MARTY'S BEST ESTATE, BUSINESS & TAX PLANNING IDEAS

CURRENT ACTIONABLE ESTATE PLANNING IDEAS

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Current Planning Environment

OBSERVATIONS ON TRENDS AFFECTING ESTATE PLANNING

Proposal to Shut Down Private Placement Life Insurance

- New Wyden Bill Would Close Private Placement Life Insurance Tax Shelter Abused by the Ultra-Rich. . APRIL 13,2026
- Senate Finance Committee Ranking Member Ron Wyden, D-Ore., will introduce legislation today to close a tax loophole abused by the ultra-rich to shelter tens of billions of dollars in income from taxes with private placement life insurance (PPLI) contracts. PPLI policies are designed to mimic hedge funds and other vehicles for the benefit of highly sophisticated investors, and they are exclusively available to the ultra-wealthy. At the moment, there is no requirement to report PPLI contracts to the IRS, allowing wealthy investors to use them to shelter profits from lucrative investments.
- PPLI contracts, which are related in name only to typical life insurance commonly held by middle class families, make up just 0.003 percent of all outstanding life insurance policies. Senator Wyden's new bill, *the Protecting Proper Life Insurance from Abuse Act,* would protect the longstanding, preferential tax treatment of traditional life insurance and make no changes to the plans that middle class families count on for financial security.
- "Life insurance is an essential source of financial security for tens of millions of middle class American families, so we cannot have a bunch of ultra-rich tax dodgers abusing its special tax treatment to set up tax-free hedge funds and shelter mountains of cash," Wyden said. "Congress has a long tradition of stepping in to prevent the abuse of the important, preferential tax rules for life insurance, and this bill is the next step in that process. Life insurance is too important to allow it to be twisted into another garden variety tax ripoff for the super-rich."

Strengthen Social Security By Taxing Dynastic Wealth Act

- The Strengthen Social Security by Taxing Dynastic Wealth Act, introduced by Senator Van Hollen, proposes to fundamentally restore the federal estate, gift, and generation-skipping transfer tax regime to levels and structural components that largely resemble those in effect in 2009. The proposal would reduce the basic exclusion amount, increase marginal estate tax rates, impose a separate limitation on the gift tax applicable credit, and modify the mechanics and utility of portability between spouses.

- A central feature of the proposal is its linkage of transfer tax revenues to Social Security financing through consolidation of the OASI and DI trust funds and the appropriation of amounts equivalent to subtitle B taxes to a single Social Security Trust Fund. Although enactment during the current administration may be viewed as unlikely, the proposal should be evaluated against broader federal, state, and local tax developments, as well as projected Social Security funding shortfalls, which together suggest a potentially altered long-term planning environment. Social Security cannot be allowed to falter and linking estate tax changes to saving Social Security, if no other financially sound options are proposed, the potential for some variation of this proposal actually being enacted may be increased.

Strengthen Social Security By Taxing Dynastic Wealth Act

- The proposal would reduce the basic exclusion amount to $3.5 million without inflation indexing, significantly lowering the threshold at which estate tax exposure begins and increasing sensitivity to valuation, discounts, and deduction positioning. That is significant and not inflation adjusting the exemption may be subtle enough that it may be overlooked by some. Assume the current inflation rate is 3.3% and that rate continues for 10 years. The $3.5 million exemption would have the purchasing power of approximately $2.53 million in today's dollars after 10 years,. That's a real reduction of about 28% over a decade.

- The estate tax rate schedule would be modified to impose marginal rates rising to 45% at relatively modest taxable estate levels, amplifying the cost of excess value above the exemption. A major structural change is the reintroduction of asymmetry between estate and gift taxes by limiting the gift tax applicable credit as if the exclusion amount were only $1 million, effectively restoring a pre-unification dynamic under which lifetime transfers consume exemption more quickly than testamentary transfers. Portability would remain available, but the proposal would cap the deceased spousal unused exclusion amount for gift tax purposes, materially reducing the usefulness of DSUE for lifetime planning and altering the calculus surrounding Form 706 filings, marital deduction planning, and reliance on portability alone.

Strengthen Social Security By Taxing Dynastic Wealth Act

- If enacted, the proposal would push estate planning toward a lower-exemption, higher-rate environment in which flexibility, valuation discipline, and basis planning regain central importance.
- Practitioners should provide for Credit shelter trusts, disclaimer planning, and Clayton-style marital deduction mechanisms in new documents even if that is not the current default plan used for clients. These techniques can incorporate flexibility into a plan to facilitate planning if a bill anything like this is eventually enacted. That is important as many clients do not return to update documents, and some may face capacity issues and not be able to modify their documents for new law. With document generation software adding further flexibility is quick and inexpensive.
- The separation of estate and gift tax exclusion mechanics would increase the importance of leveraged transfer techniques that minimize applicable credit usage, including sales to grantor trusts and carefully structured GRATs, while elevating the planning value of annual exclusion gifts (Crummey powers should perhaps be a more common default option for irrevocable trust planning then they may have been in recent years). If a $1 million gift exemption is enacted a much greater portion of wealth transfers will need to be protected with defined value mechanisms (Wandry, Petter, King and other variations).
- The proposal suggests a need to reframe client conversations to incorporate legislative trend risk, update default drafting assumptions created during the high-exemption era, and prepare planning structures in advance so they can be implemented efficiently if legislative windows narrow or exemptions compress.

Other Broader Considerations of the Current Planning Considerations

- **Litigation**. The estate planning malpractice environment is one of the worst and getting risky Practitioners need to be more cautious.
- **Trust modification**. Change by any means may be under attack by the IRS, caution is in order. Is the day of easy decanting ending? Practitioners should caution clients about the changing risk environment before modification.
- **Formalities count**. Many recent major cases include a message how the formalities of a transaction must be respected: CES 2007 Trust (DE DAPT case), Connelly (redemption buyout insurance included in entity value), Sorensen (Firehouse Sub case invalidated valuation adjustment mechanism), Levine(split-dollar insurance), and Smaldino (step-transaction case). Will clients ever learn to focus on proper administration?
- **Complexity**. Complexity continues to spiral out of control: Secure, the Corporate Transparency Act was largely declawed but what a mess and time waste it was, Basis consistency reporting, etc. And its not only tax issues, consider the explosion of IT/cybersecurity complexity, and more.
- **AI**. This is transforming estate planning. Clients will even be more likely to think that they have all the answers before meeting their advisers.
- **Increasing role of financial planners**. Financial advisers, aided by increasingly sophisticated AI tools, are taking over more and more of the estate planning conversation. This will transform estate planning. It will likely result in increased lawsuits against financial advisers getting out over their skis. Naming of accounts is one of many issues to address.

Trust Planning Considerations

ITS MORE THAN JUST SNTS AND BOILERPLATE REVOCABLE TRUSTS

Defending SLATs Uncrossed under the Reciprocal Trust Doctrine – Does DAPT-Like Planning Help?

- Reciprocal SLAT planning sometimes results in two otherwise well-designed trusts being "uncrossed" under the reciprocal trust doctrine, causing each spouse to be treated as the settlor of the trust from which that spouse benefits. Once uncrossed, the trusts are no longer viewed as third-party SLATs but instead function, in substance, as self-settled trusts.
- The reciprocal trust doctrine itself does not invalidate the trusts, does not address creditor rights, and does not prescribe the consequences of self-settlement under state trust law. Its effect is limited to recharacterizing settlor identity based on economic substance. I
- f an uncrossed SLAT is administered in, and otherwise complies with, a domestic asset protection trust (DAPT) jurisdiction, argument exists that the trust should be analyzed under that state's self-settled trust statute. Modern DAPT statutes were specifically enacted to override the traditional common-law rule that a settlor's creditors may always reach assets of a self-settled trust. These statutes generally do not condition asset protection on the trust not being self-settled; rather, they assume self-settlement and provide protection if statutory requirements are met, including trustee independence, limits on retained powers, affidavits of solvency, and compliance with fraudulent transfer statutes.
- There is no case law addressing whether an uncrossed or reciprocal SLAT that qualifies as a properly structured and administered DAPT must fail as an asset protection trust. There is likewise no doctrine holding that federal recharacterization under the reciprocal trust doctrine negates otherwise applicable state-law creditor protection statutes. As a result, a DAPT analysis may be viewed as a possible fallback position rather than an intended primary design feature. Whether the argument succeeds will depend on facts, administration, forum, creditor posture, and the absence of bankruptcy or adverse choice-of-law overrides.
- Practitioners should be cautious in describing this strategy. The DAPT backstop is untested, there is no authority directly on point, and success cannot be assured. However, when a reciprocal SLAT is otherwise well crafted, properly administered, and situated in a jurisdiction that expressly authorizes self-settled trusts, the DAPT argument may provide a meaningful defensive position if reciprocity is asserted. At a minimum, it may be preferable to having no asset protection argument at all once uncrossing occurs.

Purpose Trusts Sound Great But Can be Problematic

- A purpose trust is a trust created to carry out objectives other than benefit identifiable beneficiaries. A purpose trust does not have beneficiaries who can enforce the trustee's obligations. Instead, monitoring may be done by a designated protector. An example may be a purpose trust created to perpetuate a particular business to benefit workers or the community, etc.
- Problems with purpose trusts:
  - Enabling state law is required since a purpose trust does not conform with traditional trust structure (i.e. no beneficiary).
  - The IRS may recharacterize a purpose trust as taxable as a corporation.
  - Since a purpose trust is not a charitable trust a gift tax could be triggered on funding.
  - New concepts, like a protector and other essential management functions have to be created without historical foundation. That could be dangerous, costly and complex.

Purpose Trusts Can be Problematic – Is There A Better Approach?

- Similar goals may be achieved by applying more conventional planning structures in creative ways.
- The structure was based on a broad and flexible non-charitable trust that benefited charities and family.
- The trust was administered by an institutional directed trustee, an LLC that had a group of managers to make investment decisions and a second LLC that a group of managers could make distribution decisions.
- The two LLCs had in their operating agreements mechanisms for succession of managers so that they could function in perpetuity. The trust was formed in South Dakota which permits special purpose entities. There is no risk of recharacterization as a corporation as there were people as beneficiaries. In contrast to purpose trusts that require creating new management, control, monitoring and other mechanisms my approach relied on traditional and proven trust, and LLC law. Special provisions were included in the operating agreements and trust document.
- Both limited liability companies were organized as special purpose entities under South Dakota law. The operating agreements were drafted to address succession in a manner comparable to corporate governance documents rather than traditional individual fiduciary appointments. This approach permitted continuity similar to that often sought in purpose trust structures while relying exclusively on established and familiar business entity law. Because governance was embedded in operating agreements rather than trust documents alone, future amendments, resignations, and transitions could be managed in an orderly and predictable manner without the need to reconstitute trust fiduciaries or court involvement except where otherwise required by law..

Purpose Trusts Can be Problematic – Is There A Better Approach?

- and predictable manner without the need to reconstitute trust fiduciaries or court involvement except where otherwise required by law.
- This structure avoided all of the issues of a Purpose Trust.
- The client sold assets to the trust in a note sale with complex valuation adjustment mechanism. The purchasing trust was a grantor trust so that there were no gift tax issues on funding.
- In the context of this particular plan the goal was to accommodate specific religious beliefs of the client who was a member of the Church of Scientology.
- A central planning objective was to respect and accommodate the client's religious beliefs. Those beliefs influenced charitable beneficiary definitions, distribution standards, dispute resolution mechanisms, and fiduciary selection. The structure permitted religious considerations to be addressed without requiring the trust to exist solely for a non-charitable purpose or to rely on enforcement by an external enforcer. Instead, religious considerations were integrated into discretionary standards and governance processes in a manner consistent with private trust law. This reduced the risk that the trust could be challenged as vague, unenforceable, or contrary to public policy.

