – New Gifts/Sales – Continued

- If the estate tax exemption decreases after making a $5M gift, additional estate tax will be due
  - You may not be able to "lock in" the benefit of the $5M exemption
    - However, the combined gift/estate tax is no more than if the gift had not been made
- Key advantages of gifting:
  - Remove the future appreciation from the estate
  - Fractionalization discounts
  - Reduce the estate by paying income tax on grantor trust income
    - "Tax burn"

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## Planning After TRA 2010 – New Gifts/Sales – Continued

- Watch the impact on tax allocation clauses
  - Who gets what and who pays the tax
    - Even if the tax exemptions reverts back to $1 million
- Should everyone set up a self-settled trust?
  - Alaska
  - Delaware
  - Nevada
  - South Dakota
  - Others

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## Planning After TRA 2010 – New Gifts/Sales – Continued

- Self-settled trusts
  - Structure the trust so that transfers to the trust are completed gifts for gift tax purposes and excluded from the Settlor's gross estate
    - Even though settlor retains powers
    - Even though settlor retains discretionary rights to receive distributions
    - Watch state and bankruptcy creditor rights issues
    - Drafting alternatives to avoid possible estate tax inclusion

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## Planning After TRA 2010 – New Gifts/Sales – Continued

- Consider establishing a Beneficiary Defective Inheritor's Trust ("BDIT")
  - Third party settled trust
  - Beneficiary can:
    - Be the trustee
    - Have distribution rights
    - "Rewrite power" by means of a special power of appointment
    - Complete estate tax protection in perpetuity
    - Complete asset protection in perpetuity
  - Beneficiary is the "grantor" for income tax purposes
- As an alternative: instead of selling assets to a BDIT
    - Is a simple gift to a self-settled trust preferable for mid-range clients seeking asset protection

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## Planning After TRA 2010 - New Gifts/Sales - Continued

- **Fund inter-vivos by-pass trust to lock in the ability to transfer $5M without paying gift tax before the 2013 "sunset"**
  - But will this increase the estate tax if the estate tax exemption does down?
- **Consider Jonathan Blattmachr's "super-charged" credit shelter trust planning**
  - Turning a traditional bypass trust into a grantor defective income tax trust as to the surviving spouse
- **Gift splitting between spouses**
  - Problems if there is a reversion to the $1 million exemption



## Planning After TRA 2010 - Other Planning Issues -

- **Roth conversions**
  - New income tax rates
  - The income tax paid is out of the taxable estate
- **GST Planning**
  - Opting our of automatic allocations
  - Adding non-skip beneficiaries to direct skip trusts
  - Disclaimers
- **Transfers may impact Sec. 6166 deferral and other special provisions**
  - 35% of the adjusted gross estate



## Planning After TRA 2010 - Life Insurance -

- **Some clients will want to cancel policies because they no longer have an estate tax liability**
  - Evaluate this very carefully!
    - Life insurance as an uncorrelated asset class
      - ✓ Modern portfolio theory
      - ✓ Wealth accumulation/retirement plan
      - ✓ Rates of return
    - Risk of 2013 and the $1M exclusions
    - State estate taxes in a decoupled state
    - Liquidity
    - "Graegin" note planning
    - Insurability
      - ✓ Client may never be able to replace
    - Use survivorship policies to cover the lost basis step up-on the $5M bypass trust
    - Supercharging the ILIT funding with the $5M exemption
      - ✓ BDIT planning
    - Others



## Planning After TRA 2010 - Life Insurance - Continued

- **Restructure existing policies to fit the new tax paradigms and economic considerations**
- **Gifts to ILITs to unwind split-dollar and premium financing arrangements**
- **Gift high cash value policies to an ILIT that the $1M gift tax exclusion and limited Crummey powers previously made impractical**
- **Decanting to new trusts**
- **Sales/exchanges to new trusts**
- **Modifications/reformations**
- **Disclaimer planning**



## Planning After TRA 2010 - Asset Protection -

- **$5M gift exclusion is a tremendous benefit to super-charge asset protection planning**
  - Shift large dollars into irrevocable trusts without the issue of the gift tax cost
- **Unwind and fund insurance purchases without split-dollar leakage into the estate of the targeted client**
- **Don't unwind trusts, FLPs and LLCs because of perceived lack of need for estate tax planning**
  - Asset protection planning will remain a critical component of all planning!



