What the CPA Should Know About Trusts & Estates

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Agenda

- Introduction
- Legal Principles & Definitions
- Types of Trusts
- Trust Accounting Concepts
- Important Trust Clauses

Introduction

Introduction

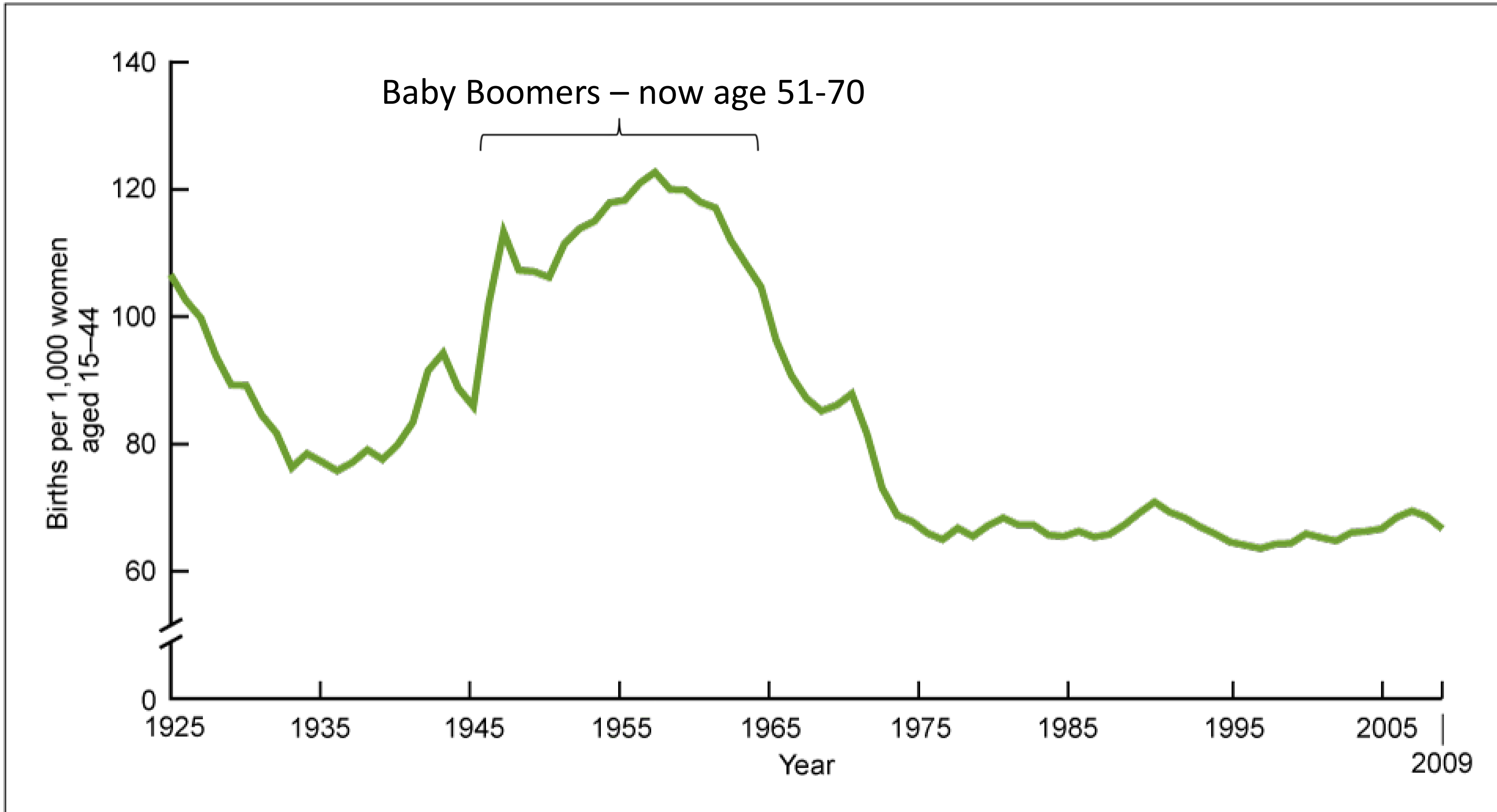
- Trust Accounting Challenges
  - Completely separate practice area from personal or business accounting
  - More “grey area” than personal or business accounting
  - Rules are dependent on state law, in addition to federal law, which causes many variations and complications
  - What’s permissible is also dependent on the trust document

Introduction

- Why Learn About Trusts & Estates
  - Over the next 30 years, the baby boomers will transfer their wealth to the next generation
  - CPAs will have a role in preparing accountings, filing returns, and developing quantitative estate planning strategies

Introduction

Figure 1. Fertility rate: United States, 1925–2009



NOTES: Data for 2009 are preliminary. Access data table for Figure 1 at: http:/www.cdc.gov/nchs/data/databriefs/db60_tables.pdf#1.