Purpose Trusts Can be Problematic – Is There A Better Approach?

- The structure avoided several recurring issues associated with non-charitable purpose trusts. Purpose trusts often require the creation of novel enforcement roles, such as enforcers or protectors who hold atypical powers that are not grounded in longstanding fiduciary doctrine. They may present uncertainty regarding federal income tax classification, potential recharacterization as business entities, or limitations on duration. Purpose trusts also frequently require bespoke monitoring regimes that may increase administrative complexity and cost. By contrast, this structure relied on traditional trust law, established directed trust principles, and well-developed limited liability company governance mechanisms.

- The presence of family and charitable beneficiaries also reduced the risk that the arrangement could be characterized as a business trust or association taxable as a corporation. The trust's purpose was not merely asset holding or business operation for its own sake, but rather the management and distribution of wealth for human beneficiaries and charitable purposes. This distinction is meaningful for both state trust law and federal tax analysis and helped reinforce the characterization of the arrangement as a trust rather than a business entity.

Special Trust Advisor And Powers Of Appointment To Safeguard Plans For LGBTQ Clients

- Issues can arise with LGBTQ beneficiaries such as name change, gender change, determination of whether an expense is permissible to be paid by the trustee as a medical expense, who is an heir, etc. A unique way to address these issues in a flexible manner, to preserve privacy, and potentially to reduce or avoid disputes is to appoint a special position to act on these and other matters.
- The governing instrument can name a special limited trust protector (referred to below as a "Special Trust Advisor") to address the issues described earlier. The idea is to name an individual, or perhaps an organization or entity (for example, the law firm that drafted documents and is intimately familiar with the client's wishes) to act in a non-fiduciary capacity, to the extent permitted under state law. Expressly address those matters specific to the LGBTQ community in the powers granted to this Special Trust Protector , which may be a clear way to provide the appropriate authority to overcome many of the common issues discussed above.
- In many situations, the concerns may not be known at the time the document is drafted, and it will be prudent to add provisions allowing flexibility in managing issues that may arise in the future. To the extent many of these matters can be addressed in a single provision, it may be feasible to more economically (in terms of drafting time) address many of these matters than taking a specific approach of drafting for each of the many different issues that may come up in the appropriate portion of a trust instrument.
- Specifying that the Special Trust Protector will act in a non-fiduciary capacity should eliminate some of the fiduciary duty concerns that a trustee might have when changing a bequest or appointing a new beneficiary of a trust, such as a non-adopted child who's clearly an intended beneficiary. While specific drafting might suffice to permit a fiduciary, such as a trustee, to add a beneficiary, naming someone in a non-fiduciary capacity might avoid concerns associated with fiduciary duties.

Special Trust Advisor And Powers Of Appointment To Safeguard Plans For LGBTQ Clients

- This power would be analogous, in some respects, to the power given to an individual in a hybrid-domestic asset protection trust to appoint additional beneficiaries (although the uncertainties of adding the settlor in a hybrid DAPT are not relevant to this application of the concept). Another power to give the Special Trust Protector is to direct distributions to beneficiaries for medical, adoption, family planning and other costs that a trustee may not believe are covered under the terms of the governing instrument.
- The Special Trust Protector could be given the power to change a name or gender reference in a separate instrument (for example, a signed action by the Special Trust Protector) . That might not suffice if a transgender individual may not wish to have their dead name (that is, the name that the trans individual may have used before transition that they no longer use) continue to be reflected in the instrument. This is far more of a concern then merely semantics in the instrument. The incidence of violence and discrimination that transgender individuals have and continue to experience is real and needs to be addressed.
- This problem might be resolved by the trustee thereafter decanting the trust into a new instrument reflecting solely that individual's current name (so that there's no legacy language remaining in the governing instrument). Perhaps the Special Trust Protector could be given the authority to direct the trustee to decant the trust to accomplish this objective. The Special Trust Protector could, or even should, be given the power to direct specifically how the name of the individual should be reflected in that new trust.

A Successful Wandry May Implicate Estate Inclusion under Powell

- A typical *Wandry* clause suffers from a key structural weakness: a valuation adjustment will necessarily result in business interests that remain in the transferor's estate. Just five years after *Wandry* was decided, the Tax Court in *Powell* required estate tax inclusion under Code Sec. 2036(a)(2) of the date of death value of all of the transferred interests because the decedent, "in conjunction with others," retained the ability to dissolve the entity and thereby affect enjoyment of transferred interests.

- The concern is not hypothetical. If a successful *Wandry* adjustment leaves even a small equity interest in the transferor, the IRS could technically leverage the successful *Powell* holding to cause estate tax inclusion of the value of all of the transferred interests. Practitioners should consider options to avoid application of *Powell* in the event of a *Wandry* adjustment. *Estate of Powell v. Commissioner*, 148 T.C. No. 18 (2017).

- Where ownership interests are adjusted between the transferor and transferee, the attendant economic consequences arising from the transferred interest from the date of the initial transfer until the date of the final determination of gift tax value must also shift . A transferee may need to return some part of distributions received from the entity back to the transferor. The entity, the transferor and the transferee might each need to amend one or more tax returns to report income and expenses shifted between the transferor and the transferee.

- A solution is to use a Secondary Sale Agreement. This is a contemporaneously executed agreement under which the transferor agrees to sell, effective as of the same date, any interests remaining in the transferor's hands after application of the defined value mechanism, at the gift tax value as finally determined.

How Do You Wandry If You Don't have an Appraisal Yet?

- A *Wandry* mechanism may be useful to facilitate a transfer when a final appraisal is not available, allowing for three valuation tiers in the transfer:
- Initial transfer (gift or sale) based on an estimate (if possible from an independent appraiser).
- An interim adjustment (the second tier of the two-tier Wandry) when the final appraisal report is received.
- The final or traditional Wandry adjustment based on the gift tax value as finally determined.

Administer Valuation Adjustment Clauses Properly

- Wandry mechanisms are very common in estate transfer planning but too often they are not administered properly.
- Trustee records, income tax returns, gift tax returns, contract documents and personal financial statements should all clarify that a dollar value of interests is owned, not a percentage or number of units or shares.
- When the gift tax audit period has tolled all the records should be updated to reflect that a specified percentage or number of units/shares is in fact owned.

SLATS and Divorce Risk

IT'S NOT SOME MYTHICAL 45-50% DIVORCE RATE THAT SHOULD MAKE YOU AVOID A PARTICULAR TECHNIQUE

What is the Divorce Rate? What Might That Mean to Joint Representation and SLATs?

- CDC data:
  - ~40–43% of first marriages end in divorce.
  - Second marriages: ~60%.
  - Third marriages: ~73%.
- Can you create SLATs for married couples knowing they face such a risk as divorce?
- Many speakers recommended care and caution, several suggested that SLATs may be inappropriate to use except in limited circumstances. Caution is always advisable.

What is the Divorce Rate Applicable to our Clients?

- CDC data is for the population as a whole, but our clients are anything but the average or mean for the population and average family.
- There is strong correlation with lower divorce rates and several factors that are typical of most estate planning clients:
  - Greater wealth.
  - Higher education.
  - Duration of marriage.
  - (I cannot vouch for the data and conclusions following as I lack the math and actuarial abilities to vet it).

Hypothetical Estate Planning Client (Not Your Average Divorce Rate Statistic)

- Take the following hypothetical couple:
  - College educated married couple.
  - They have already been married 20 years.
  - They have a $5M net worth (which is likely on the low end of net worth that a Heckerling attendee might accept, and for many a tiny percentage of the level of client they serve).
- The actual divorce rate may be 10% or less. Whatever the actual figure is, it is much less than for the average population data that seems to be the foundation of many of the anti-SLAT discussions. Also, these lower rates even if just in the ballpark of the actual figure for an estate planning client have important implications to joint representation generally.

Even Modest Wealth Accumulation Lowers the Divorce Rate

- A major 2023 demographic study demonstrates that **higher household wealth strongly correlates with lower divorce risk**.
- As documented in the peer-reviewed article:
- **Alexandra Killewald, Angela Lee & Paula England, *Wealth and Divorce*, *Demography*, Vol. 60, No. 1, pp. 147–171 (February 1, 2023), Duke University Press. URL: https://read.dukeupress.edu/demography/article/60/1/147/342803/Wealth-and-Divorce**
- The authors find that wealthier couples divorce less often, even after controlling for socioeconomic and demographic variables. The study further concludes:
- Increasing net worth from **$0 to $40,000** generates a reduction in predicted divorce risk comparable to eliminating a nonmarital birth.
- The stabilizing effect of wealth is **steepest at low-positive wealth levels**, meaning modest wealth accumulation significantly reduces divorce risk.
- Even controlling for net worth, **ownership of homes or vehicles** independently reduces divorce risk, indicating both material and symbolic stability effects.
- **Non-reviewed AI research**.

Educational Achievement Correlates with Lower Divorce Rates

- Education is one of the strongest predictors of marital stability in the United States.
- Pew Research Center reports:
- **Wendy Wang, *The link between a college education and a lasting marriage*, Pew Research Center (December 4, 2015). URL: https://www.pewresearch.org/short-reads/2015/12/04/education-and-marriage/**
- Key findings include:
- **78% of college-educated women** who married between 2006 and 2010 could expect their marriages to last **20 years or more**, compared with only **40%** of women with a high-school diploma or less.
- **65% of college-educated men** can expect a first marriage to last at least 20 years, compared with approximately **50%** for men with only high-school education.
- Additional quantitative data confirm the educational gradient:
- **Divorce Rate by Education Level**, The Center for Divorce Education. URL: https://divorce-education.com/divorce-rate-by-education-level/
- Bachelor's degree or higher: **25.9% divorce rate**
- Some college: **36.3%**
- Associate's degree: **30.1%**
- High school diploma: **38.8%**
- Less than high school: **45.3%**
- **Non-reviewed AI research.**

Educational Achievement Correlates with Lower Divorce Rates

- Higher education correlates with:
  - Later age at marriage,
  - Higher income,
  - Greater marital stability.
- **Marriage longevity statistics (Gitnux Report 2026)** show that **78% of women with bachelor's degrees remain married for 20 years**, while only 40% of less-educated women do—demonstrating strong selection effects and the stability of long marriages.
  (This does not directly show divorce *risk but* strongly evidences high survival probability at 20 years.)
- **Non-reviewed AI research.**

The Longer the Marriage the Lower the Risk of Divorce

- **Forbes Advisor** synthesizes federal datasets (U.S. Census, CDC, Pew) and reports that **"the average length of a marriage prior to divorce is eight years"**, demonstrating that divorce risk is heavily front-loaded in the early period of marriage.
- The statistical likelihood of divorce is highest in the first 5–10 years.
- Divorce risk declines substantially as marital duration increases.
- By 20+ years, the probability of divorce in any given year is extremely low (<1%).
- **Pew Research Center — "At Long Last, Divorce" (ACS/SIPP)** Shows extremely **low annual divorce rates for long marriages (≤1%)**, while early marriage data show steep dropoffs in the first decade.
- **Non-reviewed AI research.**