## Planning After TRA 2010 - Asset Protection - Continued

- **Can you justify Spousal Lifetime Access Trusts ("SLATs") if there are no estate tax concerns?**
- **However: remember that the ILIT trustee can borrow from the cash value policy and distribute the funds to the spouse, and…**
  - Ultimately, estate tax protected
  - Asset protection
  - The BDIT is probably better anyway!

## Issues in 2013 if TRA Sunsets

- The EGTRRA 2011 repeal was postponed for two years until 2013
- If the repeal happens there are many benefits of EGTRAA which will be lost - e.g.:
  - Repeal of the state death tax credit
  - Loss of liberalization of conservation easement benefits
  - End of of the automatic allocation of GST exemptions to transfers other than direct skips
    - If not renewed, this may change the exclusion ratio as if the allocation had not been made
  - Loss of liberalization regarding qualified severances
  - End of the extension of time to allocate GST exemptions
  - More restrictions on Sec. 6166 estate tax deferral
- Planning point: consider filing gift tax returns and affirmatively allocating GST exemption rather than relying on the automatic allocation rules because of the "sunset" issue



## Conclusion – Thank You Marty Shenkman –

- 2010 Tax Act packs a lot of punch, surprises and complexity into a small number of pages
- Clients/taxpayers view advisers as the little boy that cried wolf – "Oh, so in 2013 there will be a $1M exclusion just like you told me we'd have in 2011?"
- Will taxpayers understand the value of proper planning if there are no tax savings incentives?
- Every document and plan must be reviewed and revised
  - But will clients commit to the effort and cost – especially if 2013 is "Play it Again Sam"
  - Bypass trusts, revised formula clauses with floors and caps and statements of intent, etc.
- Ultra high net worth clients should plan aggressively
  - Get it while you can
  - Wealth transfer tax and asset protected forever



## Asset Protection Other Than Self-Settled Asset Protection Trusts: What Else to do to Frustrate Creditors*

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*Revised and edited by Atty. Robert G. Alexander
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## Asset Protection Planning

- **Asset protection planning is the ideal compliment to estate planning**
- **If you aren't discussing asset protection planning with your clients...**
  - You're hurting your clients
  - You're hurting your business



## Asset Protection Planning

- **Asset protection planning is a form of insurance**
  - You insure your car
  - You insure your house
  - You insure your health
  - You insure your life
  - So you should also "insure" your assets
- **Our goal is to structure the client's assets to either:**
  - Avoid a lawsuit altogether; or
  - Settle a dispute for less than what is owed



## Domestic Asset Protection Trusts

- **One popular asset protection technique is the Domestic Asset Protection Trust (DAPT)**
- **A DAPT is an irrevocable trust set up for oneself in one of the DAPT jurisdictions**
- **What else should we be doing for our clients?**

Employee Retirement Income Security Act (ERISA)

- **ERISA protection**
  - Profit-sharing plans (defined contribution plans)
  - Pension plans (defined benefit plans)
- **At least one non-family employee**

## State Law Exemptions

- **State law exemptions**
  - IRAs – limits?
  - Homestead – limits?
  - Life insurance – limits?
    - ✓ Protects the cash value and death benefit?
    - ✓ Protects the death benefit only?
    - ✓ No protection at all?
  - Annuities – limits?

## Charging Orders - LLCs/LPs

- **Charging order protection**
  - What is it?
  - Why is charging order protection good, but not perfect?

## Charging Orders - Single Member LLC

- **Case law**
  - 2003 - Ashley Albright (Colorado)
  - 2006 - A-Z Electronics, LLC (Idaho)
  - 2006 - In re Modanlo (Maryland)
  - 2010 - Olmstead v. FTC (Florida)
- **State legislation**
  - Wyoming - 2010
  - Nevada - SB405 (2011 legislative session)

## Charging Orders - Corporations

- **Nevada is the only state where corporations get charging order protection**
  - More than 1 shareholder / Less than 100 shareholders
  - SB405 (2011 legislative session) – if it passes, it will include single shareholder corporations

## Charging Orders - Opportunities

- **Pick a state where charging order is exclusive remedy**
  - Set up new company, or
  - Domestication (statutory conversion), or
  - Merger, or
  - Set up holding company

## Charging Orders - Examples

- Example #1: California LLC with $2M of marketable securities
- Example #2: California LLC with $2M business
- Example #3: Five California LLCs each with real estate

## Charging Orders - Extra Buffer

- Example: Three business partners each own 1/3 of LLC
  - Assume charging order protection
- Why might we have our client put his 1/3 interest in additional LLC?

