Trust Administration: Practical Considerations for Practitioners

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Trust Administration

Some Basic Suggested Steps To Consider

Trust Administration Preliminary Steps – Representation

- Clarify who the adviser is representing. Everyone may think the attorney who drafted the trust is representing them too: trustee, beneficiary, trust protector, etc.

Trust Administration Preliminary Steps – Annotate the Trust

- Create a trust annotation highlighting key persons and terms.
- Our approach: we convert a PDF of the trust document to word. Highlight key provisions relevant to trust. administration in yellow and add annotations to ourselves or the clients in green as steps to take to conform to the trust provisions.
- Create a summary in plain English (but note its not “official” and the document itself controls.)
- The goal is to create a roadmap that can be modified as new issues arise or facts change.

Trust Administration Preliminary Steps – Summary

- Create a trust summary of key persons and terms. Cross reference to section in the document and the pages where they appear.
- A simplified page or two summary can be valuable to all involved for a quick overview.
- For clients with many trusts a trust listing can be helpful.

Trust Administration Preliminary Steps – "Closing Binder"

- Create a trust electronic compilation of all documents and a table of contents.
- It is helpful for complex trust plans to have a compilation of all relevant documents in logical order.
- The contents listing for this compilation is a great starting point for the exhibit list for the Form 709 gift tax return, if one needs to be filed.
- We have never found a single trust where documents or steps were not identified as missing or incomplete when creating such a compilation. We believe this is a vital step to assuring that no loose strings exist.
- Explain to the client that minor foot faults should be identified and addressed before an audit. The Smaldino case is a reminder of this.
- Proactively addressing any issues identified, thereby showing a good faith effort, may affect the demeanor of an auditor on a future audit.

Sample Workflow- 1

Example of Workflow & Project Management

PIONEER WEALTH PARTNERS

Wanda Lucky Descendants' Trust

CLOSING CHECKLIST

Purchase of 99.99% Limited Partnership Interest in Smith Holdings I LP by the Trustees of Smith Descendants' Trust from the Trustees of John Smith Marital Trust

Action	*Responsible Party*[1]	*Target Date*	*Completed*
Creation and Funding of Marital Trust:			
1. Execution of Trust Agreement by John Smith, as Grantor, John Smith, as Investment Trustee, Jack Jones, as Independent Trustee, and Alaska Trust Company, as Administrative Trustee (the "Marital Trust").	MTHM, JS, JJ and ATC	Third week in June	Yes
2. Trustees of the Marital Trust open Bank/Brokerage Account and fund the Trust in an amount necessary to meet administration expenses, i.e., approximately $50,000.	JS and JJ	Third week in November	Account opened

Note:
1. Responsible Party generally means the person who must sign certain documents. We appreciate that John Smith and Wanda Lucky likely will be the persons who will ensure many of the steps will be taken.

Sample Workflow- 2

Example of Workflow and Project Management (cont'd)

PIONEER WEALTH PARTNERS

	Action	Responsible Party[1]	Target Date	Completed
28	Prior to April 15, 2008, a gift tax return must be filed for David showing the initial contributions to the Management Trust, the Marital Trust and the Descendants' Trust, making a QTIP election for the contributions to the Marital Trust, and allocating David and Mary Smith's GST Exemption to the initial transfer to the Descendants' Trust.[3]	JJ, JS and MS		*Confirm dates contributions were made*
29	Interest on Promissory Notes to be paid annually on the anniversary of the date of the Promissory Note with principal payable on the maturation date. We will prepare a payment schedule.	JS and JJ		No

Key

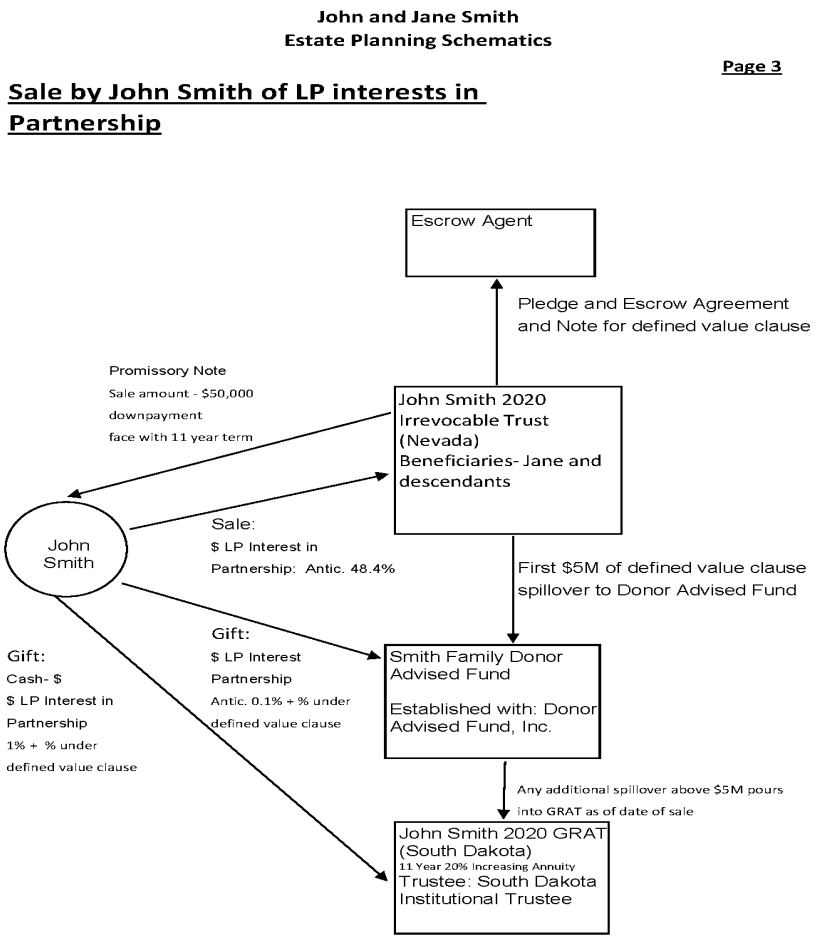
ATC	–	Alaska Trust Company
JJ	–	Jack Jones
JS	–	John Smith
MS	–	Mary Smith
MTHM	–	Milbank, Tweed, Hadley & McCloy LLP
WL	–	Wanda Lucky

Note:
3. The gift to the Descendants' Trust may be "split" with Mary. The gift to the Marital Trust may not be split but there should be no gift tax due with respect to the gifts to those trusts.

Trust Administration Preliminary Steps – Schematic

- Create a schematic of the plan. Many plans have so many moving parts that without a schematic it will be difficult or impossible for anyone to follow the sequence of the transaction.
- If a client has several trusts, consider creating an additional “snapshot” schematic showing the interaction of the various trusts and asset ownership. Providing a client with a simplified single page schematic representing their planning may help the client feel less overwhelmed with the planning implemented.