Combined Effect Of Wealth, Education, Age, and Duration

- When analyzed together, the factors above do not merely add up—they **compound** each other's stabilizing effects.
- Specifically, the couples with the lowest divorce risk are those who:
- **Are financially secure or own substantial assets**
  (Killewald, Lee & England, *Wealth and Divorce*, 2023).
- **Have higher education levels**
  (Wang, Pew Research Center, 2015; Center for Divorce Education).
- **Married in their late 20s or early 30s**
  (GTB Law, 2026; The Global Statistics, 2025).
- **Have been married for more than 10 years**
  Together, these variables create **significantly lower divorce risk**, positioning such couples as the statistically most stable demographic group.
- **Non-reviewed AI research.**

Acknowledge Increasing Gray Divorce

- **Age/“gray-divorce” headwind (apply a small upward nudge)**
- Later-life divorce risk has risen in recent decades (gray-divorce phenomenon), so for couples in their 50s–60s we should **nudge the estimate upward** slightly to reflect that macro trend. (For context on the structural shift, see cohort and age-pattern work synthesizing later-life risk.) (Stone/Wilcox/Bailey, AEI/IFS 2025, https://www.aei.org/op-eds/divorce-in-decline-about-40-of-todays-marriages-will-end-in-divorce/.) [aei.org]
- **Non-reviewed AI research.**

AI (Non-Reviewed) Conclusions At To Divorce Risk of Hypothetical Estate Planning Client – 1/5 of Average Rate of Divorce

- Compared with the general-population lifetime risk of **~42%** for first marriages, **a couple that is 20 years married, college-educated, and has $5M in net worth faces a remaining lifetime divorce risk that is roughly 1/5 to 1/10 as large**—i.e., **far lower** than average. (IFS 2025, https://ifstudies.org/blog/no-longer-a-coin-toss-less-than-half-of-marrriages-predicted-to-end-in-divorce.) [ifstudies.org]
- **Closer to 4–5% if: first marriage for both; no prior separations; low conflict; no stepchildren; strong shared social networks; and the couple is in early 50s** (i.e., fewer gray-divorce risk factors). (Education as primary stabilizer: Pew 2015; declining hazard: Kulu 2014.) [pewresearch.org], [link.springer.com]
- **Closer to 7–8% if: remarriage; blended families; substantial health shocks; impending retirement transitions; or the couple is entering the 65+ range where gray-divorce has been rising**. (AEI/IFS 2025; duration pattern: Kulu 2014.) [aei.org], [link.springer.com]
- **Bottom line** After explicitly accounting for (i) wealth's **net-of-education** effect and **diminishing returns**, (ii) education's strong 20-year survival evidence, and (iii) duration-dependent hazards (plus a small gray-divorce headwind), a **defensible, conservative** estimate for this couple's remaining lifetime divorce risk is **~4–8%**, with **case facts** determining where within that band they likely fall. (Killewald/Lee/England 2023, https://read.dukeupress.edu/demography/article/60/1/147/342803/Wealth-and-Divorce; Wang, Pew 2015, https://www.pewresearch.org/short-reads/2015/12/04/education-and-marriage/; Kulu 2014, https://link.springer.com/article/10.1007/s13524-013-0278-1; AEI/IFS 2025, https://www.aei.org/op-eds/divorce-in-decline-about-40-of-todays-marriages-will-end-in-divorce/; IFS 2025, https://ifstudies.org/blog/no-longer-a-coin-toss-less-than-half-of-marrriages-predicted-to-end-in-divorce.) [read.dukeupress.edu], [pewresearch.org], [link.springer.com], [aei.org], [ifstudies.org]
- **Non-reviewed AI research.**

Wealth Attracts Claims and Suits

- **Wealthy face risk of lawsuits – slats may help and not doing them because of divorce risk may hurt the client**
- Wealth correlates strongly with **being targeted in liability lawsuits**, particularly because lawyers pursue **deep-pocket defendants**.[marshmma.com]
- High-net-worth households report far **higher perceived and actual exposure** to litigation and carry disproportionately large umbrella policies as a result. [insurancejournal.com]
- Plaintiff strategies and the doctrine of **joint and several liability** explicitly encourage targeting the wealthiest defendant. [marshmma.com]
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- **AI Research not verified.**

Estate Planning Clients Want Asset Protection

- While not directly measuring personal-wealth lawsuit incidence, empirical studies confirm:
- Litigation risk increases when defendants have **higher assets**—a known effect in corporate litigation and malpractice cases.
- Statistically, “being collectible” is one of the top predictors of being sued.
- **Above is AI research not verified**.
- Wealthy clients want and need asset protection. SLATs and SLAT-Like trusts and related planning can facilitate asset protection planning while preserving access.
- SLATs (really SLAT-like trusts and related planning) should be evaluated in this process.

SLAT – What Exactly Is it You Don't Want to Draft?

- **Use the Lego Approach – instead of a SLAT form cobble together each component part that fits the client involved.**
- **Income tax status** – grantor (SLAT) or non-grantor (SLANT) with an adverse party approval.
  - SLATs may be used for tax burn, to transfer assets with the ability to swap back for basis adjustment, to permit broader flexibility with loan and tax reimbursement provisions.
  - SLANTs are powerful to maximize SALT, charitable, QSB (199A), state income taxes (in NY and CA as completed gift variants), and other benefits, not just estate taxes.
  - Mechanism to turn off grantor status may or may not be express.
- **Estate tax** – completed gift or incomplete gift.
  - Completed gift SLATs have been the norm to shift wealth out of a client's estate. Concerns over future estate tax changes keep this as a viable, even if not pressing, planning goal even if not applicable today.
  - Incomplete gift SLATs have not been used frequently but many SLATs have incorporated incomplete gift trusts as part of a mechanism to deflect a gift tax on a large note sale transaction. Post-OBBBA an incomplete gift SLAT might be used to secure asset protection while still qualifying for basis step up on death.
- **GST tax** – exempt or non-exempt.
  - The typical or traditional simple home-state ILIT often was not designed to be GST exempt, may have paid out to children at specified ages, and had no GST allocated to it.
  - More modern planning would typically structure SLATs as GST exempt dynastic trusts for asset protection for heirs as well as potential GST tax.

SLAT – What Exactly Is it You Don't Want to Draft?

- **Asset protection** – SLATs can be an effective part of an asset protection plan.
  - This is especially so for clients of more moderate means that will need access to the trust assets.
  - Clients of all wealth levels, not merely those with $40M net worth or higher, may benefit form this application of SLAT planning.
  - The time to implement asset protection planning is before it is needed. A young surgeon with modest wealth should consider a SLAT that they can add to in future years. Consider the recent DE case In the Matter of the CES 2007 Trust, Court of Chancery of the State of Delaware, C.A. No. 2023-0925-SEM (May 2, 2025) that stressed the importance that the ADAPT was created 7 years before the matter that gave rise to the claim.
  - Consider due diligence: AI background check, forensic analysis, projections, balance sheet, insurance summary and solvency affidavit.
- **Basis planning** – Post-OBBBA basis planning is a more significant planning objective for many.
  - SLATs can include a circumscribed GPOA to senior family members with wealth below the $15M exemption amount to gain a basis step up. This one benefit/technique could justify a SLAT plan for a couple with a net worth of only a few million dollars.
  - Swap powers (or the purchase of assets) can facilitate bringing assets back into the estate to gain a basis step up.
  - Powers of appointment can be included to facilitate basis adjustment.

SLAT – What Exactly Is it You Don't Want to Draft?

- **Access** – SLATs can be an effective part of an asset protection or tax plan, but a key motive is assuring access if needed.
  - Have an insurance plan done to fill financial gaps in the plan. The agent will need to understand differences for reciprocal trust planning, etc. Depending on age, wealth and anticipated work: disability, long term care, life on one or even both spouses.
  - What does the financial modeling reflect? Consider a 50% likelihood of success to table life expectancy to deflect an implied agreement or fraudulent conveyance and a 80% likelihood to age 95 or 100 for client peace of mind. The financial forecasting can direct what mechanisms and access the plan needs and which it might leave out. Stress test the results.
  - Spousal access but consider cautions about use, savings language, separate checking accounts, risks of premature death and divorce.
  - SPAT, DAPT, hybrid-DAPT and other provisions for enhanced access. The conversation should never be about "SLATs" but about all the variants that are possible and which make sense to the client. The client should weigh the benefits that perhaps a DAPT may provide for increased access versus the increased risk that may add to a SLAT variant.
  - Variations on the above with, for example, hurdles: 10 years + 1 day before beneficiary status becomes active, net worth under specified threshold, no spouse, other?
  - Loan provision.
  - Tax reimbursement clause.
  - Right of non-fiduciary to add charitable and other beneficiaries.

SLAT – What Exactly Is it You Don't Want to Draft?

- **Fiduciaries**– which fiduciary, non-fiduciary and powerholder positions might you include to accomplish client goals, differentiate the trusts for purposes of the reciprocal trust doctrine, permit access, and more?
  - Spouse as trustee.
    - Pros: No cost, easy, simple and comfortable for clients.
    - Cons: May not adhere to formalities, creates opportunities for abuse if a divorce is planned, no independence, less protection from arguments by creditors or IRS as to estate inclusion. Limitations on distributions to HEMS by spouse.
  - Non-spouse individual trustee.
  - Corporate trustee in trust friendly jurisdiction.
    - Pros: better state law, back up DAPT argument if non-reciprocal SLATs are uncrossed, better state tax position when trust is or becomes non-grantor, professional management, better asset protection.
    - Cons: costs, complexity.
    - Hybrid – name a family member or friend as trustee now and give a trust protector the right to change trustees, governing law and situs.
  - Separate or bifurcated trustee positions:
    - Insurance Trustee.
    - Distributions Trustee.
    - Art Trustee.
    - General and administrative trustee.
    - Others?
  - Investment advisor or trustee.
    - Create directed trust structure for more flexibility.
    - Investment advisor committee to facilitate business succession planning. How many people and how robust the provisions?
    - Different investment advisers appointed for different categories of assets.
  - Should any of the fiduciaries and powerholders be "housed" in an entity formed in the state where the trust has situs?

SLAT – What Exactly Is it You Don't Want to Draft?

- **Powerholders, Non-Fiduciaries** – which fiduciary, non-fiduciary and powerholder positions might you include to accomplish client goals, differentiate the trusts for purposes of the reciprocal trust doctrine, permit access, and more?
  - Spouse may be given 5/5 power in one SLAT (but not the other spouse in the other SLAT). Consider the power this can create to remove wealth from the trust and redirect it, e.g., to children from a prior marriage.
  - Circumscribed GPOA to try to obtain a basis step up on death of a family member with an estate well below the exemption.
  - Hybrid DAPT or SPAT power held by independent non-fiduciary.
    - Should the Hybrid DAPT or SPAT be in a DAPT jurisdiction from inception or required to be moved by a trust protector action before the hybrid DAPT or SPAT mechanism can be triggered?
    - Variations on the above with, for example, hurdles: 10 years + 1 day before beneficiary status becomes active, net worth under specified threshold, no spouse, other?
  - If grantor SLAT a power to a non-fiduciary to add a charitable or other beneficiary.
  - Power to loan held by non-fiduciary.
  - Power for independent trustee to reimburse for income taxes.
  - Swap or substitution power.
  - Power to beneficiary to disclaim entirety of transfer to trust.