## Third-Party Irrevocable Trusts

- Third-party trusts are irrevocable trusts in which the settlor is not a beneficiary
- The $5M gift tax exemption opens up huge opportunities
  - Use a transfer tax strategy as an asset protection tool
  - Trust for spouse and descendants
  - Trust for descendants

## Trust for Spouse and Descendants

- Settlor retains the power to fire and hire trustees
- Use a "floating spouse" provision
- Might draft the trust so it splits for the descendants at death of survivor of settlor and settlor's spouse
  - Why?

## Trust for Descendants

- Do you ever hear of anyone doing this as an asset protection tool for the settlor?
  - We never do!
- Settlor retains the power to fire and hire trustees
- If settlor loses his assets, his children can take care of him

## Irrevocable Trusts - Examples

- Example #1: $5M net worth
  - Gift $1M into trust for spouse and descendants (or for desc. If no spouse)
- Example #2: $10M net worth
  - Gift $2M to $3M into trust for spouse and descendants (or for descendants if there is no spouse)
- Example #3: $20M net worth
  - Gift $5M into irrevocable trust for spouse and descendants (or for descendants if there is no spouse)
  - Can leverage the $5M with valuation discounts, installment sales, etc.

## Combining Trusts with Charging Order Protection

- **In all three Examples, what do we do with the other assets?**
- **Charging order protection**
- **The ability to indirectly live out of the trust through your family is what makes the charging order over the other assets work so well**


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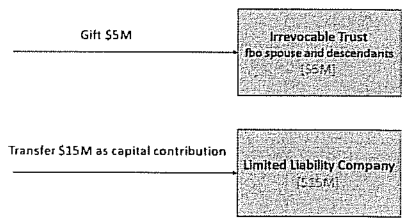
## Combining Trusts with Charging Order Protection

Why does this combination work so well?





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## Third-Party Discretionary Trusts

- **Third-party discretionary trusts**
  - Discretionary trusts (sole and absolute discretion)
  - Support trusts (such as "health, education, maintenance and support")


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## Support Trust

- **Support Trust**
  - What is it?
  - Most are health, education, maintenance and support
  - Relies on spendthrift provision
  - Statutory exception creditors
  - Judicially created exception creditors


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## Support Trust - Exception Creditors

- **Exception creditors – Restatement Second of Trusts**
  - Alimony or child support,
  - Necessary services or supplies rendered to the beneficiary (such as medical services),
  - A claim by the U.S. or a state to satisfy a claim against a beneficiary (such as a tax lien), and
  - Services rendered and materials furnished that preserve or benefit the beneficial interest in the trust (such as attorneys' fees to protect a trust)


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## Discretionary Trust

- **Discretionary trust**
  - "Sole and absolute discretion"
  - "Unreviewable by a court of law"
  - Doesn't have to rely on a spendthrift provision


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## The Nevada Asset Protection Trust
## - Combining it with the Double Nevada LLC -

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## Asset Protection Planning

- **Asset protection planning is a form of insurance**
  - You insure your car
  - You insure your house
  - You insure your health
  - You insure your life
  - So you should also "insure" your assets
- **Our goal is to structure your assets to either:**
  - Avoid a lawsuit altogether; or
  - Settle a dispute for less than what is owed



## Domestic Asset Protection Trust

- **A DAPT is a U.S. asset protection trust in which the trust grantor is a permissible beneficiary**
- **Twelve states allow DAPTs**
  - 2-yr. statute of limitations – Nevada
  - 3-yr. statute of limitations – South Dakota, Utah
  - 4-yr. statute of limitations – All other states



## Statutory Exception Creditors

- **Eleven of thirteen states have statutory exception creditors**
  - Such as divorcing spouses
  - Such as preexisting tort creditors
- **Nevada and Alaska – the only states with no statutory exception creditors**

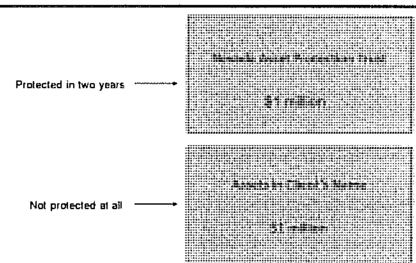


## Comparing Statutes of Fraud

- **Nevada: 2-yr. statute of limitations / no statutory exception creditors**
- **Alaska: 4-yr. statute of limitations / no statutory exception creditors**
- **Therefore, Nevada may be the best state for domestic asset protection trusts**



Nevada Asset Protection Trust with No LLCs: Example - $2 million



## Here Come the Creditors

- So now what happens?