Sample Note Transaction Schematic with Defined Value Mechanism Waterfall



Trust Administration

Trust Terms Affect How You Administer the Trusts

Avoiding an Unwanted Transfer via Disclaimer

- Does the trust have (or does state law provide) a disclaimer mechanism? Has that mechanism and the time limit to act been reviewed with the client?
- Some trusts include a provision permitting one beneficiary to disclaim on behalf of all trust beneficiaries. That should give 9 months to look for a disclaimer to disclaim which under Sec. 2518 would result in the exemption not being used and the assets being restored and assets reverting to the settlor.
- The above mechanism can be integrated into a new trust but for an old/existing trust the right may have to be included in the transfer documents. So, you may have to review ancillary documentation in addition to the trust.
- Other commentators suggest the above won't work for a pot trust and the trust must be solely for the person holding the power to disclaim. Others disagree. If this was done, then a LPOA may have to be exercised to get the trust where the client intended.

Was a QTIP-able Trust Used?

- Some clients made transfers to a trust that will qualify for the marital deduction if a QTIP election is made on a gift tax return by the 2021 extended filing date. The trust may provide that if the election is not made the assets would pass to a non-marital deduction trust for the surviving spouse that would use exemption.
- Have you identified this attribute in the trust? Has this been reviewed with the client to determine what position should be taken? Can a trust be decanted and still disclaimed?

Defined Value Clauses – 1A Wandry

- Determine what type of defined value mechanism was used in each transaction and be certain that forms 709s, 1040s and 1041s, and other statements such as K-1s, properly reflect the existence of such a mechanism.
- Defined value clauses - Wandry.
  - Defined value clauses endeavor to deflect a gift tax valuation challenge by defining the gift in a manner that mitigates the impact of an IRS valuation challenge.
  - Wandry clauses are the most common approach as they are simple and inexpensive to implement.
  - A more complex approach may be safer.
  - I gift (sell) $_____ worth of LLC interests. Those interests have been estimated based on an appraisal to be _____% of the LLC. The actual percentage interest given/sold shall be determined by the value finally determined for federal gift tax purposes.

Defined Value Clauses – 1B Wandry

- Tax Court in *Wandry* T.C. Memo 2012-88 upheld the defined value mechanism based on the specific wording of the clause in the assignment documents.
- IRS issued a statement refusing to acquiesce to the Tax Court's conclusion, signaling strong disagreement of *Wandry* (Action on Decision 2012-004) – but not enough to appeal the case. It seems appropriate to recommend for a client to consider other options (see below), as Wandry is not the guarantee some practitioners might believe.
- *Wandry* approach results in only the intended dollar amount of the assets being transferred with any excess above that amount remaining in the transferor's estate.
- Any assets remaining in the transferor's estate are subject to future estate tax.
- Confirm that bank trust records, client and trust financial statements, all reflect the uncertainty of ownership interests if applicable under the precise mechanism used.

Defined Value Clauses – 2 Christenson/Petter Waterfall

- Defined value clauses can be structured in a different manner than Wandry. Some commentators believe these approaches are safer.
  - The client parts with 100% of the desired interests in the transfer. This contrasts with Wandry were some of the interests may not be transferred in the transaction.
  - I hereby transfer all of my rights and interests in XYZ, LLC pursuant to this transaction. I gift (sell) $_____ worth of LLC interests to the Smith Family Trust. Those interests have been estimated based on an appraisal to be _____% of the LLC. The actual percentage interest given/sold shall be determined by the value finally determined for federal gift tax purposes as of the date of this transfer. Any interests in XYZ, LLC not transferred to the Smith Family Trust above shall pass to the Smith Family Donor Advised Fund, up to a maximum amount of $2 million dollars. Any excess value over the amounts transferred to the Smith Family Trust and the Smith Family Donor Advised Fund are hereby transferred to [Smith Family GRAT] [Smith Family Incomplete Gift Trust] [John Smith Marital Trust], etc.
  - The benefit of this type of waterfall clause is that the client has parted with all interests no matter what the values are. Consider how to deal with income tax reporting?

Defined Value Clauses – 3
Nelson Case

- Nelson case.
  - Nelson v. Commissioner, T.C. Memo 2020-81: the taxpayer's valuation adjustment mechanism failed because it did not use the requisite language of referring to: gift tax value as finally determined for federal tax purposes and instead had a reference to an appraised value.
  - The value used in a valuation adjustment mechanism must be based on the gift tax value as finally determined for federal gift tax purposes. In Nelson the value of a baule (a piece of art) was based on the appraisal. Use the language used in the case law like Wandry, don't vary from that.
  - CPAs should review the language and if it is wrong, advise counsel to correct the documentation if feasible. Also, consider what should be disclosed on a gift tax return. If the language in the Wandry clause is not sufficient and a revision is made, should both documents be attached as exhibits for "adequate disclosure"?

Defined Value Clauses – 4 Double Wandrys

- One problem with a Wandry clause is that some portion of the equity interests the client is shifting out of their estate may remain in the estate if there is a valuation adjustment. That is because only a fixed dollar value is transferred. But as suggested earlier, a Wandry clause can be used to define one part sold/given and the balance otherwise disposed of (similar to a will that divides a married decedent's property into marital and non-marital deduction shares.)
- Having a residual interest in the estate could be particularly problematic if discounts are repealed, transfers to grantor trust included in the grantor's estate, and other changes enacted.
- One solution is to use the Petter/Christenson waterfall as discussed above.
- Another approach is to use what might be referred to as a "double Wandry." The "first" part of the Wandry is the traditional Wandry transfer. The "second" or "double" portion of the Wandry is to sign a secondary sale agreement that sells, effective as of the date of the initial transfer, any equity remaining in the client's estate, at the gift tax value as finally determined.
- This approach removes 100% of the desired interests from the estate and should do so without gift tax implications.

Defined Value Clauses – 5 Double King

- A King price adjustment mechanism increases the face amount of the note to equal any gift tax value as finally determined. So instead of changing the percentage of shares transferred, or allocating using a waterfall, the note amount on a sale is increased to reflect the proper value.
- This is based on a 10th Circuit case, King v. United States, 545 F.2d 700 (10th Cir. 1976). Some commentators do not suggest that a King clause because it is only a 10th Circuit case and may not be as secure as a Wandry clause which is based on a Tax Court case. Other commentators suggest that since King adjustments are commonly used in the business world that there is significant merit to the technique. On the latter point, some commentators suggest that King adjustment mechanisms should be used in transactions that have a business context.
- In a client's haste to complete planning before changes in the law, if a King note adjustment mechanism is used, does the transfer have to wait to receive the valuation? Yes.
- But if the client is anxious to close the transfer, perhaps an estimate of value can be used. Then, when the appraisal is received the King note will be adjusted. The "second" or "double" adjustment will occur for gift tax value as finally determined in which case the note will be adjusted a second time.

Estate Tax Planning Considerations in Trust Administration

- Practitioners must monitor key tax strategies built into the trust. First, review the trust and overall plan to determine what mechanisms may be involved. Then review current facts and confer with the client to determine if action is advisable.
- Basis maximization can provide valuable income tax planning opportunities, and irrevocable trusts can be tailored to facilitate this through:
  - Distribution of assets to beneficiaries, e.g., a spouse/beneficiary of advanced age.
  - Use of powers of appointment, e.g., given to an elderly parent a general power of appointment to cause trust assets to be included in their estate and to achieve a basis step up during the grantor's lifetime or to trigger the Delaware Tax Trap per Section 2041(a)(3).
- Swap powers (see section 675(4)(c)) can provide more flexibility to maximize income tax basis or accomplish several other important planning goals. The traditional application of a swap power is for an elderly or infirm grantor to swap cash into the trust in exchange for highly appreciated trust assets. Have assets appreciated? Has the power holder's health deteriorated?