SOURCE: CDC/NCHS, National Vital Statistics System.

Legal Principles & Definitions

Legal Principles & Definitions

- Core Estate Planning Documents:
  - Power of Attorney over Financial Affairs
  - Power of Attorney over Healthcare
  - Healthcare Directive (living will)
  - Will
  - Revocable Trust

Legal Principles & Definitions

- General Definitions:
  - *Probate* – legal process of administering the estate of a deceased person; involves resolving claims against the estate (including paying taxes) and distributing assets
  - *Will* – an instrument a person uses to direct the distribution property after their death
  - *Executor* – person directed to carry out the directions of a will (aka executrix or personal representative)

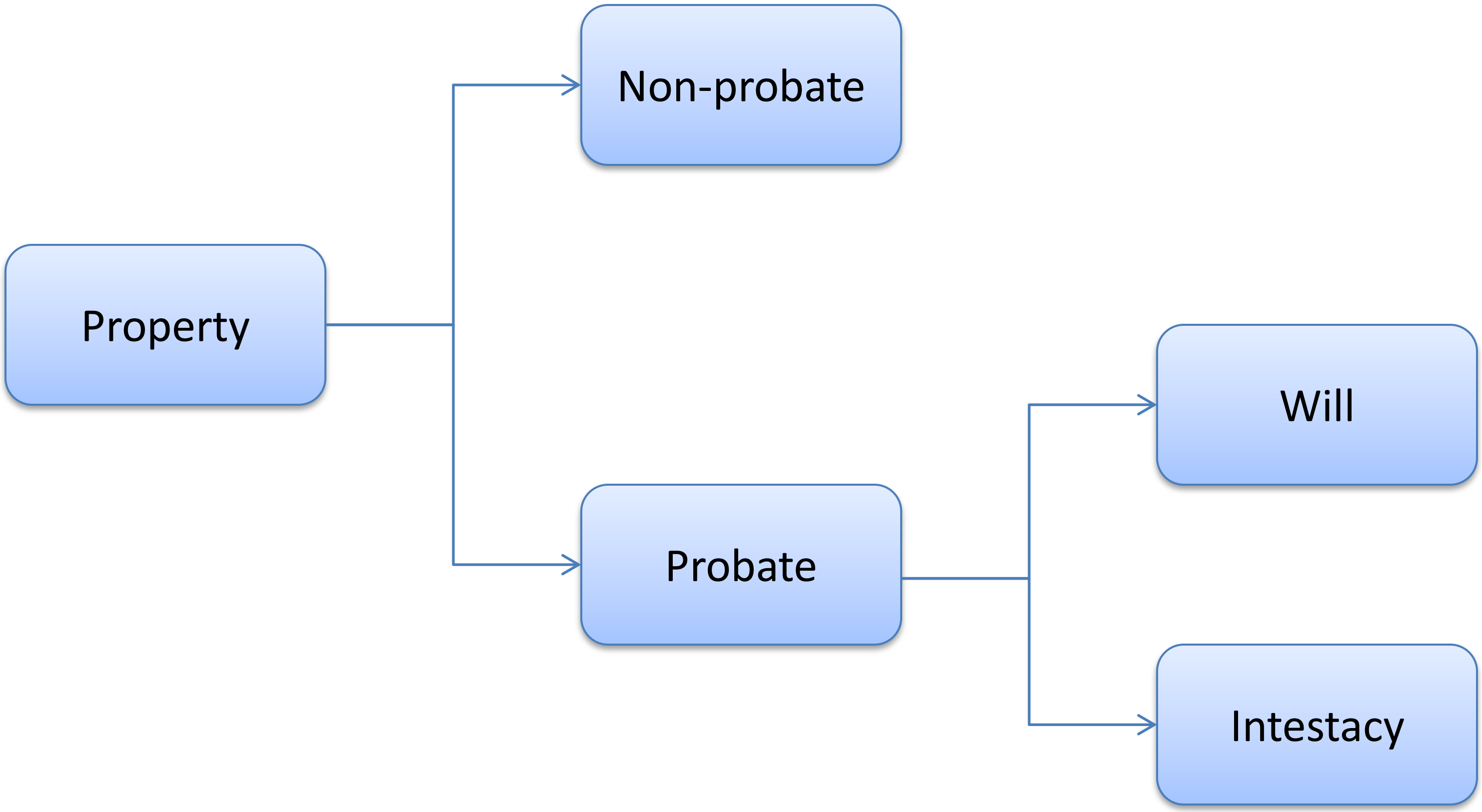
Legal Principles & Definitions

- Probate:
  - Transfers assets belonging to deceased persons
  - Administered by a court
  - Collects and marshals assets, satisfies creditors, resolves conflicts, and distributes the estate
  - Fail-safe system to shift property to from a decedent to another