## Nevada Asset Protection Trust with No LLCs: Example - $2 million

Nevada Asset Protection Trust

$1 million

Protected in two years

First two years: $2 million lost

After two years: $1 million lost



## Nevada Limited Liability Company

- Nevada law makes the "charging order" the exclusive remedy of a judgment creditor
  - As do some other states
- A "charging order" is a lien
- So a creditor can only get a lien on the LLC membership interest and can't force a distribution
- Now combine the LLC with the NAPT



## Nevada Asset Protection Trust with One LLC: Example - $2 million

Nevada Asset Protection Trust

Immediate charging order protection

Nevada LLC

Client = 1% voting
NAPT = 99% non-voting

$1 million

Not protected at all

Assets in Client's Name

$1 million



## Here Come the Creditors

- So now what happens?



## Nevada Asset Protection Trust with One LLC: Example - $2 million

Nevada Asset Protection Trust

Immediate charging order protection

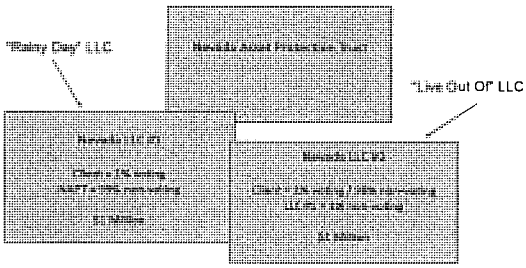
Nevada LLC

Client = 1% voting
NAPT = 99% non-voting

$1 million

$1 million lost

### Nevada Asset Protection Trust with Two LLCs: Example – $2 million



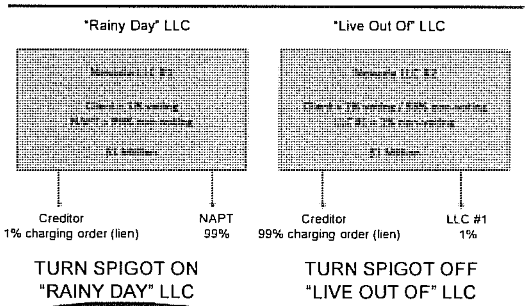



## Here Come the Creditors

- So now what happens?



### Nevada Asset Protection Trust with Two LLCs: Example – $2 million






## Summary of $2 Million Example

- **NAPT with no LLC**
  - 1st two years – Protect $0M / Lose $2M
  - After two years – Protect $1M /Lose $1M
- **NAPT with one LLC**
  - 1st two years – Protect $1M / Lose $1M
  - After two years – Protect $1M / Lose $1M
- **NAPT with two LLCs**
  - 1st two years – Protect $2M / Lose $0M
  - After two years – Protect $2M / Lose $0M



### The Beneficiary Defective Inheritor's Trust – Creating the Ideal Wealth Transfer and Asset Protection Plan –

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### The Ultimate Trust! A Beneficiary Defective Inheritor's Trust

- **Combines:**
  - A third-party settled trust with
  - Grantor trust income tax status for the beneficiary
- **Finessing the "pipe dream"**

Understanding the Dynamics of Modern Wealth Planning

- **What our clients need is also what our clients want!**
- **The eight essentials of advanced wealth planning – the "pipe dream" plan**
  - Freeze the size of the estate
  - Transfer wealth on a leveraged basis
  - Income tax planning
    - The "tax burn"
    - Family income tax planning
    - State income tax planning - situs



Understanding the Dynamics of Modern Wealth Planning - Continued

- **Multi-generational/dynasty planning**
- **Family wealth management and control**
- **Protect assets from predators, creditors, and divorces**
- **Flexibility to modify or change the plan downstream – changing circumstances**
- **A "no-risk" plan**
- **In other words – I want to have my cake and eat it too!**



## The "Ideal" Estate Plan – The BDIT –

- **A trust set up for my benefit in which I have:**
-
  - The opportunity for income tax deferred (and preferably tax-free) wealth compounding
  - The ability to access the income from my property until my death
  - The ability to have my assets available for my use and enjoyment until my death