Trust Protectors

- If Trust Protectors are named in the instrument, what powers do they hold? There is no standardization to the powers given so that you must review them to ascertain what can be done.
- This position has become more common in irrevocable trusts. Giving a protector, acting in a fiduciary capacity or in a non-fiduciary capacity (you need to know which capacity the trust protector is serving in, as that may affect the ability to exercise various powers), the power to change the governing law and situs, and so forth, infuses flexibility to respond to future changes. Is a change warranted?
- Caution – naming a protector who is a fiduciary as opposed to someone merely holding a special limited power of appointment in a non-fiduciary capacity might subject a trust, once no longer a grantor trust, to state tax nexus based on the residence of the protector. One approach suggested to mitigate this risk is to “house” all ancillary functions (trust protector, investment adviser, etc.) inside an LLC formed in the trust friendly jurisdiction where the trust is based. Has this been reviewed?

Trust Protector Possible Powers

- The power to remove Trustees.
- The power to appoint an individual, corporation or other entity with fiduciary powers to replace any removed Trustee, or to add a new additional co-Trustee.
- The power to appoint an individual, corporation or other entity who is not related or subordinate to the Grantor or the Beneficiaries with fiduciary powers to exercise powers granted in this Trust. Rev. Rul. 95-58 safe harbor.
- The power to change situs and governing law of the trust, correct scrivener's errors, modify administrative provisions that have no effect on the beneficial interests in the trust.
- The power to modify or amend the supplemental needs trust provisions herein to conform with any changes in applicable law.
- The power to restrict or eliminate the right of the Trustee to apply the income of this trust to pay life insurance premiums on the life of the Grantor and/or the Grantor’s spouse.
- Note that even if falling under the Rev. Rul. 95-58 safe harbor, it may not protect assets from claims of creditors of the Grantor who holds the power.

Trust Protector Possible Powers

- The power to change the name of the Trust and governing law.
- The power to demand an accounting and the right in the Trust Protector's sole discretion to submit same to a court or not.
- The power to direct the Trustee as to which beneficiaries, fiduciaries or other persons holding powers hereunder (whether in a fiduciary capacity) (individually or collectively "Notice Persons") shall or shall not be entitled to receive information concerning this Trust, including but not limited to periodic investment statements and other notifications, to the extent not inconsistent with applicable state law. While Grantor is alive and not disabled no such notifications shall be given to any Notice Persons hereunder other than the Grantor and the Trust Protector unless the Trust Protector authorizes same, or applicable state law requires otherwise. No trustee shall be liable for notifications following Grantor's disability until such Trustee has actual knowledge, or receives written notice from.
- The power to restrict or eliminate the powers granted to the Designator or the Appointer. These terms are explained and illustrated below.

Permit Adding/Including Charitable Beneficiaries

- The trust might include a right for a person, acting in a non-fiduciary capacity, to add a charitable beneficiary. This right, during the grantor's lifetime, characterizes the trust as a grantor trust.
- With all the uncertainty over income and estate tax law changes, some have added a broader charitable designator provision. Review what is in the particular trust, and consider whether action should be taken.
  - If the estate tax is repealed, there may be no downside to making charitable gifts of trust assets.
  - If the income tax rules for charitable contribution deductions become more restrictive, perhaps it will be advantageous from an income tax perspective to make the gifts out of a trust instead of by the individual.
- Does the power end on the grantor's death? Some trusts permit it to continue in perpetuity since the purpose is not merely to trigger grantor trust status, but to add flexibility to planning. If the estate plan is successful, significant wealth will be shifted out of your client's estate to long term irrevocable trusts. What resources will future generations direct to charity if their inherited wealth is in trust with no charitable beneficiaries?
- Consider IRC Sec. 642(c) – can a trust get a FMV deduction for gifts in kind? IRC Sec. 642(c) is more limited then IRC Sec. 170.

Provision to Make Loans

- First determine whether the trust is intended to be a grantor or non-grantor trust. A loan for less than adequate security to the settlor will characterize the trust as grantor.
- It had been common to include a power to a person acting in a non-fiduciary capacity to make loans to the settlor of the trust. Adequate interest should be charged but adequate security is not necessary according to some provisions. What does the trust permit? This too should have characterized the trust as a grantor trust.
- While grantor trust status might be achieved with a swap power, perhaps a loan provision should still be included, but now more for providing a means for the settlor to access trust principal than for grantor trust characterization. If the estate tax is repealed your client might be happier with the planning knowing that there is a means to provide the client access to trust funds, even if that is as a loan.
- Should you always use a loan provision to back stop issues some commentators perceive with swap powers not assuredly granting/creating grantor trust status?
- Should a loan be made? If the trust is intended to be non-grantor that could taint the trust as grantor.

Sample Loan Provision

I appoint Mary Simpson as the Loan Director. During my lifetime, the Loan Director shall have the power, exercisable at any time and from time to time in a non-fiduciary capacity (within the meaning of Code Sec. 675) without the approval or consent of any person in a fiduciary capacity within the meaning of that section, to compel the Trustee to loan some or all of the trust property to me without adequate security within the meaning of Code Sec. 675(2) although with adequate interest within the meaning of that section. I direct that this power is not assignable. In the event that Mary Simpson dies before I die, the successor Loan Director shall be such individual (other than me, any person acting as a Trustee under this instrument or anyone who is an adverse party within the meaning of Code Sec. 672) whom Mary Simpson shall have designated by instrument in writing. Any person other than Mary Simpson acting as a Loan Director hereunder shall also have the power to name a successor Loan Director by an instrument in writing. In the event that no one else is acting as a Loan Director hereunder, the oldest individual acting as a Trustee hereunder (or if none, the corporation or other entity acting as Trustee hereunder) shall be the Loan Director but acting only in a non-fiduciary capacity.

Using a Loan Provision

- If the trust is non-grantor, perhaps no loan should ever be made to the settlor. If a loan must be used, consider trying to find an alternative (e.g., get a third-party loan and a trust guarantee).
- If the trust is grantor be certain adequate interest is charged. Document the loan with a written signed loan document.

Express Decanting Power

- Practitioners can no longer assume that an irrevocable trust cannot be changed. If you can decant the trust, you may have the ability to reduce or avoid state income taxation. You might be able to change inefficient or undesirable trust administration provisions. So, periodic reviews of the trust to determine what might be changed should now be considered.
- Many trusts give the trustee an express power to decant. If not, you have no choice but to rely on state law. The power may permit the trustee to merge the trust into a new and improved trust so administrative provisions can be modified to address future circumstances. Decanting can be used to add or remove a swap power, add an insurance trustee provision so insurance can be added to a trust that did not provide for it, and so much more. Even if the desired modifications can be accomplished with a trust protector action, or non-judicial modification by beneficiaries, including broad decanting powers is like chicken soup – it can't hurt.