SLAT – What Exactly Is it You Don't Want to Draft?

- **Assets** – Which assets to be transferred and how:
  - Simple old style ILIT with life insurance and small bank account.
  - Robust GST exempt SLAT like trust in a trust friendly jurisdiction directed to hold non-marketable assets.
  - Gifts of assets.
  - Gifts of assets subject to a defined value mechanism.
  - Sale of assets.
    - For a regular installment note.
    - Modified provisions in the installment note.
    - Self cancelling installment note (principal or interest adjustment).
  - Sale of assets subject to a defined value mechanism.
  - Home or vacation home the couple can use.
    - Transfer existing home vs. SLAT buying a new home.
  - What portion of the clients' wealth to be transferred now and perhaps in future years?
  - What impact on title to assets from current ownership to impact of trust?
  - Contractual arrangement affecting assets in trust, e.g. lease from trust owned real estate LLC to family operating company in another trust or retained, etc.

SLAT – How Many Variants of a SLAT Like Trust Are There?

- **If you don't like to draft SLATs because of divorce risk or reciprocal trust doctrine risk can you specify which particular type of SLAT-like trust you don't like?**
- 4 trust types (SLAT, DAPT, Hybrid DAPT, SPAT)
- Assume 12 possible variables, (tax reimbursement provision, loan provision, 5/5 power, power to add a charitable beneficiary, etc.) each with 2 choices (yes/no)
- Step 1 — Variations per trust type
- Each variable is binary →
- 2^12=4,096" variations per trust"
- Step 2 — Multiply by 4 trust types
- 4096×4=16,384
- Thus, you can create 16,384 distinct trust designs.
- Which of those variants are commentators saying is problematic when it is suggested not to do SLATs?

SLAT for Mass Affluent Clients (not Just Those over $40M)

- Example: Jane and John Smith are both physicians and worried about malpractice claims. They are in their early 40s, have a couple of young children and $2 million of non-retirement savings. Their estate will likely grow in coming decades as their professional careers grow and mature. They have inadequate life insurance to protect themselves or their children. The term coverage they have is owned by them personally.
- The couple has no concerns about estate taxes now but acknowledges that their estate might grow so that in decades from now that might be an issue. They understand the uncertainty of the political system and that in some future election the estate tax may be reinstated and/or made much harsher (e.g., a $3.5M exemption). Because that is so far into the future, they are not keen on spending much money on tax planning for that future risk.
- Jane's mother is in her 90s and not doing well. They help her out financially sending a check every month.

SLAT for Mass Affluent Clients Example Continued

- Under your guidance Jane and John create two non-reciprocal SLAT-like trusts.
- The trusts are created in their home state to save money as compared to using a better DAPT state for asset protection purposes. But because of their significant worries over malpractice risks in the next few years as their incomes grow Jane's trust will be moved to Nevada and John's to Alaska.
- Their uncle is named trust protector and give the right to move each trust to a new state, change the governing law for each trust and appoint a new trustee.
- Since a primary goal of the Smith's is to have sufficient assets in retirement **many ways to access funds in the trust** are created. The trusts include loan provisions, tax reimbursement clauses, the ability to appoint charitable beneficiaries and other means of access since the Smith's may need access to trust assets in their retirement. Jane's trust has a hybrid DAPT provision and John's a SPAT provision. Those additional means of access, especially to address the risk of premature death, are greatly appreciated by the Smiths. They understand that these provisions cannot be used until the trusts are moved to better jurisdictions.

SLAT for Mass Affluent Clients Example Continued

- Jane's mother is given a general power of appointment over each trust. On her passing the investment assets you have helped them grow will be included in her mother's estate and get a basis step up. That will eliminate all capital gains on their entire non-qualified plan investment portfolio.
- The client's financial adviser provides financial forecasts, and insurance analysis and all the review necessary to support the plan.
- Each SLAT includes a separate **insurance trustee** (Jane's cousin in her SLAT, and John's nephew in his) and insurance provisions. Each trust buys life insurance to create the plan that you determine protects all of their interests.
- The financial adviser reviews and helps each of Jane and John obtain more appropriate **disability coverage** then the meager policies provided at their practices.
- Jane gifts $500,000 to her SLAT. John gifts $650,000 to his SLAT. They will each make gifts in each future year as their income rises and you help document that they can afford to do so.

SLAT for Mass Affluent Clients Example Continued

- Jane and John now have a valuable **asset protection** plan that will grow as their wealth grows. Even though their estate tax concerns were at best lukewarm they appreciate that the wealth growing in their SLATs will be protected from estate taxation if they can grow their estates to that point (and recognizing the risks of unknown future tax law changes).
- Jane and John needed **insurance trusts** and a more robust life insurance plan and now they have that. But unlike their family and colleagues that complain about the complexity and hassle of annual gifts and those "Crummey" powers, Jane and John will never have to worry about annual hassles to fund their insurance trust as there is plenty of money in their SLATs.
- Jane and John had discussed setting up **trusts for their children** after they completed funding 529 plans. Now they don't have to do that.
- The **income tax savings** on Jane's mother's passing will be significant and pay for the plan many times over.

Ethical Obligations to Present and Explain Planning Options to Clients

- **SLAT-like trusts and ancillary planning is so broad and so varied that to make statements about the risks of a "SLAT" or that a "SLAT" should generally be avoided, or that a "SLAT" is only generally appropriate for a narrow wealth band doesn't make sense as variations of a SLAT and SLAT-like technicians and the variability of the structure, terms and application are so broad.**
- ABA Model Rules of Professional Conduct, **Rule 1.4(b)** states: "A lawyer shall explain a matter to the extent reasonably necessary to **permit the client to make informed decisions** regarding the representation." [americanbar.org]
- Does this create a professional obligation to **present the client with all legally viable options**, explain the consequences, risks, tradeoffs, and alternatives, and ensure the client has enough clarity to choose among those options based on their own goals? Can you ethically exclude SLAT-like planning from your discussion?
- Based on an analysis of recent high-profile estate planning **malpractice cases**, presenting a client with options and enabling the client to choose which options for planning they wish to pursue is protective of the adviser.
- Isn't it best to give the client options, explain the risks about using SLATs and the potential impact of divorce, but also explain the benefits, and permit the client to make an informed decision?

SLAT Divorce Planning Options

- Spouse/beneficiary loses that status upon divorce. This could be a dangerous option. Cutting a spouse out may eliminate grantor trust tax issues but will the post-divorce couple have sufficient assets to survive post-divorce?
- Split the trust into two SLATs on divorce: ½ into a new SLAT that is identical to the existing SLAT and the second half into a new SLAT that has a floating spouse clause so that the donor/settlor spouse may have if they remarry a new opportunity for indirect access.
- Use a hybrid DAPT, SPAT or DAPT structure so that the donor/settlor spouse can gain access to the trust if necessary to negotiate divorce arrangements.
- Contrast these other options with the automatic removal of the spouse on divorce. Which approach provides the access the clients need now and post-divorce?
- Some clients may reasonably assess that they are more concerned about estate tax, asset protection or other SLAT-like plan benefits then they are about divorce risk. Some clients may weigh the tax and asset protection risks and complexity of DAPT, hybrid-DAPT, SPAT uncertainties as greater than the risks of divorce.

SLAT Divorce Practice Considerations

- Practitioners might consider adapting some variation of the following practices in the representing spouses pursuing any planning, including SLATs:
- Try to communicate key consequences and warnings in writing. Clients are unlikely to remember, or may develop selective memory, if a future issue arises.
- Remember, this is not only about SLATs. If clients retitle asset ownership that may have an adverse consequence if a future divorce occurs. The most common and basic planning can have material and negative impact. This is not only about SLATs.
- Include provisions about conflicts that are inherent in representing spouses in your retainer agreement.
- Explicitly address in your retainer agreement whether you must disclose confidences from one spouse to the other spouse or whether you cannot do so. Be clear as to whatever policy you have and be sure everyone is aware of it.
- State in your retainer agreement that if one spouse only attends the meeting that they agree to inform the other spouse of what was discussed, and that the other spouse agrees to this. Be certain to address all communications to both spouses if both are represented.
- Remind clients in communications of issues, considerations and options. Let the client make the final decision as to whether the estate tax, asset protection or other benefits of a SLAT-like plan outweigh the risk of divorce. Guide the client to make the decision. Only the client can weigh how they view the different risks.

SLAT Divorce Practice Considerations

- If non-reciprocal SLAT-like trusts are used identify many of the key differences in a letter or memo in addition to the draft trusts containing these clauses. That should reinforce the reality that there are material economic consequences to provisions drafted to address tax issues, e.g., the reciprocal trust doctrine.
- Have the client's financial adviser prepare projections and review both investment and insurance planning to determine which of the financial "gaps" created by the SLAT-like plan can be addressed in those manners. Having a second adviser on the planning team independently meet with the clients and explain these considerations is helpful for the clients to understand these matters and may be protective of the estate planner since another independent adviser confirming that the client understood the economic consequences and considered investment and insurance options that may address some of those gaps will be helpful.
- Offer the client DAPT, hybrid DAPT and SPAT variations or splitting a SLAT into two trusts one with a floating spouse clause and one with the same spouse continuing. There are options. Let the client choose.

Is The Over-Controlling Husband The Achilles Heel of SLAT Planning?

SLATS AREN'T INHERENTLY BAD, BAD ACTORS ARE

United States V. Estate Of Grace 395 U.S. 316 (1969)

- Estate of Grace is the seminal case on the reciprocal trust doctrine. But consider the control the husband exercised that called the plan into question:
- "Decedent [husband]retained effective control over the family's business affairs, including the property transferred to his wife. She took no interest and no part in business affairs and relied upon her husband's judgment. Whenever some formal action was required regarding property in her name, decedent would have the appropriate instrument prepared and she would execute it."
- "The trust instruments were prepared by one of decedent's employees in accordance with a plan devised by decedent to create additional trusts before the advent of a new gift tax expected to be enacted the next year. Decedent selected the properties to be included in each trust."
- "Grace, acting in accordance with this plan, executed her trust instrument at decedent's request."
- "Indeed, they were part of a single transaction designed and carried out by decedent."

Smaldino v. Commissioner, T.C. Memo 2021-127 (Nov. 10, 2021)

- The Smaldino Court recharacterized a purported transfer from husband to wife and then wife to trust as a direct gift from husband to the trust because of the excessive control the husband maintained.
- "Mrs. Smaldino testified that before the purported transfer in question she had already made "a commitment, promise" to her husband and family that she would transfer the LLC units to the Dynasty Trust."
- "…as a practical matter **there was never a time when Mrs. Smaldino would have been able to effectively exercise any ownership rights** with respect to any LLC membership interests. Moreover, for the reasons previously discussed, we do not believe that petitioner ever intended for her to do so."