## The "Ideal" Estate Plan - Continued

- **A trust set up for my benefit in which I have:**
  - The right to decide who will receive my property at my death or during my lifetime
  - The power to determine in what form and when my beneficiaries ultimately will inherit my wealth
  - The right to manage, control and use my wealth until my death



## The "Ideal" Estate Plan - Continued

- **A trust set up for my benefit in which I have:**
  - The ability to protect my wealth from creditors, including divorcing spouses, in perpetuity
  - The opportunity for income tax benefits and estate tax savings
  - The ability to keep my wealth outside the transfer tax system in perpetuity



## The "Ideal" Estate Plan - Continued

- **A trust set up for my benefit in which I have:**
  - The ability to "rewrite" the plan in order to react to changed circumstances
- **All of this "risk free"**
- **The ultimate comprehensive wealth accumulation, estate, asset protection and retirement plan!**

## So What Is A BDIT?

- **A dynasty trust set up for my descendants which avoids their**
  - Transfer taxes
  - Creditors, including divorcing spouses
- **A beneficiary "controlled" trust**
- **Allows gifts and sales to a trust that is income tax defective as to the beneficiary**
  - Crummey power of withdrawal – § 678
- **Wealth transfer leveraging with discounted entities**




## So What is a BDIT - Continued

- **Combines the planning opportunities of:**
  - Chapter 13 – GSTT rules
  - IRC § 678 – beneficiary income tax status
  - Rev. Rul. 85-13 – non-recognition of sales to IDITs
  - Rev. Rul. 93-12 – no family attribution rules for purposes of discounting
  - Rev. Rul. 2004-64 – no additional gift on payment of income tax




## BDIT Design

- **Established and initially funded by a third party**
- **Fully discretionary distribution standards**
- **Controlled trusteeship**
  - Family trustee
  - Independent trustee
- **The "use" concept**
- **Broad SPA – a "re-write" power**
- **Perpetual**
- **Beneficiary has the functional equivalence of outright ownership of the trust assets**




## BDIT Tax Results

- **Estate freeze**
  - Installment notes in the estate
  - Post-transfer appreciation shifted
- **Estate squeeze**
  - Discounted assets removed from the transfer tax system
- **Income "tax burn" – the beneficiary pays the tax on the income generate by the trust**
  - Section 678
  - Crummey power of withdrawal




## BDIT Non-tax Results

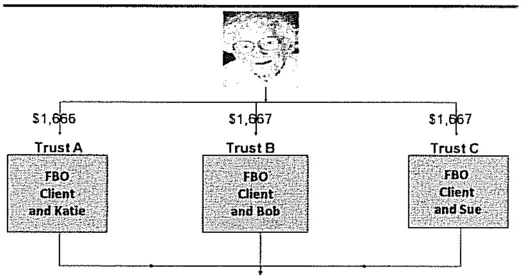
- **The client/beneficiary is in control of the BDIT**
- **Assets are creditor protected for the client/beneficiary and his/her family**
- **Assets are available after the "tax burn"**
- **Client/beneficiary has a "re-write" power with a SPA**
  - Protects against potential family conflicts
  - Protects against inadvertent gifts to the trust




## BDIT Non-tax Results - Continued

- **Opportunity shifting**
  - Business and investment opportunities
  - Giving free advice or managing trust assets
- **Quintessential life insurance trust**
  - Life insurance on a beneficiary who is also a trustee
  - Decision must be made by an independent trustee
  - Beneficiary cannot have a SPA over life insurance

## Seeding the Trust – Gifts to Trust

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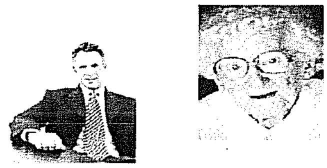
## Transfer Tax & Creditor rights

- **Who is the Grantor?**
- **Owner for Income Tax Purposes - IRC § 678(a)**



Caveat: Client has a Power of Withdrawal over all gifts to BDIT
Caveat: Client never makes a gratuitous transfer to BDIT

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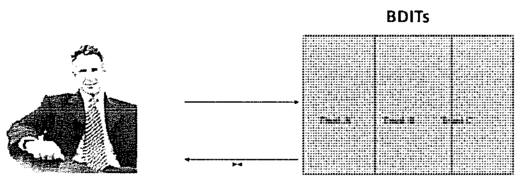
## Tax-Free Sale to BDIT – Assets –Installment Notes