Swap/Substitution Powers

- In a grantor trust periodically review the swap power and evaluate options to using it.
- This power can be used to create grantor trust status (income of the trust is taxed to the settlor). Section 675(4)(C).
- But it also is an incredible tool to build in flexibility. Your client can transfer family business interests to an irrevocable trust, locking in valuation discounts available under current law. But, if your client later wants to return those assets to their name, the settlor can swap in an equivalent amount of cash and get the business back.
- This could be useful to obtain a basis step up on death. It could enable the client to change his or her dispositive scheme and transfer the business to another heir. See above.
- If a capital gains tax on death is enacted, a reverse swap might prove beneficial. Shift appreciated assets into the trust (the opposite of what most clients try to do under current law) to avoid a capital gains on death.

Make Swap Powers Practical

- The client/settlor must have property available to effectuate a swap. In many cases cash might be the easiest or preferable asset, but few settlors have addressed this. Practitioners can assist these clients in creating lines of credit to be “at the ready.”
- Analyze trusts for highly appreciated assets as part of the annual review process.
- Assure that if a swap is done that the terms of the trust are followed so that the transaction is in compliance with its requirements.

Broader use of Swap Powers

- Some only consider swap powers in the context of swapping into an elderly grantor's estate to obtain a basis step up for low basis trust assets on grantor's death, but there are more planning options.
- Consider an irrevocable trust holding stock in a family business. Grantor/donor/parent wants to change the dispositive scheme. Can that stock be swapped out back into grantor's name for assets of equivalent value and then given or bequeathed to a different family member?
- What about using a swap power to pull out highly appreciated assets from the trust and then donating them to a donor advised fund (DAF)? That would leave the value of the assets in a GST asset protected trust intact (i.e., in contrast to the trust making the donation directly if it were permitted to do so).

Swap Powers and Divorce

- **Example**: Wife started a widget manufacturing company and gifted 20% of the stock to an irrevocable trust for the children. Husband was named trustee. The business grew substantially. In the maelstrom of the divorce the status of the trust was overlooked. Post-divorce, wife wanted to reclaim her stock, since a 20% minority interest in the business out of her control would be an impediment to her selling the company. So, she attempted to swap a personal note to the trust in exchange for the stock. The now ex-husband, who remained the trustee, refused to honor the transaction. So, while a swap power could have been an important tool for flexibility had the issues been addressed during the pendency of the divorce, it may prove elusive.

Swap Powers and Divorce

- A similar fact pattern arose in a recent case. The trustee was the wife and mother of the daughter of the marriage who was the beneficiary of the trust. The couple divorced. The ex-husband tried to exercise swap power and now ex-wife trustee refused. He tried to swap in a note and the ex-wife/trustee objected saying it was not of equivalent value as required by the trust instrument. Schinazi v. Eden, 2016 WL 5867215. In the divorce the issue of trustee and trust actions should have been addressed. It may have been preferable for all involved to have had the wife/ex-wife resign as trustee in favor of an independent, and ideally an institutional, trustee.
- If a swap power is included in a trust, consider naming an independent trustee. The trustee may have to confirm that the value of the property being swapped into the trust is of equivalent value to the property being swapped out of the trust to the settlor. If a spouse is trustee for a trust with a swap power, as part of the divorce negotiations, consider naming an independent trustee to prevent the ex-spouse/trustee from unreasonably inhibiting the exercise of a swap or other powers.
- Even better, provide that upon a divorce any interest a spouse has should be terminated (i.e. Spouse deemed to be predeceased). Consider the impact on grantor trust status for income tax purposes.

Powers of Appointment

- Many trusts include powers of appointment (someone can designate how trust property will be distributed and to whom). This can provide flexibility. As part of the administration of the trust review the powers to determine if any should be exercised.
- Granting someone the power to transmute limited powers of appointment ("LPOA") into general powers of appointment ("GPOA") that can be used to cause some or all the trust assets to be included in the client's estate to qualify for a basis step up on death should that prove advantageous under a future tax system.
- Caution: A GPOA also means a step down in basis for depreciated assets which is not desirable.
- If the power holder dies without exercising a GPOA the property subject to the power is include in the power holder's estate and will be subject to a step-up in basis. Treas. Reg. Sec. 1.1014-2(b)(2).

Powers of Appointment

- Review and understand the details of the POA in the particular trust and any possible implications of its application. Note that this may change significantly from when the trust was created.
- How far can this go? Can the general power of appointment be granted only over appreciated assets?
- Might it be feasible to structure a tiered formula of sequential contingent general powers of appointment to secure a basis step up on assets exposed to the highest tax brackets first?
- For those living in a decoupled state, the cost of a state death tax must be factored into the analysis. Some practitioners might prefer not having the spouse serve as the trustee if these powers are granted.
- If the client is uncomfortable giving this person a general power of appointment over the trust assets, there are options to make this approach safer.
- Will an institutional trustee ever convert a LPOA to a GPOA? Perhaps never.
- Include in a trust that may grant an LPOA a named trust protector who can grant or modify the terms of a limited power of appointment “LPOA” and convert it to a general power of appointment.

Sample Optional General Power

Option to confer a general power on spouse:

Disinterested Trustee May Confer Power. The Trustee (excluding, however, any Interested Trustee) may at any time, prior to the death of my Wife, by an instrument in writing (1) confer upon my Wife a power exercisable by my Wife's Will or other signed writing that is acknowledged before a notary public, specifically referring to this power of appointment, to appoint all or part of the Family Trust to the creditors of my Wife's estate (other than any taxing authority), and the instrument conferring such power upon my Wife may require the consent of the Trustee (other than any Interested Trustee) to exercise the power, (2) revoke any such instrument previously executed, with or without executing a replacement instrument and/or (3) irrevocably relinquish the powers conferred under (1) and/or (2). Without limiting the Trustee's discretion, the Trustee may use the authority conferred by this paragraph to subject the trust property subject to the power of appointment to estate tax in my Wife's estate to obtain a basis adjustment under Section 1014 of the Code when it appears that it may reduce overall taxes to do so.

Powers of Appointment to Poor Elderly Family Member

- Include additional beneficiaries, e.g., an elderly family member, who have modest estates.
- “My clients would never do that.” Think again.
- 32% of those who have a parent aged 65 and older have provided financial support to that parent.
- This data suggests many clients have an elderly relative (the statistic is only for parents) who they may support and thus who likely has a modest estate (or why else would they need support).
- If the client provides financial assistance to this elderly family member there is likely some level of trust.
- What is the size of the exemption and the value of the elderly family members GPOA? Have family dynamics changed?

LPOA Converted to GPOA

- Grant the beneficiary a limited testamentary power of appointment over the trust assets (e.g., to the client's children or only to the person's creditors).
- Give the trustee (or another specified person) the authority to divide the trust into separate trusts and to use the power to create a sub-trust to which all highly appreciated assets can be transferred.
- Give the trustee the right to convert the beneficiary's limited power of appointment into a general power of appointment over the appreciated asset sub-trust.
- This will cause inclusion in the beneficiary's estate of those appreciated assets, and obtain the desired basis step up without the need to actually distribute those assets to the beneficiary and potentially years or decades before the surviving spouse dies.
  - Caution – confirm that state law that governs the power will not expose the mere existence of an unexercised GPOA to the power holder's creditors. Consider whether that would be the law of the state governing the trust creating the power or the law of the state where the power holder resides?