C.S. V. R.H., 2025 N.Y. Slip Op. 51426(u), 2025 Wl 2640123 (N.Y. Sup. Ct. September 8, 2025) - 1

- "…since the outset, he [the husband] has and continues to actively manage and control the trust assets."
- "…Wife impressed as a committed woman who **acquiesced to Husband on all things**…"
- "…completely trusted Husband with the family finances…"
- "Husband lacked credibility on the core financial issues, specifically as to the critical matter of his control over the Trusts…he alone decided who to appoint and remove as Trustee and Managing Director of the LLCs and which assets went into the Trusts and when, and that he alone set the below-market rents for the Trust properties in which the family lived…"
- "Husband did not adequately explain why he did not seek court approval for his post-commencement conduct with respect to Trust assets, including, *inter alia*, removing Wife from the LLCs and evicting her from the Trust homes; paying "distributions"; and, ultimately, decanting the Trusts into two new Trusts formed under Delaware law."
- "…**Husband was Mr. McCabe's [estate planning attorney] "main point of contact**…"
- "I trusted him, and I had a full plate with the girls and it didn't interest me."
- "…Wife testified credibly that **she first saw documents when the parties went into Mr. McCabe's office to sign them; she was not provided any documents prior to the meetings**…

C.S. V. R.H., 2025 N.Y. Slip Op. 51426(u), 2025 Wl 2640123 (N.Y. Sup. Ct. September 8, 2025) - 2

- "Wife received no independent legal or financial advice about the creation of the Trusts and was not advised to obtain independent counsel; she was not informed as to what would happen to the marital assets held in trust in the event of divorce…"
- "Wife testified credibly that she does not know what a GRAT is (10/13/22 Tr. 51) and the record is devoid of proof that she was involved in their formation."
- "Wife was not consulted or involved in the creation of any of the LLCs, did not know what her duties and responsibilities as Managing Director were, and was not advised to seek independent counsel with respect to her removal as Trustee and appointment as Managing Director (10/13/22 Tr. 79; 12/2/22 Tr. 41, answering questions as to how Wife signed the LLC operating agreements: "R. asked me to sign it, and I signed it")…"
- "…Husband commenced a systematic effort to totally remove her from the Trusts, cut her off from the marital assets and out of the family wealth, and evict her from her homes without court approval or any notice."
- "Husband has had and continues to maintain unrestricted control over and access to Trust assets and enjoys their use and benefit without interruption. On the other hand, Wife never had any control over the Trusts, LLCs, or assets; she was a figure-head who served in name only at Husband's pleasure."

Netter v. Netter – DAPT Funded During Marriage to Defraud Your Spouse Shouldn't Succeed, and Didn't

- Netter v. Netter provides a comprehensive appellate framework for analyzing whether trust interests are treated as divisible property in a marital dissolution proceeding.
- The decision protected/respected a third-party spendthrift trust created by the spouse's parent before marriage, This trust was not funded by marital assets. The trial court found that under the trust agreement, trustees other than the defendant had the power to pay or apply net income or principal to or for the use of the defendant and his issue as they, in their sole discretion, determined to be advisable for the comfort, support, and maintenance of the defendant and his issue.
- The court discussed a two part test. The first prong asks whether the holder has a presently enforceable right to receive the interest based on contractual principles or a statutory entitlement, and if such a right exists, the interest is part of the marital estate and is distributable as property.
- The second prong is described as more fact intensive and focuses on the likelihood that the holder eventually will acquire an enforceable right in the interest, including whether the interest will likely vest or whether the holder will otherwise acquire a definitive right to it.

Netter v. Netter – DAPT Funded During Marriage to Defraud Your Spouse Shouldn't Succeed, and Didn't

- Netter describes the other three trusts as self-settled trusts formed by the defendant after the marriage with marital assets. The Court disregarded three self-settled spendthrift trusts, DAPTs, created during the marriage and funded with marital assets, notwithstanding their South Dakota domestic asset protection trust form. The DAPTs were funded without the wife's knowledge and while the marriage was in trouble. The defendant husband used most of the marital assets in doing so.
- Connecticut will not enforce the law of another jurisdiction nor rights arising thereunder that contravene Connecticut public policy,
- If a domicile court uses this reasoning, planners may need to assess whether reliance on a favored DAPT jurisdiction's substantive rules will be effective when the relevant litigation forum applies local public policy and distribution doctrines.
- Netter concludes that this dissipation concern supported the conclusion that even if the trusts satisfied the Connecticut Act, they would be void as a matter of public policy because sustaining them and excluding their assets from distribution would unfairly prejudice the spouse,

SLATs Are Not Inherently "Bad" But Bad Actors Are

- Where a spouse exerts unreasonable control over the transactions, LLCs, and trusts the intended consequences, whether for tax, asset protection or matrimonial purposes, may not be realized.

- Practitioners need to be wary of the controlling spouse and **be certain that the passive spouse**:
  - Is involved in meetings.
  - Receives documents to review in advance of meetings directly.
  - Understands documents she signs.

- Practitioners should **warn the overly controlling spouse** to:
  - Respect the formalities of the trust and any entity structures.
  - Observe formalities.
  - Permit those properly charged with certain functions and duties to fulfil them, and not to usurp them.

SLATs, Divorce, and the Trustee's Perspective

GRANTOR'S INTENT VERSUS BENEFICIARY'S RIGHTS – SLIDES FROM ABIGAIL O'CONNOR OF PEAK TRUST

Spouse-Beneficiary's Requests

- Request often comes to trustee during the divorce.
- Requests for:
  - Legal bills.
  - Living expenses.
  - Large distribution for a new home.
- Trustee's primary considerations:
  - Spouse's interest as a beneficiary.
  - Impact on other beneficiaries (duty of impartiality).
  - Grantor's intent.

Spouse's Interest as Beneficiary

- Three general approaches seen most frequently:
  - Spouse is named as beneficiary and continues as beneficiary during and after divorce.
  - Spouse is defined and deemed deceased upon the initiation of a divorce.
  - Spouse is defined and deemed deceased upon finalization of divorce or dissolution of the marriage.
- Decision will be different depending on the definition.
- Trustee needs clarity in the document to understand the exact nature of the interest.

Other Considerations

- The other beneficiaries.
  - Are children current beneficiaries or remaindermen?
  - Consents are generally unavailable.
- Grantor's intent.
  - Is payment of legal fees to fight against the grantor consistent with the grantor's intent?
  - If this is a concern is there a drafting solution?
- Other issues that arise.
  - Discovery requests.
  - Depositions.

Aging Clients

ITS MORE THAN JUST SNTS AND BOILERPLATE REVOCABLE TRUSTS

Revocable Trust Can Be More Protective

- Variations of typical revocable trust planning can provide better protection for aging and infirm clients.
- Fund the trust with all assets possible to have more control during disability, chronic illness or cognitive decline.
- Obtain a tax identification number and use it on all trust accounts.
- Name an institutional co-trustee or successor trustee.
- Name a trust protector and provide express powers to remove and replace trustees, and perhaps other powerholders, include a power to demand an accounting, etc.
- Consider mandating periodic evaluation and reports by an independent care manager given to the trustee, trust protector and a family member (e.g. the agent under the client's health proxy).
- Require the consent of a non-adverse party to modify or revoke a revocable trust (e.g. and adviser).

Asset Protection

IMPORTANT FOR MOST CLIENTS REGARDLESS OF ESTATE TAX

Huckaby – Really Bad Facts Assure DAPT Had to Fail

- U.S. v. Huckaby is a bad-facts, poorly executed DAPT case. It should not pose a serious threat to carefully structured domestic asset protection trusts (DAPTs).
- The court permitted the IRS to attach and foreclose on California real estate held in a Nevada domestic asset protection trust (DAPT) to satisfy a tax judgment against the settlor-beneficiary.
- The trust's settlors were California-connected individuals, the sole trust asset was California real estate, and the settlors served simultaneously as settlors, beneficiaries, and trustees. Despite drafting the trust under Nevada law, the plan ignored longstanding conflict-of-laws principles governing creditor claims against trust assets.
- Applying Restatement (Second) of Conflict of Laws § 280, the court held that California law—the situs of the real property—controls creditor access to the asset. Because California does not recognize spendthrift protection for self-settled trusts, the DAPT failed.
- The court concluded that Huckaby held both the legal interest (as trustee) and the equitable interest (as beneficiary) in the property, making the IRS lien enforceable. The court rejected arguments that trustee title insulated the asset, and it granted summary judgment authorizing foreclosure of Huckaby's one-half interest. This outcome was entirely foreseeable. DAPTs have long been vulnerable when the settlor is not resident in a DAPT state, the assets are located in a non-DAPT state, or bankruptcy or major creditors are foreseeable. Huckaby reinforces that a Nevada DAPT cannot override California property law, and that careless execution—especially using California real estate and a California-controlled trust—will defeat asset-protection planning.
- United States v. Huckaby, 2026 WL 587784 (E.D. Cal. Mar. 3, 2026).

Netter v. Netter – DAPT Funded During Marriage to Defraud Your Spouse Shouldn't Succeed, and Didn't

- Netter v. Netter is discussed above under divorce considerations of planning. A key consideration post-Netter is it just a really bad fact case where the husband abusing the DAPT technique was treated appropriately, or does it suggest that based on the Netter Court's reasoning that states will assert public policy objectives to overturn or pierce DAPTs that were not as egregious.

Domestic Asset Protection Trust Upheld In DE

- This is a favorable case but all risks and issues not addressed, e.g. full faith and credit. There are many of lessons to learn.
- Many clients do not have the wealth to shift assets out of their estates to protect them from creditors. A DAPT may be, subject to some remaining uncertainties, a worthwhile plan to protect clients who view themselves as below the current exemption levels.
- Many clients need to pursue asset protection planning. They may have no worry about estate tax.
- Self Settled Domestic Asset Protection Trusts (DAPTs)
- In the Matter of the CES 2007 Trust, C.A. No. 2023-0925-SEM.
- **Claim**. The claimant sought to pierce the trust to reach assets held in limited liability companies (LLCs) and the Court refused. The Court found that the trust met the requirements of Delaware law to qualify as an asset protection trust and should be respected. This case provides you with a roadmap of many dos and "don'ts" in pursuing this type of planning.
- **Facts of Case**. The settlor created the Trust on April 30, 2007, for the benefit of its beneficiaries, namely the settlor's wife (if any), parents, and issue. The trust predates the claimant's loan and the follow-on Michigan litigation. In 2014, the claimant loaned one of the settlor's companies' money to finance a luxury real estate development project in Michigan. The deal wasn't successful and the claimant sued. In 2019, the Michigan Court entered a judgement of almost $14 million in favor of the claimant. A Michigan court held in favor of the claimant and gave him an award the settlor of the trust plan was personally required to pay. Because the settlor had no assets to pay the claim, the claimant tried to pierce the trust plan involved in this case to get at the valuable real estate assets it held.

Domestic Asset Protection Trust Upheld In DE

- **Requirements for a Delaware Asset Protection Trust**:
  - The Qualified Dispositions in Trust Act (the "Act") permits someone to create an Asset Protection Trust, and irrevocably transfer assets to the trust, to protect those assets from claims against the grantor/former owner. The requirements are contained in 12 Del. C. §§ 3570–76.
  - The requirements include: The transfer must be a "qualified disposition." To a qualified trustee, which is a Delaware resident or an entity authorized to act as a trustee in Delaware who is subject to supervision by the Bank Commissioner of the State, the Federal Deposit Insurance Corporation, or the Comptroller of the Currency.
  - The trust agreement must invoke Delaware law.
  - The trust must include a spendthrift provision.
  - The trust must be irrevocable.
  - The trustee must maintain or arrange for custody in Delaware some of the property that is the subject of the qualified disposition.
  - Records for the trust should be maintained.
  - The trustee must either prepare or arrange for the preparation of fiduciary income tax returns for the trust, or the trustee must otherwise materially participate in the administration of the trust.