- **Wealthy client sells discountable income producing assets for an Installment Note**

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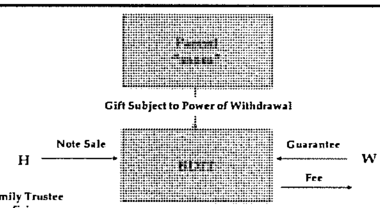
## Note Sale to a BDIT with a Guarantee




1. Family Trustee
2. Beneficiary
3. I/T Grantor
4. Seller

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## Planning Opportunities - Continued

- **Grantor trust income tax planning**
- **Sales of "hot" assets – IRC§ 751**
- **Structuring buy-sell arrangements**
- **State income tax planning**
- **Multi-jurisdictional asset protection planning**
- **Private retirement plan**

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## Planning Opportunities - Continued

- **Advanced Life Insurance Planning**
  - Access to cash values
  - No transfer for value problems
  - Super-charge the insurance funding
  - Super-charge life insurance partnership planning
  - Premium financing techniques
  - Split dollar arrangements

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## Wealth Planning with Disregarded Entities


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## Goal

- **To Transfer Substantial Wealth**
  - Wealth Transfer tax-free
  - Income tax-free



## Modern Wealth Planning

- **The interaction and blending of several important components:**
  - Trusts
    - Dynastic
    - Income tax defective with respect to:
      - ✓ the grantor (IRC §§ 671-677); or
      - ✓ to the beneficiary (IRC § 678)
    - Split-interest trusts – GRATs



## Modern Wealth Planning

- **Enhancing the Wealth Shift by Adding the "Disregarded Entity" Component**

□ X



### Enhancing the Wealth Shift by Adding the "Disregarded Entity" Component

- **Entities which are disregarded for income tax purposes, but are recognized for state law and wealth transfer tax purposes**
- **The assets being transferred have low cash flow or cash flow insufficient to pay solely out of cash flow:**
  - the GRAT annuity; or
  - the installment obligation
- **The goal is to avoid "in-kind" payments to the grantor that will be subject to valuation discounts**



### Enhancing the Wealth Shift by Adding the "Disregarded Entity" Component

- **The client would like to leverage the wealth shift, and**
  - Maintain management and control
- **The entity has low basis assets that we would like to use in the wealth shifting process, but which we would like to receive back so that they will receive a set-up in basis at death**

## Sample Client Profile

- $10 million real estate property
- Cash flow 5%, appreciation 5%
- Three children
- Desire to give 1/3 to each child
- Assume 40% valuation discount
- Assume
  - AFR 6%
  - Annual Midterm Rate 5%



## Our Unique Problem

- Major assets have a low cash flow - 5%
- GRAT - Actual payment of the annual annuity must be made. Treas. Regs. §25.2702-3
- IDGT - Interest and balloon payment must be paid
- Desire to contribute discountable assets and receive back non-discountable assets



## Concepts We Will Be Using

- Income Tax Defective Trust
  - Rev. Rul. 85-13
- Disregarded Entity
- The Estate Planner's Dream –

"Passing on More Wealth Than Meets the Taxable Eye"



## Planning The Estate Planner's Dream

- Transfer discountable, income – producing property
- Receive back cash (or non- discountable assets)
  - In effect, the discount is passed on tax-free to the donor in a tax-free transfer



## Disregarded Entity

- Single owner entity that has not elected to be classified as an association (corporation)
  - IRC §7701; Treas. Reg. §§301.7701-1(a) and 301.7701-2(c)(2)
- Entity existence is ignored
  - A "tax nothing"
- Concept similar to the "Defective Trust" concept



## Disregarded Entity

- Rev. Rul. 2004-77
  - An eligible entity with two owners under local law can be treated as a disregarded entity
- Rev. Rul. 2004-88
- Other Examples
- Pierre v. Comm'r, 133 T.C. No. 2 (Aug. 24, 2009)

# GRAT/DISREGARDED ENTITY COMBO

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## GRAT

- **Gift to trust in exchange for an annuity substantially equal in value to transferred property**
- **Generally annuity increases by 20% a year**




## Low Cash Flow GRAT

- **For transfer tax purposes, no aggregation of transfers to separate trusts. Rev. Rul. 93-12**