Consent Requirement on GPOA

- If the GPOA includes a consent requirement be certain it is addressed.
- **Example**: Aunt Nellie is named as an additional beneficiary of an inter-vivos SLAT. She is given a GPOA to appoint trust assets. The client is a bit worried that she might add in other nieces and nephews.
- A possible solution to provide the client comfort is to make Aunt Nellie's exercise of the power subject to the consent of a non-adverse person.
- The person holding the consent power cannot have a substantial interest adverse to the exercise of the power in favor of the decedent, his or her estate, his or her creditors or the creditors of his or her estate. Treas. Reg. Sec. 20.2041-3(c)(2).
- The client's brother who is not a beneficiary of the trust is given the power to consent to Aunt Nellie's exercise of the GPOA before it can be effective.
- A trust with GPOA in state where disclosure is not required (Delaware, Nevada or South Dakota), i.e. where a quiet trust is permitted, may achieve this goal. There is no law confirming that a general power of appointment the holder is not informed of is valid for basis step up purposes.

Grantor SLATs

What Happens When One Spouse Dies?

Death of First Spouse

- Even if a spousal lifetime access non-grantor trust ("SLANT") permits distributions to a spouse with consent of an adverse party, it cannot include the powers to benefit the donor spouse after the death of the beneficiary spouse as those powers would taint the trust as grantor.
- Must consider risks of death of first spouse in a SLAT or SLANT. The economics of all of this may have changed from when the trust was funded. Has this been reviewed?
- Financial modeling.
- Life insurance.
- In a Grantor SLAT consider whether the following have been provided:
  - Loan provisions.
  - Hybrid DAPT.
  - SPAT – special power of appointment trust.

Hybrid DAPT

- Is such a provision included? Is the trust in a DAPT jurisdiction? If not, should it be moved?
- If the trust is formed and administered in one of the 18 states that permit self-settled domestic asset protection trusts (DAPTs), the settlor can be a beneficiary of his or her own trust.
- However, if the settlor resides in a state that does not permit these trusts, some advisers view it as risky, or even not viable, to create a DAPT in a state that does.
- There is a hybrid solution that might reduce the risk some experts perceive yet leave open the possibility of the settlor benefiting from the trust. Don't name the settlor initially as a beneficiary. Instead give someone the right to add as beneficiaries of the trust the descendants of settlor's grandparents. So, if your client/the settlor is not a beneficiary now, the trust should not face that risk. But the client has the possibility of being a beneficiary if your client needs access in the future.

Hybrid DAPT Provision - 1

- Did the trust grant the person who might be called the "Designator" the right/power to add descendants of Grantor's grandparents, including grantor, as a beneficiary of the trust?
- Sample Provision:

Power to Designate Additional Beneficiaries

- The Grantor appoints NAME as the Designator. During the Grantor's lifetime, the Designator shall have the power, exercisable at any time and from time to time in a non-fiduciary capacity, and without the approval or consent of any person in a fiduciary capacity, to add as additional beneficiaries hereunder any person who is a descendant of Grantor's grandparents who is not already designated herein as a…

Hybrid DAPT Provision - 2

Power to Designate Additional Beneficiaries

- …Beneficiary. Further, the Designator may at any time remove any person so added by written notice to the General Trustee, so that from the date of such written notification that added descendant of Grantor's grandparents shall cease being a beneficiary hereunder. The Grantor directs that this power is not assignable. In the event that NAME dies before the Grantor dies, the successor Designator shall be such individual (other than the Grantor, any person acting as a Trustee under this instrument) whom NAME shall have designated by an instrument in writing. Any person other than NAME acting as a Designator hereunder shall also have the power to name such additional beneficiaries as hereinabove provided.

Hybrid DAPT issues

- What if the person holding the power, the Designator, dies or becomes incapacitated, before exercising the power? Is a successor named?
- Might a court infer an implied agreement between the Designator and the settlor?
- Will a client have a person or persons they are comfortable to name?
- Consider the Ionatti case.

SPATs

- Special power of appointment trust (“SPAT”) provisions can be integrated into the SLAT format to address risk of spouse’s premature death.
- Give someone a collateral power of appointment, allowing distribution of trust property to anyone in a class that includes the grantor (such as descendants of the grantor’s grandparents).

Grantor Irrev Trust: Additional Ways to Provide Grantor Access - 1

- **Loans**: Consider granting to someone the power, in a non-fiduciary capacity, to loan the grantor trust assets. Some might refer to this as a "loan director," but other titles might be used as well. A loan director can determine to loan funds to grantor of the SLAT without adequate security for the loan (but the loan director could be required to charge adequate interest to avoid tax issues). This mechanism provides the grantor another means to access trust assets should the grantor require them.
- **Charity**: You might also infuse another means of the grantor indirectly "accessing" funds in a SLAT. Give someone, in a non-fiduciary capacity, the power to add charitable beneficiaries. This person might be called a "charitable director," but other titles might be used as well. A charitable director can determine to add charitable beneficiaries to a SLAT. This provides the grantor an indirect means of "access" to the SLAT by making a charitable donation the charitable director can add the charity to the SLAT and the donation can be made out of SLAT funds not the grantor's funds. However, the SLAT cannot pay a charitable pledge of the grantor.

Additional Ways to Provide Grantor Access - 2

- **Vacation Home**: A SLAT could own an interest in a vacation home. And if the grantor's spouse/beneficiary uses the vacation home, the grantor presumably can as part of the spouse's family. Bear in mind if that is to be done a limited liability company ("LLC") should be formed in the state where the SLAT is governed and administered. That LLC should be authorized to do business in the state where the vacation home is located. That LLC would own the vacation home property and in turn the trust could own some or all of the interests in the LLC.
- **Income Tax Reimbursement**: If the SLAT is structured to be a grantor trust (i.e., the grantor pays the income tax on trust income) consider including a discretionary income tax reimbursement clause. This permits the trustee of your SLAT, in the trustee's discretion (it cannot be mandatory) to reimburse the grantor for income tax paid on trust income. A tax reimbursement provision can add valuable flexibility and access to the grantor.

Non-Reciprocal SLATs

Be Alert to Differences Between Trusts During Operations

Checklist of Differences to Integrate into SLATs - 1

- The following checklist is from Steiner and Shenkman, “Beware of the Reciprocal Trust Doctrine,” Trusts & Estates magazine pages 14-18, April 2012.
- Draft the trusts pursuant to different plans. A separate memorandum or portions of a memorandum dealing with each trust separately may support this. Have the different plans been followed?
- Don’t put a husband and wife in the same economic position following the establishment of the two trusts. Have the trusts been operated in this manner?
- Use different distribution standards in each trust. For example, one trust could limit distributions to an ascertainable standard, while the other trust could be fully discretionary. However, limiting distributions to an ascertainable standard reduces flexibility, may prevent decanting and may expose the trust assets to a beneficiary’s creditors. Are the trustees respecting the different distribution standards?