DE Defendant Loses in Subsequent CO Case

- The Defendant in the DE DAPT case was reached by a later Colorado Court for transferring a valuable real property to an LLC held by his DAPT. That holding unwound the transfer as a fraudulent conveyance but did not disturb the DE Court's upholding the validity of that DAPT..
- Note that the DE case contained details of many foot faults that ignored entity/trust formalities and could have undermined the favorable result. That the Defendant continued such actions is no surprise. That those actions were overturned is also no surprise.
- October 2014, the plaintiff made a construction loan to a limited liability company Schubiner controlled. Schubiner executed a Non-Recourse Carve Out Guaranty (the "Guaranty") providing that the plaintiff could collect against him personally for a default on the loan.
- January 2020, the Michigan state court entered an order enjoining Schubiner "from transferring assets outside of the normal course of business pending satisfaction of the final judgment."
- March 2020 Defendant Schubiner transferred real property to defendant Harbor Real Estate Company, LLC ("Harbor")for $10. That transfer was one made without receiving reasonably equivalent value in exchange. So, the CO Court held that it was a fraud aimed at evading collection on a judgment against Schubiner.
- Can IV Packard Square LLC v. Harbor Real Estate Co., LLC, and Craig E. Schubiner, No. 23-cv-00934-CYC (D. Colo.) 2025.

Basis Step Up

$15M EXEMPTION SHIFTS FOCUS TO BASIS

Should you Terminate Old Credit Shelter Trusts?

- Though your clients might still have them, they are in some instances no longer advantageous. They used to be more common when the estate tax exemptions were much lower and prior to portability, and thus the threat of paying higher estate taxes loomed larger. They were also more popular at a time when portability didn't exist (in other words, before widows could use their deceased spouses' estate tax exemption). The objective of the credit shelter trust was to let the surviving spouse benefit from assets when the first spouse died, but to keep those assets out of his or her estate.
- But the past goals of the trust are increasingly irrelevant. In 2026 the federal estate tax exemptions will be $15M. So, many clients who still have credit shelter trusts don't really end up avoiding any estate taxes with them. Instead, they have costs incurred every year to administer the trusts and to file the trust income tax returns—and all for assets that won't get a step-up in income tax basis when the surviving spouse dies. That could lead to a significant income tax cost.
- The solution may be to terminate such trusts entirely if your clients have them and put all the assets back into the spouse's name. The result may be simpler and better tax results.
- However, you also have to make sure there are no liabilities (such as medical costs) that could dissipate those assets if the trust is terminated, and the assets are distributed to the surviving spouse. Review the trust to determine whether it can be terminated, to confirm that there are no legal reasons for keeping it, confirm other beneficiaries are agreeable and then to draft the documents to end the trust.

Basis – Grantor Trust Under Revenue Ruling 2023-2.

- Letter to Treasury, on March 20, 2023, Senators Elizabeth Warren, Bernard Sanders, Chris Van Hollen and Sheldon Whitehouse wrote a letter to Janet Yellen Secretary of the Department of the Treasury encouraging her to "…use your existing authority to limit the ultra-wealthy's abuse of trusts to avoid paying taxes. Billionaires and multi-millionaires use trusts to shift wealth to their heirs tax-free, dodging federal estate and gift taxes." The letter goes on to detail various loopholes and abuses that they believed should be acted upon. Shortly after the sending of the above letter, Revenue Ruling 2023-02 below was issued.
- One of the issues raised in many estate tax proposals by the Democrats has been the concern about the perceived abuse of practitioners taking the position that assets in an irrevocable grantor trust can obtain a step-up in income tax basis at the grantor's death even though those assets are not included in the taxpayer's taxable estate.
- Revenue Ruling 2023-2 makes the IRS position now clear that there's no step-up in basis, according to the IRS, for such assets being stepped up.
- Section 1014 is inapplicable because no estate-tax inclusion and it is not a bequest under state law
- If there is debt between the trust and grantor this Ruling does not apply.
- Some advisers believe the IRS is wrong. If you do take a contrary position disclose it clearly on the returns affected. One suggestion is file an income tax return paying income tax based on a calculation without a basis step up. Then file a refund claim and fully disclose the rationale.
- What can be done? Swap assets out for a step-up. That should be part of an annual review. Then the asset would get a basis under 1014.
- What is the trust's basis in case of sale to grantor trust if 1014 is inapplicable? Ruling does not address this. If Section 1014 does not apply, the possibilities are Section 1015(a), 1015(b) or 1012
- Is there gain at death? The Ruling does not answer this question.
- "nonrecognition on death is among the strongest principles inherent in the income tax" See Backemeyer 147 T.C. 526, 544 (2016).

Basis – Grantor Trust Case for Step Up

- Bellmont Investments, LLC Scott Seldin as partnership representative is a case that appears to be addressing this issued.
- IRC § 1014 Step-Up in Basis: The strategy employed by the grantors involved the trusts being treated as grantor trusts during their lives. Upon the death of a grantor, the assets held in the grantor trust that cease to be a grantor trust are treated as if they were transferred from the decedent's estate, thereby potentially receiving a fair market value basis adjustment (step-up) under IRC § 1014.
- Partnership Basis Adjustments (IRC §§ 754, 755, 734(b), 743(b)): Belmont Investments, LLC, as a partnership, made elections under IRC §§ 754 and 755 to adjust the basis of partnership property under IRC §§ 734(b) and 743(b) upon the deaths of Mrs. Seldin and Mr. Seldin.
- IRC § 743(b): This election allows for an adjustment to the basis of partnership property when a partnership interest is transferred (e.g., due to death), effectively giving the transferee (the trust, in this case) a basis in its share of partnership property equal to its basis in the partnership interest.
- Commissioner's Disallowance: The Commissioner has disallowed these basis adjustments, arguing that the UBIA (Unadjusted Basis Immediately After Acquisition) of qualified property, and consequently the QBI deduction, was overstated. This disallowance is the central point of contention in the Tax Court petition.

Basis – Grantor Trust Case for Step Up

- Impact on Depreciation and Capital Gains: The disallowance of basis adjustments has significant implications for future depreciation deductions, calculated capital gains or losses upon asset sales, and other tax attributes related to the partnership's assets. For instance, the petition states the adjustment to "Buildings and Other Depreciable Assets" and "Land" was disallowed, impacting their reported tax balances.
- Tax Optimization Opportunities (as indicated or implied by the petition)
  - Grantor Trust with Basis Step-Up: The strategy of using an irrevocable grantor trust (with a power of substitution) that terminates its grantor trust status at death (or upon exercise of the power) to achieve a basis adjustment under IRC § 1014 is a sophisticated tax planning technique designed to allow assets to remain outside the grantor's taxable estate while still receiving a new income tax basis at death. Mr. Seldin's exercise of his power to reacquire trust corpus for his grantor portion further highlights a proactive approach to basis management.
  - Litigation as Part of Optimization: The petition itself represents an effort to optimize the tax outcome by challenging the IRS's adjustments, thereby seeking to preserve the intended tax benefits of the planning.

Should Incomplete Gift Trusts Now Be Used for Basis Step Up

- The calculus of which types of trusts should be used will be different for some clients post-OBBBA.
- You can create an incomplete non-grantor trust and have both estate inclusion for step up and a non-grantor trust to garner increased SALT, charitable, 199A and other tax benefits under OBBBA.
- Caution – NY and CA will no longer respect incomplete gift non-grantor trusts so there may be no state income tax savings. Completed gifts trusts may still avoid NY and CA income taxation but then you MAY have to use other tools to gain estate inclusion for basis step up.
- Caution – The IRS will no longer issue PLRs on ING trusts.
- Settlor retains testamentary and inter-vivos LPOA to cause estate inclusion?
- Other considerations.

Opt in Community Property Trust

- If a couple residing in a non-community property state (with no community property assets) creates a trust in a jurisdiction that has an **opt in community property trust statute** (AK, TN, SD, and others), they may qualify for a full step up in income tax basis on the first spouse's death.
- 1014(b)(6)..

Estate Inclusion Considerations

PLANNING POST POWELL/MOORE AND OTHER ISSUES

Implied Agreement Remains a Risk

- Clients frequently (mostly) refuse annual review meetings and proper administration of their plans. That can set up the risk of improper actions that corroborate an implied agreement that defeats the plan.

- An implied agreement may be found even if the settlor is never a beneficiary of the trust. Estate of McCabe v. United States, 475 F.2d 1142 (Fed. Cir. 1973) - Husband established trust with longtime friend and business associate as trustee. Income plus principal for illness or emergency to wife, remainder to children. 20 years later, wife sent trustee letters requesting distributions be made to her husband the grantor. Four payments were made to him before his death. Court found IRC 2036 retained interest even though he was never added as a beneficiary. This probably was sloppy administration of the trust as the husband had no right to distributions.

- "The facts of the instant case however show as clearly as in those cases a retained life interest. Decedent was not a detached settlor, and the trustee (to all intents the individual trustee was the sole trustee) did not act exclusively for the benefit of the ostensible beneficiary, Mrs. McCabe. The dealings among the three of them — decedent, trustee and wife — in my opinion raise an inference of a prearrangement that decedent should retain control for his benefit so long as he lived. In these dealings, Mrs. McCabe and the trustee recognized and surrendered to the decedent's interests, throughout."

2036(b) Voting Stock Considerations

- IRC Code Sec. 2036(b) states that if a taxpayer transfers entity interests to a trust, but retains voting rights over those interests, the entity interests will be included in the taxpayer's estate. Note that this may not make the transfer an incomplete gift.
- If the settlor of the Trust retains control of investments in the trust (i.e., as an Investment Advisor or Investment Trustee), the trust could include a carveout for 2036(b) stock.

- **Sample Language**: Notwithstanding anything else herein to the contrary:
  - in no event shall any power or authority granted hereunder permit any Investment Trustee to vote, directly or indirectly, the shares of any controlled corporation described in Code Sec. 2036(b) and the Regulations thereunder if the existence of such a power could result in the inclusion for Federal estate tax purposes of such stock in the gross estate of such Investment Trustee or the Grantor of any trust hereunder.
  - in no event shall any power or authority granted hereunder permit any Investment Trustee to vote, directly or indirectly, the voting interests in any manner that affect distribution rights, liquidation rights, or the provisions of any governing document governing such rights, if the existence of such a power could result in the inclusion for Federal estate tax purposes of any equity holding in the gross estate of such Investment Trustee or the Grantor of any trust hereunder.
  - In either of the above cases such Investment Trustee shall be disqualified from participation in such action and such powers shall be exercised only by the remaining Investment Trustees who are not so disqualified, if any. If there are no qualified Investment Trustees, then INDEPENDENT-NAME shall take such actions if not in violation of this provision. If the aforementioned person is unable or unwilling to serve then the Trust Protector shall appoint a person to serve in such capacity.

- Advise clients that they should not sign any documentation on behalf of the Trust voting the stock, as that may defeat the clause provided in the trust.