## GRAT Illustration
### Graduated 10-Year: 5% income, 5% growth

| | |
|---|---|
| §7520 Rate: | 6.00% |
| Income Earned by Trust: | 5.00% |
| Term: | 10 |
| Annual Growth of Principal: | 5.00% |
| Pre-discounted FMV: | $10,000,000 |
| Discounted FMV: | $6,000,000 |
| Percentage Payout: | 5.69699% |
| Annual Annuity Payment Growth: | 20.00% |
| Value of Grantor's Retained Interest: | $5,999,990.11 |
| Taxable Gift: | $9.89 |




## GRAT Illustration
### Graduated 10-Year: 5%income, 5% growth

| YEAR | BEGINNING PRINCIPAL | 5.00% GROWTH | 5.00% ANNUAL INCOME | ANNUAL PAYMENT | REMAINDER |
|---|---|---|---|---|---|
| 1 | $10,000,000.00 | $500,000.00 | $512,500.00 | $341,819.40 | $10,670,680.60 |
| 2 | $10,670,680.60 | $533,534.03 | $546,872.38 | $410,183.28 | $11,340,903.73 |
| 3 | $11,340,903.73 | $567,045.19 | $581,221.32 | $492,219.94 | $11,996,950.30 |
| 4 | $11,996,950.30 | $599,847.52 | $614,843.70 | $590,663.92 | $12,620,977.60 |
| 5 | $12,620,977.60 | $631,048.88 | $646,825.10 | $708,796.71 | $13,190,054.87 |
| 6 | $13,190,054.87 | $659,502.74 | $675,990.31 | $850,556.05 | $13,674,991.87 |
| 7 | $13,674,991.87 | $683,749.59 | $700,843.33 | $1,020,667.26 | $14,235,557.22 |
| 8 | $14,038,917.53 | $701,945.88 | $719,494.52 | $1,224,800.71 | $14,415,452.38 |
| 9 | $14,235,557.22 | $711,777.86 | $729,572.31 | $1,469,760.85 | $14,207,146.54 |
| 10 | $14,207,146.54 | $710,357.33 | $728,116.26 | $1,763,713.02 | $13,881,907.11 |
| SUMMARY | $10,000,000.00 | $6,298,809.02 | $6,456,279.23 | $8,873,181.14 | $13,881,907.11 |




## Options to Pay Annuity

- **"In Kind" distributions of LLC**
- **interests**
  - Grantor trust – no income tax on
  - payments "in kind" of appreciated
  - property
  - Discountable
  - Appraisal and valuation problems
  - Future growth back in estate
    - ✓ Reduces wealth transfer
    - ✓ Violates to goal of receiving assets back
    - ✓ not subject to discounts

## Options to Pay Annuity - Continued

- **Purchase the property from the LLC**
  - LLC owns 100 % of property
  - Purchase is of 100% of property
  - No discount
  - Can be by note
    - » Potential cash flow issue
    - » Can use GRAT annuity payments to
    - ✓ alleviate cash flow problems




## How Does The "Disregarded Entity"/GRAT Income Tax Combo Work?

- **GRATs are grantor trusts. IRC §§673(a),677(a)**
- **Each GRAT is "owned" by the grantor for income tax purposes**
- **Entity with a single owner is disregarded. IRC §7701**




## GRAT Illustration
### Graduated 20-Year: 2%income, 6% growth

| | |
|---|---|
| §7520 Rate: | 6.00% |
| Income Earned by Trust: | 2.00% |
| Term: | 20 |
| Annual Growth of Principal: | 6.00% |
| Pre-discounted FMV: | $10,000,000 |
| Discounted FMV: | $6,000,000 |
| Percentage Payout: | 1.27810% |
| Annual Annuity Payment Growth: | 20% |
| Value of Grantor's Retained Interest: | $5,999,996.99 |
| Taxable Gift: | $3.01 |