Checklist of Differences to Integrate into SLATs - 2

- Use different trustees or co-trustees. Has this been respected, or have they changed the trustees to now be identical?
- Give one spouse a noncumulative “5 and 5” power, but not the other. If done has this been respected in trust operations? Should a spouse holding a power partially exercise it to demonstrate its reality?
- As in *Levy* and PLR 9643013 (note that a PLR is not considered precedent), give one spouse a special power of appointment, but not the other. However, the absence of a power of appointment reduces the flexibility of the trust. This might be viewed as particularly significant in light of the continued estate tax uncertainty. Do the client’s wills, for example, reflect the appropriate exercise of powers only where they exist?

Checklist of Differences to Integrate into SLATs - 3

- Give one spouse the broadest possible special power of appointment and the other spouse a special power of appointment exercisable only in favor of a narrower class of permissible appointees, such as issue, or issue and their spouses. Do the client's wills, for example, reflect the appropriate exercise of powers only where they exist?
- Give one spouse a power of appointment exercisable both during lifetime and by will and the other spouse a power of appointment exercisable only by will.
- In the case of insurance trusts, include a marital deduction savings clause in one trust, but not the other.

Checklist of Differences to Integrate into SLATs - 4

- Create different vesting provisions for each trust. For example, the two trusts could mandate distributions at different ages, or in a state that has repealed or allows a transferor to elect out of the rule against perpetuities, one trust could be a perpetual dynasty trust. However, mandating distributions severely reduces the flexibility of the trust, throws the trust assets into the beneficiary's estate for estate tax purposes and exposes the assets to the beneficiary's creditors and spouses. Whatever terms are in the trust confirm that they are being respected when distributions are made.
- Instead of mandating distributions, give the beneficiaries control or a different degree of control, at different ages. For example, the ages at which each child can become a trustee, have the right to remove and replace his co-trustee, and have a special power of appointment could be different in each trust.
- Vary the beneficiaries. For example, one spouse could create a trust for the spouse and issue, and the other spouse could create a trust just for the issue. Note that if, for example, the husband creates a trust for his wife and their first child, and the wife creates a trust for her husband and their second child, the gifts could still be viewed as reciprocal. Is this being respected?

Checklist of Differences to Integrate into SLATs - 5

- Contribute different assets to each trust, either as to the nature or the value of the assets. Contributing different assets may not negate the application of the reciprocal trust doctrine, since the assets in a trust may be susceptible to change over time. However, if one trust is funded with non-liquid assets, or assets subject to contractual restrictions on sale (e.g., operating agreement restrictions on transfer of interests in an LLC) that may be viewed as a more meaningful difference in assets that may not be susceptible to ready modification. Have assets changed? Has this been monitored to maintain different plans?

What to do About Old ILITs, QPRTs, etc.

- Many practitioners drafted QPRTs (when interest rates were higher), typical or traditional ILITs for spouses, etc. Years ago, there was much less attention given to those trusts from a reciprocal trust doctrine perspective.
- Should anything be done now?
- Should one ILIT/QRPT or other trust be decanted to change its terms?

Irrevocable Trusts and Forms 709s

Discounts, Adequate Disclosure Complex/Unique Planning and More

Be Sure to Meet Adequate Disclosure Requirements

- IRC Sect. 6501(c)(9): If a gift is “adequately disclosed” after 3 years, the IRS cannot re-evaluate the transfer for gift or estate tax purposes.
- Gifts not adequately disclosed may be subject to challenge indefinitely.
- Be certain the client’s attorney gets the CPA, if the CPA is preparing the return a closing pack on the plan with all documents.

Adequate Disclosure in Brief

- Description of transferred property.
- Consideration received by transferor.
- Identity & relationship between transferor and transferee(s).
- Valuation of transferred property.
- Copy of trust instrument.
- Statement describing any position contrary to proposed, temporary or final Treasury Regs or revenue rulings.

Treas. Reg. Sec. 301-6501(c)-1(f)(3): Elements of a Qualified Appraisal

- Date of transfer, date of appraisal and purpose of appraisal.
- Description of transferred property.
- Description of assumptions, conditions and restrictions affecting appraisal.
- All information considered in determining value.
- Procedures followed & underlying reasoning.
- Valuation method used, rationale for method.
- Specific basis for valuation.

Treas. Reg. Sec. 301-6501(c)-1(f)(2)(iv): Detailed Description in Lieu of Qualified Appraisal

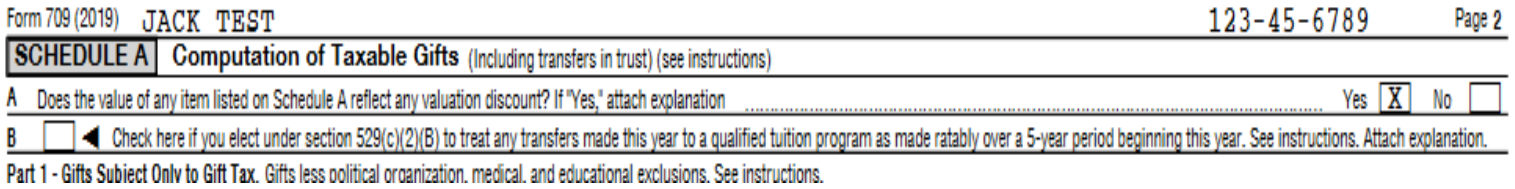
- If a client wants to save money by avoiding a qualified appraisal, make sure the client understands the substantial additional compliance measures required.
- Financial data (e.g., balance sheets, with explanations of adjustments.)
- Restrictions on transferred property considered.
- Description of any discount claimed in valuing the interests
- If actively traded stocks: identify exchange where interest is listed, CUSIP, value is highest/lowest quoted selling price on valuation date.
- If not traded: identify net asset value, discounts, pro rata value of entity transferred, FMV of interest and to whom it was transferred and their relationship to the transferor.

Appraisal Should Set Forth Revenue Ruling 59-60 Factors

- Nature of company, capital structure.
- Operating and investment assets & management.
- Current and prospective economic conditions.
- Book value and financial condition of business.
- Earning capacity of the company.
- Balance sheets, detailed profit & loss statements.
- Dividend paying capacity.
- Goodwill or other intangible value.
- Arms-length sales of the same stock.

Disclosures of Valuation of Transferred Property

- IF DISCOUNTS - Check the box at the top of page 2 of Form 709:



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SCHEDULE A **Computation of Taxable Gifts** (Including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If "Yes," attach explanation ..... Yes [X] No [ ]

B [ ] ◀ Check here if you elect under section 529(c)(2)(B) to treat any transfers made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

Part 1 - Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusions. See instructions.

Valuation Discounts – Another Word about "the Box"

- The box for discounts has always been a dicey topic for operating businesses, the value of which tends to be based on a multiple of earnings before interest, taxes, depreciation, and amortization (EBITDA).
- The EBITDA multiplier (a form of a price-to-earnings ratio) tends to be derived from results of publicly-traded companies, which have discounts for lack of control baked into them instead of being separately stated. Does that mean the box should be checked?