Entity and Complex Transfer Planning Ideas

PRACTICAL IDEAS THAT MAY ENHANCE PLANNING

Master Governing Document For Client With Scores Of Entities

- Some clients have a tremendous number of entities. For example, a real estate developer would be advised to set up a separate LLC for each deal/property. But that might result in dozens, even scores of entities. How can documentation be created for governing this many entities without the cost and complexity of a separate document for each LLC? An answer might be to create a single master or aggregate operating agreement for all entities and have each entity sign one agreement. That would greatly reduce the paperwork and costs of a transfer where you might need to only amend and restate one agreement for each phase of the transaction rather than scores of documents.
- Master Operating Agreement Selected Provisions
- WHEREAS, the intent of this Operating Agreement is to provide a “master” or umbrella operating agreement which the real estate entities owned primarily by a member of the Client-Name family, and trusts for such family members, can be bound to simplify the administration of all such real property limited liability companies, provide uniformity of the governing provisions and documentation for such entities, and thereby reduce legal and administrative costs and complexity.
- WHEREAS, it is the express intent of each Party hereto that this Operating Agreement, in conjunction with any joinder or adoption agreement, be equivalent to a separate operating agreement signed by each individual Company, the members of that Company, and the Manager of each Company. By way of example and not limitation, each Party hereto covenants and agrees to execute any further documentation, such as a variation of this Operating Agreement reflecting only information pertinent to that particular Company, its members and the Manager and redacting any information pertinent to any other Company and their Managers.
- WHEREAS, any reference to a “Member” or “Membership Interest” or any other term relevant to any member, Company, etc. shall only refer to a Member or Membership Interest or any other such term in a particular Company and in no manner shall provide any Member or Membership Interest in any one Company any rights or obligations in any other Company.

Savings Language For Governing Documents Whose Interests May Be Transferred Subject to Defined Valuation Mechanism

- Trust companies and CPAs may inadvertently overlook Wandry adjustment language and incorrectly list a specific number of shares or percentage of membership interests as an asset of a trust or on a K-1. Consider adding savings language to the entity governing documents as a fallback argument. While there is no assurance that this will work consider:

- **Membership Interest or Interest:** A Member's Percentage Interest, right to distributions under this Agreement, and any other rights which such Member has in the Company, subject to such Member's obligations to the Company as provided herein or under the Act. Membership interests may be transferred based on fixed dollar formulas such as the approach used in Wandry v. Commissioner, T.C. Memo. 2012-88. IRS non-acquiescence: Action on Decision (AOD) 2012-04, published in IRB 2012-46 (November 13, 2012), or other defined value mechanism approaches. In such event the listing of a percentage membership interest in this Agreement or in any other application when in fact that interest is not at that time a known percentage interest but rather a dollar value subject to a valuation adjustment mechanism shall expressly not change the legal right from being a dollar interest to being a percentage interest until such time as such change shall become confirmed and certain under the terms of the defined valuation mechanism governing that interest.
- Remember under the Sorrenson case if the formalities of the valuation adjustment are ignored they may be disregarded.

FLP/LLC interests may avoid estate inclusion under a Powell challenge

- Removing all interests from the client's estate may not suffice.
- In the Powell case FLP assets were included in decedent's estate under Code Sec.2036(a)(2) even though the taxpayer only owned LP interests (i.e., the taxpayer did not own any GP interests that would have clearly provided him control). The decedent, the Court reasoned, retained right in conjunction with other person to designate who could enjoy the property or its income under Code Sec. 2036. Also, under Code Sec. 2038 the taxpayer/decedent had retained the power to alter, amend, revoke, or terminate the transfer. The court reasoned that the decedent as owner of 99% of the FLP interests "in conjunction with" all the other partners could dissolve the partnership at any time. Even though some argue that Powell was a bad fact case many practitioners are concerned to try to avoid its reach by having the decedent divested of any rights to control distributions from the entity, liquidation of the entity, or the right to change the provisions of the governing instrument that pertain to those two rights.
- Estate of Powell v. Commissioner, 148 T.C. No. 18 (May 18, 2017) June, 2017.

There Are Various Approaches To Endeavor To Negate A Powell Argument

- Not addressing the issue.
  - This non-approach might be used for client LLCs where that level of planning is too complex or costly and/or when an active business interest is involved. This approach is not necessarily without thought or merit as some commentators view the Powell/Moore cases as a bad fact case that should not necessarily apply in all other situations, and certainly not if there is an actual operating business.
- Special Voting Membership Interests.
  - One approach is to create a special voting membership interest and have the taxpayer/transferor divest him or herself of all those interests. A common way that is implemented is recapitalizing the entities involved creating a special voting membership interest that controls liquidation, distributions, and amending that provision so of the governing documents. Then, the taxpayer/transferor would sell (not gift) that special voting membership interest to a trust in which the taxpayer/transferor has no interests or control.
  - The goal of this approach is for the company to segregate specific powers and voting rights governing decisions as to distributions, dissolution and amending provisions governing those matters in its operating agreement in and as a voting membership interest as provided for in the operating agreement.
- Authorized Member Voting Rights.
  - Carve out voting rights in the operating agreement. For a multi-member LLC, a definition of "Authorized Members" could be provided to endeavor to address the Powell Issue as an alternative. It could be designated in the operating agreement that only the Authorized Member may vote on liquidation, distribution or changing those provisions in the operating agreement. Effectively other named persons who are not subordinate to the taxpayer would be the special voting members.

There Are Various Approaches To Endeavor To Negate A Powell Argument

- Sell Entity Interests to Irrevocable Trust.
  - The client may sell all ownership interests in the entity to an irrevocable trust. If this is done the taxpayer should not be the investment advisor of the new trust and in fact the trust document should preclude her from serving in that role.
- Independent Trust Protector Consent.
  - You could require that the operating agreements governing the entity, for trust members to have consent of an independent trust protector for distributions and liquidations. Since the taxpayer is commonly named as the investment trustee or investment advisor and the trust protector is (or must be in this approach) independent, this may be a viable approach although there is no law on this (or most aspects of the planning discussed in this letter). The trust protector would have to approve any modification of the operating agreement as to distribution or liquidation requirements or to make a distribution or liquidation from the LLC.
- Business Judgement Rule.
  - Some believe that drafting governing documents to include a business judgment rule/requirement may suffice to deflect the Powell issue. This concept is that if the persons holding distribution and liquidation rights have to exercise the powers that for example a manager in an arm's length arrangement with unrelated parties would have to exercise that there could be no inappropriately retained rights to cause estate inclusion.

Other Clever LLC Drafting Considerations from Alan Gassman, Esq.

- If a transfer into the LLC would cause a 721(b) tax it goes to a separate compartment of the LLC and is not "mixed into avoid the diversification that could trigger gain.
- If an LLC interest is gifted to a Crummy Trust the transferability restriction could be abated if the Trust is for relatives of the majority or voting control owner to perhaps make the Crummey Power viable and the interest in fact a “present interest.”
- Possible transfer on death provisions so that probate may be avoided upon death under the Florida case law on this.
- Consider making the LLC operating agreement an executory contract so that charging order protection will hold up n bankruptcy.
- Safety clause to avoid violation of 2nd class of stock rules for S corporations and LLCs taxed as S corporations.
- Safety clause to avoid loss of tenants by the entirety (“TBE”) status by breaking the 6 unities by accident.

Observe Formalities

Recent Cases Demonstrate A Theme To IRS Audit Challenges

Formalities are Critical to Observe

- Every practitioner knows that you must observe formalities of entities and trusts. Everyone knows that if a client is president of a corporation she should sign in that capacity when signing on behalf of the corporation. Similarly, it is common knowledge that if a taxpayer is a shareholder in an S corporation that taxpayer should be issued a Form K-1 covering the number of days shares were owned during the year. And so on. Yet, how often do clients give their advisers the latitude to guide them to observe formalities? Not often enough.
- In the context of complex estate plans, adhering to formalities, including the economic adjustment mechanism and updating reporting when the gift tax statute of limitations period ends, as discussed above, is even more important.
- A theme of several recent cases is that when taxpayers respect formalities, their transactions may succeed, and when they do not, their plans will likely fail. These cases are a good reminder of the importance of observing formalities.

Related Party Transactions Subject to Increased Scrutiny

- "Transactions between persons in a close family group, whether or not involving partnership interests, afford much opportunity for deception and should be subject to close scrutiny." Kuney v. Frank, 308 F.2d 719, 721 (9th Cir. 1962)." (quoting H.R. Rept. No. 82-586, at 33 (1951), 1951-2 C.B. 357, 381)).
- "A transaction between family members is * * * subjected to heightened scrutiny to ensure that it is not a sham or disguised gift." Estate of Bongard v. Commissioner, 124 T.C. 95, 119 (2005).
- Cases Remind us to Observe Form of Transactions
- There have been several recent important decisions out of the United States Tax Court, Levine Est. v. Comr., 158 T.C. No. 2 (February 28, 2022), a taxpayer victory in an intergenerational family split-dollar estate tax case, and Smaldino v. Comr., T.C. Memo. 2021-127 (November 10, 2021), a taxpayer loss in an indirect gift case. Most recently the Sorensen v. Commissioner, Tax Ct. Dkt. Nos. 24797-18, 24798-18, 20284-19, 20285-19 (decision entered Aug. 22, 2022) highlighted the importance of proper documentation and implementation of planning.
- While both cases present a plethora of substantive law issues worthy of our discussion, today, we're going to focus instead on the rich lessons for estate planning professionals of all stripes.
- Understanding what was done right or wrong provides valuable guidance on how to better structure and implement estate plans.

Smaldino v. Comr., T.C. Memo. 2021-127 (November 10, 2021)

- From a planning perspective, the IRS and the Tax Court recast a gift by husband to wife and then almost immediately by wife to an irrevocable trust for the benefit of the husband's descendants (who were not descendants of the donor wife in their blended family) as a gift by the husband/father to a trust for the benefit of his descendants. The wife was viewed as a mere conduit for the husband's gift transfer.
- Mr. Smaldino "purportedly" transferred about 41% of LLC membership interests in a family real estate business to his wife on April 14, 2013. Mrs. Smaldino "purportedly" then gifted those same interests to a dynasty trust the very next day. The Tax Court had little difficulty recharacterizing the claimed gift Mr. Smaldino made to Mrs. Smaldino, followed by her gift to the dynasty trust, as if Mr. Smaldino himself had made the gift directly to the trust. Mrs. Smaldino held the interests possibly only for a day.
- She transferred the same exact interests she received from her husband as a gift to her, as her gift to the Dynasty Trust, and the family and their advisers skipped numerous steps that should have been followed to corroborate that they respected the transaction. Avoid circular transactions where identical assets, interests or values.
- Issues with the above plan also include that Mrs. Smaldino only held the interests in the LLC for one day. But that one day ownership was not respected by the Smaldino's. The transfers did not follow the requirements of the operating agreement. Adhering to the formalities of the operating agreement restrictions would not have taken much effort, Mr. Smaldino as trustee of the trust, and as manager of the LLC, could have easily given written consent for the admission of Mrs. Smaldino as a member, showing adherence to the formalities required by the operating agreement of the entity.
- Further disregard was evidenced in the tax reporting. On the Schedules K-1, Partner's Share of Income, Deductions, Credits, etc., attached to the Form 1065, the LLC listed Mr. Smaldino as a 51% partner, and the dynasty trust as a 49% partner for the entire tax year. Mrs. Smaldino was not listed as a partner for any part of the tax year. Thus, the income tax returns did not reflect a partial year ownership (1 day) for Mrs. Smaldino, which was contradictory to the position the taxpayers' tried to argue.
- The gift by Mr. Smaldino to Mrs. Smaldino didn't have to be included on the gift tax return. IRC Sec. 6019(2). But should it have been notwithstanding IRC Sec. 6019(2)? Notwithstanding IRC Sec. 6019(2), practitioners might consider disclosing all spousal gifts on the Form 709.