## GRAT Illustration
### Graduated 20-Year: 2% income, 6% growth

| YEAR | BEGINNING PRINCIPAL | 6.00% GROWTH | 2.00% ANNUAL INCOME | ANNUAL PAYMENT | REMAINDER |
|---|---|---|---|---|---|
| 1 | $10,000,000.00 | $600,000.00 | $206,000.00 | $76,686.00 | $10,729,314.00 |
| 2 | $10,729,314.00 | $643,758.84 | $221,023.87 | $92,023.20 | $11,502,073.51 |
| 3 | $11,502,073.51 | $690,124.41 | $236,942.71 | $110,427.84 | $12,318,712.79 |
| 4 | $12,318,712.79 | $739,122.77 | $253,765.48 | $132,513.41 | $13,179,087.63 |
| 5 | $13,179,087.63 | $790,745.26 | $271,489.21 | $159,016.09 | $14,082,306.01 |
| 20 | $25,897,090.02 | $1,553,825.40 | $533,480.05 | $2,449,964.32 | $25,534,431.15 |
| SUMMARY | $10,000,000.00 | $22,221,429.62 | $7,629,357.47 | $14,316,355.94 | $25,534,431.15 |




## Comparison of GRAT Results

- **Level payment GRATs has insufficient cash flow beginning in year one (1)**
  - Must make payments "in-kind"
- **Increasing payment GRAT has insufficient cash flow beginning in year (5)**
  - Must make payments "in-kind"
- **GRAT with disregarded entities is able to make payments out of cash flow for every year, beginning in the first year**




## Note Sale to IDGT/Disregarded Entity Combo

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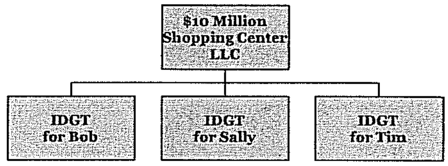
## IDGT - Note Sale

- **Non-controlling interests are sold to an income tax defective trust in exchange for an installment note, generally interest only with a balloon payment.**



## Low Cash Flow Note Sale

- **For transfer tax purposes, no aggregation of transfers to separate trusts. Rev. Rul. 93-12**






## Note Sale to IDGT with Low Cash Flow Asset

- **Interest paid from**
  - "Seed" money
  - Cash flow
- **When "seed" money and cash flow insufficient – buy asset from entity**



## Alternatives to QPRTs – Qualified Personal Residence Trusts and Alternative Solutions –

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## What is a QPRT?

- Grantor transfers residence to trust
- Grantor retains:
  - Right to use and occupy residence for
  - specified term; and
  - Contingent reversionary interest



## QPRT Disadvantages Which We Want to Eliminate or Reduce

- **Large gift**
- **Mortality Risk**
- **Prohibition against reacquisition**
  - To obtain step-up in basis at death
  - To live in residence
- **Complex, rigid regulatory requirements**

## QPRT Strict Regulatory Rules

- **Reg. §25.2702-5(c) contains a long list of requirements**
- **Reacquisition of residence prohibited either during or after the term - Reg. §25.2702-5(b)(9)**




## QPRT v. GRAT

- **Unified credit used**
  - QPRT substantial
  - GRAT insignificant
- **Term – risk of estate tax inclusion**
  - QPRT substantial
  - GRAT term can be condensed
- **Right to reacquire property in GRAT**




## QPRT v. IDGT

- **Sale v. Gift**
- **Survivorship feature**
- **Right to reacquire property**
  - To own
  - To obtain basis step-up
- **Generation-skipping**




## Other Applications

- **Double LLC Technique**
- **SCIN/ GRAT Technique**
- **Nevada Asset Protection Trust with Two (2) LLCs**
- **Beneficiary defective Inheritor's Trust ("BDIT")**




## Selected Additional Sources of Information

- www.laweasy.com articles and other updates
- www.estateplanninganswers.org NAEPC website for the public
- American Bar Association Section of Real Property Trust & Estate Law. Webinar "Planning with the TRA 2010 Transfer Tax Rules: The Sun Has Risen. January 6, 2011. 331 pp.
  - Regular section webinars
- www.lorman.com 90-minute webinar "Responding to the New Estate Tax Bill" with more extensive handouts and CPE/CLE credit. December 30, 2010 and January 18, 2011, 1-2:30 p.m. EST.
- www.amazon.com 120 page e-book "Estate Planning After the 2010 Tax Act" available December 27, 2010. Martin A, Shenkman




## Selected Additional Sources of Information

- AICPA – www.cpa2biz.com expanded 150+ page professional book "Estate Planning after 2010 Tax Act" with accompanying podcast, power point for professionals and another for consumers, practice aids, checklists, etc.
  - Martine A. Shenkman and Steve Akers
- Leimberg LISI – NAEPC partner
- NAEPC Journal of Estate and Tax Planning
  - www.naepc.org
- CCH Wolters Kluwer - Library of publications and webinars
  - NAEPC partner

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