Be Alert to Variations on *Wandry* & the Impact on 709 preparation

- Review valuation adjustment clauses carefully to understand whether there are any mechanisms which would pour excess value into a non-taxable receptacle. Be sure you understand each component to the transaction.
- Exercise additional caution in disclosing the contours of the transaction & do not say anything inconsistent with the transaction documents.
- Attach instruments incorporating the defined value mechanism.

Additional comments on disclosing *Wandry*-type transfers

- Strongly recommended for preparers to attach a complete copy of the trust instrument – even if trust previously provided on prior gift tax return.
- Include all attendant documents related to the operation of the defined value mechanism: e.g., GRAT instrument, sales agreements, etc.
- When a Wandry formula is used, include statement that the assets are **estimated** to be X units, but the purchase price is **fixed** at $Y.

Defined Value Mechanisms: Important Considerations

- Pouring Excess to GRATs.
  - Disclose funding of the GRAT with any other assets.
  - Calendar dates for annuity payments.
  - Does this work after CCA 202152018?
  - Make sure there is some excess so the regulatory exception can apply.
- Spillover to Charities.
  - Consider reporting potential charitable contribution on donor's Form 1040.
  - Will potential refund claim need to be filed.
  - UBIT issues?
  - Note that basis must be reported or no deduction at all.

Must SALES be Disclosed? Consult Treas. Reg. Sec. 25-2512-8

- For those wondering if SALES must be disclosed, consider this language from the regulation:
  - Transfers reached by the gift tax are not confined to those only which, being without a valuable consideration, accord with the common law concept of gifts, but embrace as well sales, exchanges, and other dispositions of property for a consideration to the extent that the value of the property transferred by the donor exceeds the value in money or money's worth of the consideration given therefore.

Potential Sale on Redetermination of Value for Gift Tax purposes

Use CAREFUL language to describe what was sold, possibly as follows:

Part 1 - Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusion

A Item number	B ● Donee's name and address ● Relationship to donor (if any) ● Description of gift ● If the gift was of securities, give CUSIP no. ● If closely held entity, give EIN
1	JACK FAMILY TRUST C/O TRUSTEE 12-7202100 THAT PERCENTAGE OF INTERESTS IN THE ENTITY DEEMED TO HAVE BEEN SOLD BY OPERATION OF THAT CERTAIN [ASSIGNMENT INSTRUMENT] EXECUTED ON [ORIGINAL DATE OF THE TRANSACTION], BETWEEN, AND AMONG JACK AND THE TRUSTEES OF THE JACK TRUST AND THE JILL TRUST, AS MAY BE ADJUSTED UPON A FINAL DETERMINATION FOR FEDERAL GIFT TAX PURPOSES OF THE FAIR MARKET VALUE OF THE INTERESTS IN THE ENTITY AS OF [ORIGINAL DATE OF THE TRANSACTION].

Potential Sale of Undetermined Value of Shares in Business e.g., Double Wandry (continued…)

- Reference the Assignment Document and qualified valuation report.
- Include a copy of trust agreement, promissory note, sales agreement, etc.
- Report the sale on the appropriate section of Schedule A.
- The transferor has estimated in good faith that NO interests are being sold so both the fair market value & the basis is $0.

Other Factors

- The Gift Tax return is not the only tax filing that will include reference to the transactions, and consideration should be given to how the following income tax returns should reference the defined value mechanism:
  - Entity income tax return.
  - Individual income tax return(s).
  - Fiduciary income tax return(s).

Proposed language about preliminary allocation of interests

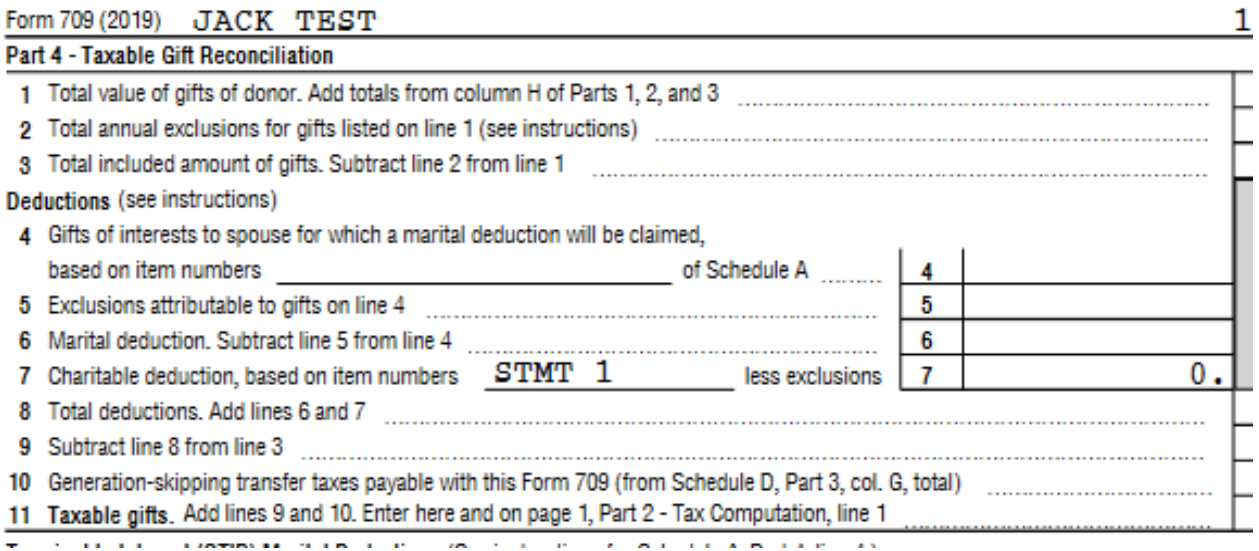
- Too often income tax returns don't reflect the gift tax valuation adjustment mechanism, be sure they do.
- Each income tax return should include language such as the following:
  - The preliminary allocations of interests in the Entity to the Individual(s) and/or the [NAME] Trust(S) based upon the valuation performed by [third party valuation professional], a third party valuation professional, in accordance with Revenue Ruling 59-60 and other regulations and rulings where appropriate, is for administrative convenience only with respect to the value and percentage of the Entity interests until the fair market value of the Entity interests is finally determined for federal gift tax purposes.

Charitable Gifts as the Non-Taxable Receptacle

- A common gift tax return oversight is the failure to report charitable gifts.
- If any omitted charitable gifts constitute a substantial understatement of gifts, the statute of limitations may be extended from a three-year period to a six-year period IRC 6501(e)(2).
- Especially problematic if charity is used in valuation adjustment clauses (e.g., as part of the waterfall on a note sale transaction).