Legal Principles & Definitions

- Why people avoid probate:
  - It's slow – can be less than six months, but its not unheard of for it to take several years
  - It's expensive – executor fees, attorneys' fees, court costs, appraisal fees; 2%-10% of the estate can easily be expended
  - It's public – debts, assets, and distributions are in the public record for anyone to lookup

Legal Principles & Definitions



Legal Principles & Definitions

- People avoid probate with the following mechanisms:
  - Transferring assets into trust (revocable or irrevocable)
  - Re-titling property so its held in a joint tenancy with the right of survivorship (JTWROS) or tenancy by the entirety
  - Transfer on death (TOD) accounts & deeds
  - Payable on death (POD) accounts
  - Life Estates
  - Joint accounts
  - Beneficiary designation forms

Legal Principles & Definitions

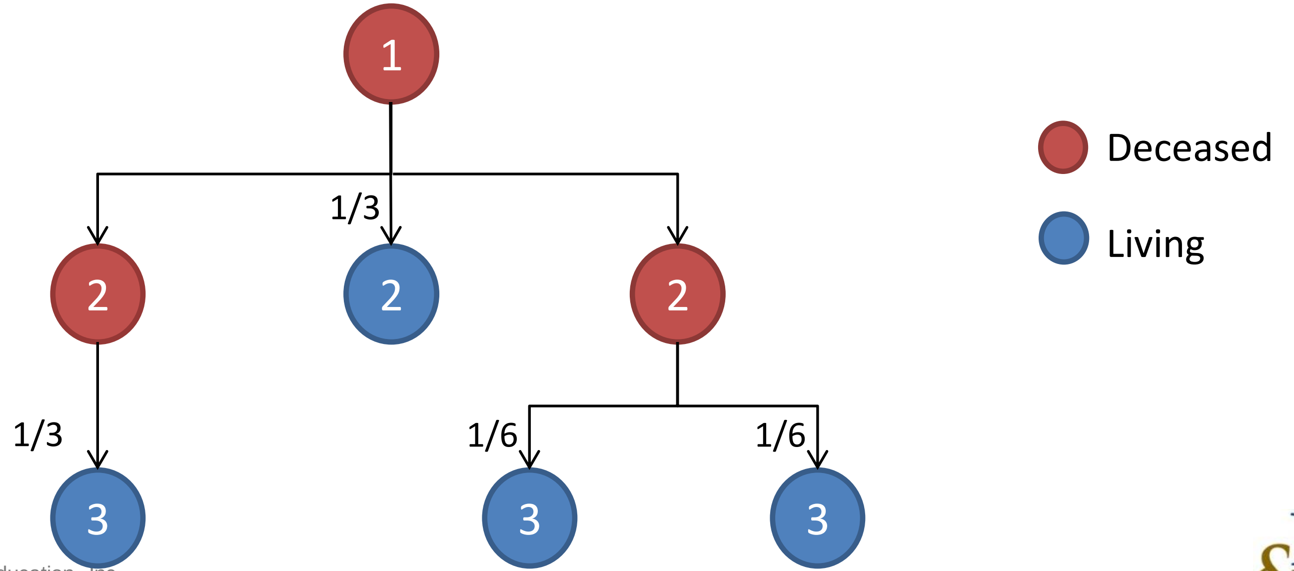
- General Definitions:
  - *Intestacy* – the condition of an estate of a person who dies without a will
  - *Intestacy laws* – state law which define the rules of inheritance for someone who dies without a will
  - *Escheat* – transfers property of someone who dies without a will or heirs to the state
  - *Heir* – a person who receives property under the intestate statute
  - *Issue* – descendants, such as children and grandchildren
  - *Ascendants* – ancestors, such as parents and grandparents

Legal Principles & Definitions

- General Definitions:
  - *Life Estate* – ownership interest in property (typically real property) that terminates at the death of the holder of the interest
  - *Remainderman* – person who is entitled to an interest in property upon termination of another's interest in the property (typically at the end of a life estate; also a second taker in a will)