Levine Est. V. Comr., 158 T.C. No. 2 (February 28, 2022

- This Tax Court case decision provided a resounding victory (at least for now) to the taxpayer who had pursued what some might view as an aggressive split-dollar life insurance plan to minimize estate taxes. The following comments will not address the split-dollar issues the case is known for, but rather the general lessons that can be gleaned from the case about better planning that is more likely to succeed.
- The Levine Est. court noted "estate planners as skilled as the ones the family retained." The Levine Court seems impressed throughout the opinion with the professionalism of how matters were handled. The Court noted positively how the estate planner analyzed the pros, cons and implications of the planning for the client, even preparing a PowerPoint presentation to explain the plan to her. Perhaps practitioners should educate clients that preparing a memorandum explaining the transactions planned may not only help the client understand better but might help the transaction succeed.
- Fiduciary duty is an important factor in the Court's analysis in Levine Est., as it was to the United States Supreme Court in Byrum v. U.S., 408 U.S. 125 (1972). The Insurance director/trustee (under the title of Investment Committee) had a fiduciary obligation to the beneficiaries to make reasonable decisions. Is this a Byrum type of argument? The Court noted above the independence of the person named (he was not family), and his business and financial acumen. The Court also noted positively the naming of an institutional trustee, South Dakota Trust Company as general trustee. Practitioners should inform clients that insist on naming family trustees, usually out of concern for paying trustee fees, that having truly independent trustees, and corporate trustees, may well help their plan succeed.

Sorensen v. Commissioner, Tax Ct. Dkt. Nos. 24797-18, 24798-18, 20284-19, 20285-19

- The donors relinquished dominion and control of all the shares in 2014 so that the gift of the full amount of shares, not the $5 million worth of shares contemplated under the Wandry fixed dollar transfer. Similar to the Smaldino case above, the taxpayers failed to respect the formalities of the transaction they created, so that the IRS and then the Court did not respect it either.
- The reporting by the entity did not comport with the purported defined value transfer. The company reported that each trust owned 9,385 shares on its stock ledgers and on income tax returns instead of the fixed dollar value that was intended to be transferred. The stock ledger and tax returns should have included an "asterisk" referencing an explanation of the intended transaction. Practitioners might provide clients, the entities and trustees, with recommended language to the effect that $5 million of shares were transferred.
- In Sorensen, the trusts received pro rata distributions based on the ownership of estimated number of 9,385 shares. Distributions should be based on the initially determined amount of shares, which could be adjusted to be based on finally determined gift tax values.
- The transferors and their trusts would make appropriate adjustments between themselves if the shares were changed. Incorporate into the transfer documents an economic adjustment mechanism to assure that if there is a gift tax valuation adjustment the economics of the transaction are properly adjusted as between the parties and charge a CPA with this task. See the discussion above of an economic adjustment clause.
- In Sorensen, the IRS argued that the defined value mechanism should not be respected as there was no agreement with the recipient trust as to the adjustment for prior distributions or on the later sale of shares to acknowledge the supposed existence of a defined value mechanism. The trusts have agreed to transfer shares in accordance with the defined value formula, and should have countersigned the stock powers, which should have described the transfers as defined value formula transfers. The trusts should have countersigned the stock powers to specifically acknowledge the conditions under which they were receiving the stock transfers.
- A preferable approach might be to not have the equity interests pass to the donee trust in the case of a gift (or purchasing trusts in the case of a note sale) but rather be held in escrow with an independent escrow agent pending resolution of the contingency of the gift tax value as finally determined. The use of an escrow arrangement was not suggested in the case and may exceed what commentators of the case have recommended, but it would introduce a higher level of respect for the transaction.
- Be certain that every record of the transaction reports it in a manner consistent with the actual valuation adjustment mechanism used. Adhering to formalities in all transactions is vital to enhancing the likelihood of success.

Gift Tax and Gift Tax Returns

ADEQUATE DISCLOSURE AND MORE

GST Waterfall

- GST Allocation between Trusts. When GST is allocated to two or more trusts, if the GST exemption can potentially be exhausted, we recommend attaching an affirmative statement of how GST will be allocated between the various trusts. Suggested language is as follows:
  - In the event that the value of any assets transferred by the Taxpayer to the Trusts reported on Schedule A, Part 3 as referenced below is re-determined for federal gift tax purposes, the formula allocation of the Taxpayer's GST exemption should be allocated in the following order:
    - The smallest amount of the Taxpayer's GST exemption shall be allocated to the value of the assets as finally determined for federal gift tax purposes to have been so transferred to the Trustname as may be necessary to produce an inclusion ratio for GST purposes, as defined in the Internal Revenue Code Section 2642(a), which is closest to, or if possible, equal to zero.

GST Waterfall

- To the extent that the Taxpayer has any GST exemption then remaining after the specific allocation of GST exemption as set forth in 1 above, the Taxpayer directs that the smallest amount of the Taxpayer's GST exemption shall be allocated to the value of the assets as finally determined for federal gift tax purposes to have been so transferred to the Trust2name as may be necessary to produce an inclusion ratio for GST purposes, as defined in the Internal Revenue Code Section 2642(a), which is closest to, or if possible, equal to zero.
- To the extent that the Taxpayer has any GST exemption remaining after the specific allocation of GST exemption as set forth in 1 and 2 above, the Taxpayer directs that the smallest amount of the Taxpayer's GST exemption shall be allocated to the value of the assets as finally determined for federal gift tax purposes to have been so transferred to the Trust3name as may be necessary to produce an inclusion ratio for GST purposes, as defined in the Internal Revenue Code Section 2642(a), which is closest to, or if possible, equal to zero.
- Add additional entries as needed to account for each GST allocation.

Do Annual Gifts Still Make Sense?

- While classic estate planning advice is to consider annual exclusion gifting, for many it may not make sense. The exclusion amount is $18,000 in 2024, increasing to $19,000 in 2025, per person per year tax. In addition, a donor can pay donee's health and education expenses if paid directly to the provider. It is also permitted to accelerate gifts by making 5-years worth of 529 gifts.
- Do annual exclusion gifts really make sense for most taxpayers given the high exemption? Might it be better to make one larger gift and forgo future annual gifts? Perhaps taxpayers should revisit whether or not to continue annual gifts to trusts as for many it may not be optimal.
- The recent proposal to Save Social Security by Taxing Dynastic Wealth might suggests including annual demand or Crummey powers in any trust for which it is feasible in case the gift exclusion is in fact reduced to a mere $1 million.

IRA – Using a NIMRCUT

INCOME TAX SAVINGS POSSIBLE BUT IT IS COMPLEX AND COSTLY

IRA Paid to NIMCRUT: The Tax Deferral Can be Valuable

- Which Clients are Potential Candidates for a IRA/NIMCRUT/LLC Approach?
- The IRA owner is willing to incur the cost and endure the complexity of this Plan bearing in mind that the Plan owner will have no benefit from the approach, only the heirs of the Plan owner.
- Costs will include professional fees, the .1% of the LLC that may be given away, and the remainder interest to charity.
- IRA assets have to be valuable enough to warrant the costs of creating a NIMCRUT, the LLC, and administering the complexity of the plan.
- The heirs who will be named non-charitable beneficiaries of the IRA/NIMCRUT have to be able to forgo any distributions for 20-years to maximize the wealth accumulation that the approach might provide.
- The heirs will have to incur the costs and endure the complexity of the administration of the approach.
- The IRA owner and her heirs will have to accept the risk of the plan. These risks might include:
  - The failure to properly operate the plan.
  - A challenge by the IRS that the underlying LLC should not be respected as a blocker of FAI. If the same non-charitable beneficiaries control the .1% and are managers of the LLC, or directly or indirectly can control the LLC, or if the person who does control the LLC acts as the alter-ego of the non-charitable beneficiaries, the approach may implode.
  - The non-charitable beneficiaries have to be willing to stick with the terms of the approach and not receive withdrawal potentially for two decades.

Steps in IRA-NIMCRUT Plan

- Acknowledgements to Jonathan G. Blattmachr, Esq. for the IRA/NIMCRUT idea. The following slides are based on an article we have in process.
- Create a NIMCRUT during lifetime but make it revocable. The trust instrument would not require any special tailoring as compared to any other NIMCRUT.
- Form an LLC to be owned 99.9% by the NIMCRUT and .1% by the person who will be the manager of the LLC. On account of Rev. Proc. 97-23, the manager should not be the trustee or a beneficiary of the CRT or anyone related or subordinate to either of them. This could be the attorney or CPA for the client, or an independent corporate fiduciary such as a bank.
- Name the LLC as a beneficiary of the Plan. You do not name the NIMCRUT as the beneficiary, as the NIMCRUT owns 99.9% of the LLC.
- On death of the IRA owner, the IRA assets pass to the LLC by the beneficiary designation and the income from the IRA will be attributed to the NIMCRUT which will report the income but pay no income tax because it is income tax exempt. The NIMCRUT will have no FAI to distribute to its beneficiaries. Since all income on the IRA is triggered at this time the NIMCRUT will have realized 99.9% of the value of the IRA as taxable income, but none of that will be subject to income tax by reason of the income tax exemption of the CRT.
- In any year in which the LLC does not make an actual cash distribution to the NIMCRUT, the NIMCRUT will have no FAI, the NIMCRUT will not have to make a distribution to the non-charitable beneficiaries, and any tax on the income realized on the NIMCRUTs receipt of the Plan assets, will continue to be deferred.
- If the non-charitable beneficiaries needed or wanted distributions the LLC could distribute FAI to the NIMCRUT. Properly structured that distribution would be FAI and then that amount would have to be distributed to the non-charitable beneficiaries. They would then realize income tax, based on the four tier tax system of CRTs. Thus, ordinary income would be deemed distributed first. Since the full value of the IRA would be deemed ordinary income in the year of the Plan owner's death, there would almost assuredly be a substantial amount of ordinary income for each distribution. Capital gain income could only be realized by the non-charitable beneficiaries of the NIMCRUT after the income of the entire value of the Plan on the Plan owner's death were distributed to them.
- At the end of the 20th year of the NIMCRUT all assets would have to be distributed and all income recognized. That is the maximum deferral period.
- Note that this would "buy" generally speaking an additional ten years of deferral versus merely accepting the 10-year payout of the Plan under general post-SECURE Act rules. Recognize that the Proposed Regulations that clarified that RMDs must be paid during the intervening ten years before the final payout could provide a further advantage to the IRA/NIMCRUT approach as that could be avoided.
- Caution: Rev. Proc. 97-23 does not prohibit having a CRT own an LLC but provides the IRS may not rule favorably on the CRT status of the trust if the grantor, trustee, or beneficiary, or anyone related or subordinate to one of them is the manager of the LLC owned 99.9% by the NIMCRUT.

Hart-Scott Rodino

TRAP FOR THE UNWARY

Consider Hart-Scott Rodino Filings with FTC

- On any large transaction of perhaps $100M and above confer with FTC counsel as to whether a filing requirement may be triggered. This is can be overlooked and the penalties can be tremendous $50,000+ per day and if willful $100M and 1 year in jail.
- The threshold is inflation adjusted and is now about $126 million but be careful.

What is the Applicable Definition of Value?

- Valuation definitions may differ for 409A, FTC filings, gift tax, and 368/482 income tax purposes.
- Be careful.

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- For more information see:
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Contact Information

We welcome your comments, suggestions and inquiries