Defined Valuation Mechanism with Charitable Spillover

- Report the potential charitable gift on Schedule A Part 1, showing $0 gift tax value and $0 basis.
- Complete Schedule A Part 4, line 7:



Form 709 (2019) JACK TEST 1

Part 4 - Taxable Gift Reconciliation

1	Total value of gifts of donor. Add totals from column H of Parts 1, 2, and 3		
2	Total annual exclusions for gifts listed on line 1 (see instructions)		
3	Total included amount of gifts. Subtract line 2 from line 1		
Deductions (see instructions)			
4	Gifts of interests to spouse for which a marital deduction will be claimed, based on item numbers _____ of Schedule A	4	
5	Exclusions attributable to gifts on line 4	5	
6	Marital deduction. Subtract line 5 from line 4	6	
7	Charitable deduction, based on item numbers STMT 1 less exclusions	7	0.
8	Total deductions. Add lines 6 and 7		
9	Subtract line 8 from line 3		
10	Generation-skipping transfer taxes payable with this Form 709 (from Schedule D, Part 3, col. G, total)		
11	**Taxable gifts.** Add lines 9 and 10. Enter here and on page 1, Part 2 - Tax Computation, line 1		

Defined Valuation Mechanism with Charitable Spillover

- Report the potential charitable gift on Schedule A Part 1, showing $0 gift tax value and $0 basis:

SCHEDULE A, PART I CONTINUATION SHEET

Part 1 - Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusi

A Item number	B ● Donee's name and address ● Relationship to donor (if any) ● Description of gift ● If the gift was of securities, give CUSIP no. ● If closely held entity, give EIN
1	CHARITY THAT PERCENTAGE OF INTERESTS IN THE ENTITY DEEMED TO HAVE BEEN DONATED TO [CHARITABLE ENTITY] BY OPERATION OF THAT CERTAIN [ASSIGNMENT INSTRUMENT] EXECUTED ON [ORIGINAL DATE OF THE TRANSACTION], BETWEEN, AND AMONG TAXPAYER AND THE TRUSTEES OF THE [ ] TRUST, AS MAY BE ADJUSTED UPON A FINAL DETERMINATION FOR FEDERAL GIFT TAX PURPOSES OF THE FAIR MARKET VALUE OF THE INTERESTS IN THE ENTITY AS OF [ORIGINAL DATE OF THE TRANSACTION].

Defined Valuation Mechanism – Excess to Spouse or Marital Trust

- The gift tax return preparer should report the potential marital gift on Schedule A Part 1, showing $0 gift tax value and $0 basis.
- Further, the gift tax preparer should reference the specific item number of the potential marital gift on Schedule A Part 4, line 6.

GST Exemption and Valuation Adjustment Clauses

Thoughtful Allocation of GST Exemption

Consider How GST Exemption Might be Allocated to Various Transfers

- It may be important to provide a prioritization of which trusts get GST allocation and in what order, especially in case there is a valuation adjustment that affects the allocation anticipated on the return. Too often this is ignored.
- The first trust that you certainly want to treat as a GST trust, to which you want to allocate GST exemption, should be elected to be treated as a GST trust.
- The remaining trusts should have an election not to be treated as GST trusts so that a Notice of Allocation can better control the manner in which GST exemption is allocated.
- Include a Notice of Allocation stating the donor's intention that GST exemption allocations should be done by formula which will change if values are modified on audit.

EXAMPLE: Allocating GST Exemption Among Multiple Trusts

- Suppose the client made transfers to a grantor trust to which a family business interest was transferred, and separately to a simple life insurance trust owning term life insurance. This might be the reporting approach you want to take if GST exemption is limited to assure that if there is a revaluation of the business that trust is protected by an allocation of GST exemption over the ILIT:
  - FIRST: protect the trust holding the family business by reporting it as a GST Trust to which exemption is automatically allocated.
  - SECOND: opt out of automatic allocation for the ILIT and allocate GST exemption up to the donor's remaining GST exemption, using a formula allocation.

Grantor Retained Interest Trusts

- For trusts that are includable in the Grantor's estate (e.g., GRITs, GRATs) - the inclusion ratio is not calculated until the estate tax inclusion period (ETIP) closes.
- When ETIP closes - taxpayer may allocate GST exemption to the value of the remainder interest as if the gift had been made on the day the ETIP closes (taking into account any prior allocations).
- This is rarely done as it is inefficient as by then property hopefully will have appreciated (and if it has declined, has too much exemption been allocated?) However, if it is anticipated that GST exemption may be reduced, perhaps then allocation should be considered.

Reporting 2020-2021 Transfers for Married Taxpayers

Many Complications

Relinquishment of Interests in Joint Property

- Consider intra-spousal gifts in light of the Smaldino case.
- Too often clients and even counsel give little or no attention to who owned which assets before the plan. That can be problematic.
- Say all assets were in wife's name and those assets are divided so each spouse can fund a SLAT. But because of worries about the effective date of law changes the couple only waits a week after division to make their gifts.
- There are pros/cons of disclosing intra-spousal transfers.
- Be wary of the step transaction doctrine.
- Since not required – unclear if disclosure will toll statute of limitations as to whether ownership was relinquished.
- Failure to relinquish asset could disrupt planning.

Spousal Lifetime Access Trusts (SLATs) – Reciprocal Trust Doctrine

- SLATs have become perhaps the default plan in the current environment. But they are not without risk.
- SLATs should be sufficiently different to reduce the risk of a reciprocal trust challenge. In fact, consider one SLAT and one SPAT as one differentiation between the trusts.
- Created at different times, with different assets and trustees & different terms (e.g., powers of appointment, distribution standards, etc.)
- Practitioners preparing gift tax returns might consider whether to obtain corroboration for their gift tax file as to the differentiation of each SLAT and the respective planning.

Gift Tax Return Reporting Should Dovetail the SLAT Strategy

- Most gifts to SLATs may not be split – maybe the spouses should not elect to split at all (may be possible if HEMS standard, etc., but should you?)
- Assets conveyed should be identified as those owned by the donor spouse individually (i.e., not joint assets.)
- Consider making overt disclosure on a gift tax return to marital deduction savings clause embedded in the terms of an insurance trust.

2020-1 Inter Vivos QTIP Trusts for the Reluctant Client

- Reluctant clients may have needed a safety valve.
- Some attorneys drafted trusts with specific language allowing the trust to qualify for an inter vivos QTIP election, as described in Code Sec. 2523(f):
  - The trust must grant to the donee spouse a qualifying income interest for life; and
  - The donor must make a QTIP election on a timely filed gift tax return.
- Preparer and planner should be coordinated to ensure timely elections if desired.

Reporting Note Transactions

- Low Interest Rates May Have Meant More Notes and Note Sales

Substituting Higher-Interest for Lower-Interest Notes

- If possible, get involved in the structure and planning of the note refinance. Many commentators believe that no "consideration" is necessary. Other suggest that whether or not required a principal payment should be made, the term shortened, or perhaps additional collateral given.
- Consider disclosing as non-gift transaction.
- Failure to disclose could result in the statute of limitations not tolling.
- Consider income tax issues if borrower was an individual or non-grantor trust.

Documentation to Include in Disclosing Note Refinance

- Original Note – should include no prepayment penalty provision or documentation resolving such provision. Be sure the client's attorney has reviewed the note and confirmed this.
- New Note – fully executed.
- Modification of Pledge and Escrow Agreement (if original Note was part of sale). This is often overlooked. It is not merely about creating a new note but also must include addressing all ancillary documentation relating to that note.
- Novation Agreement – confirms the original agreement notwithstanding cancellation of the original Note

Trust Administration

Conclusion and Additional Information

Conclusion

- The tax law and planning environment are and likely always will be in a state of flux.
- SLATs provide a useful planning tool for many married couples to achieve a wide range of both tax and non-tax goals.
- Plan SLATs with flexibility.

Additional information

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