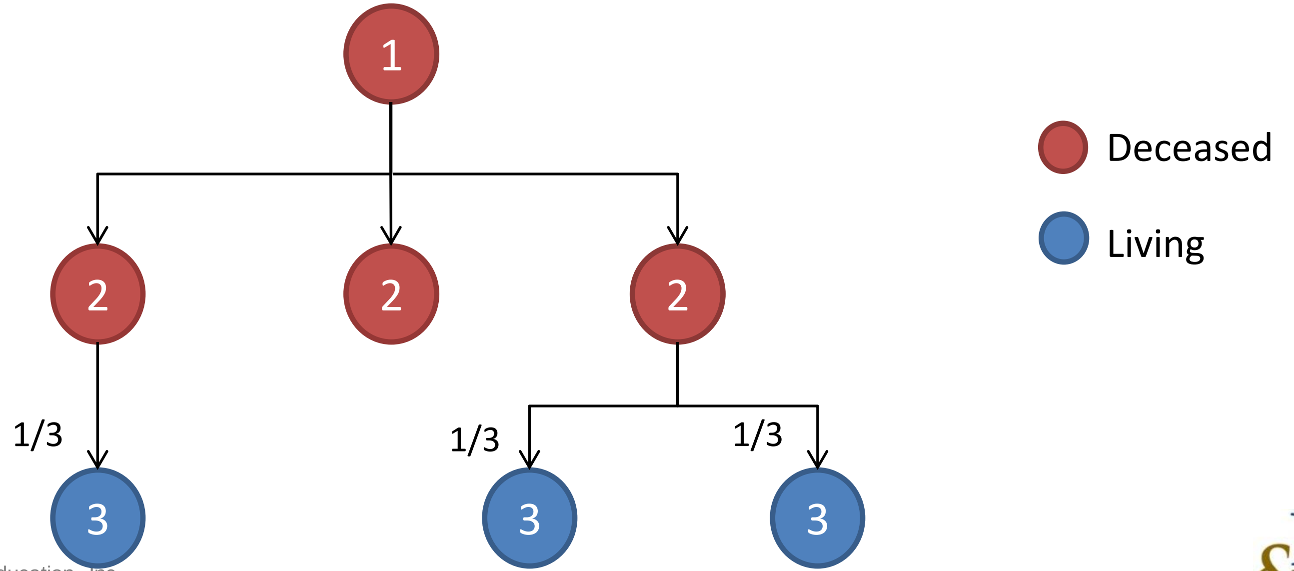
Legal Principles & Definitions

- Definitions regarding distribution:
  - *Strict Per Stripes* – each branch of the family receives an equal share



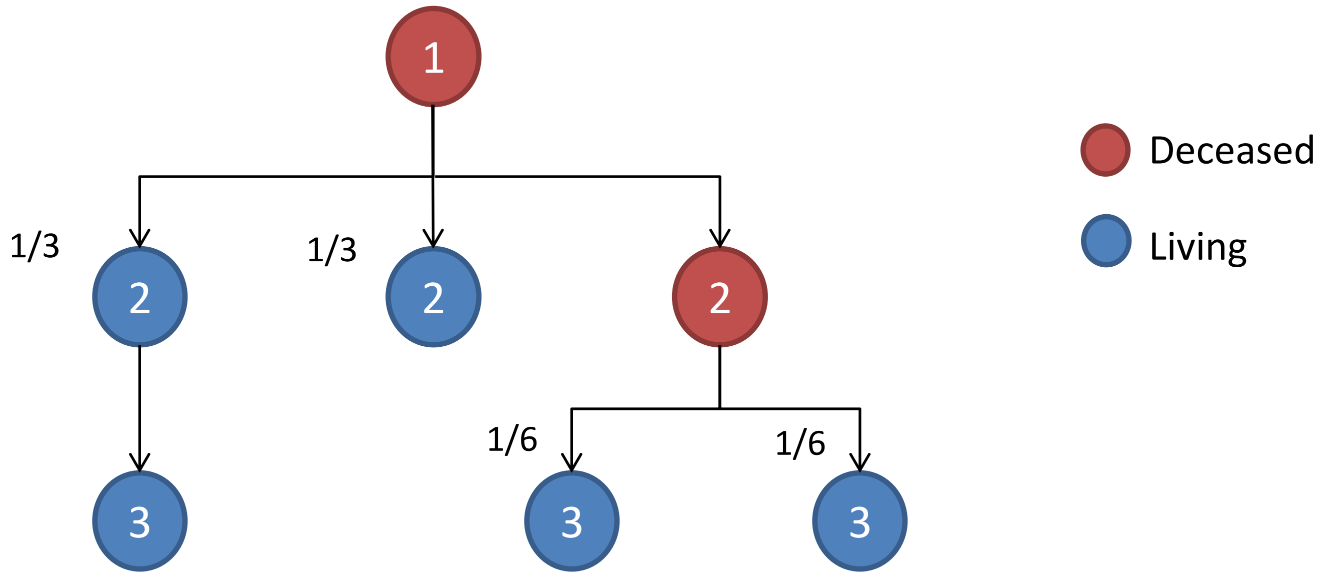
Legal Principles & Definitions

- Definitions regarding distribution:
  - *Modified Per Stripes* – modifies per stripes by providing that all descendants of the same generation receive an equal share



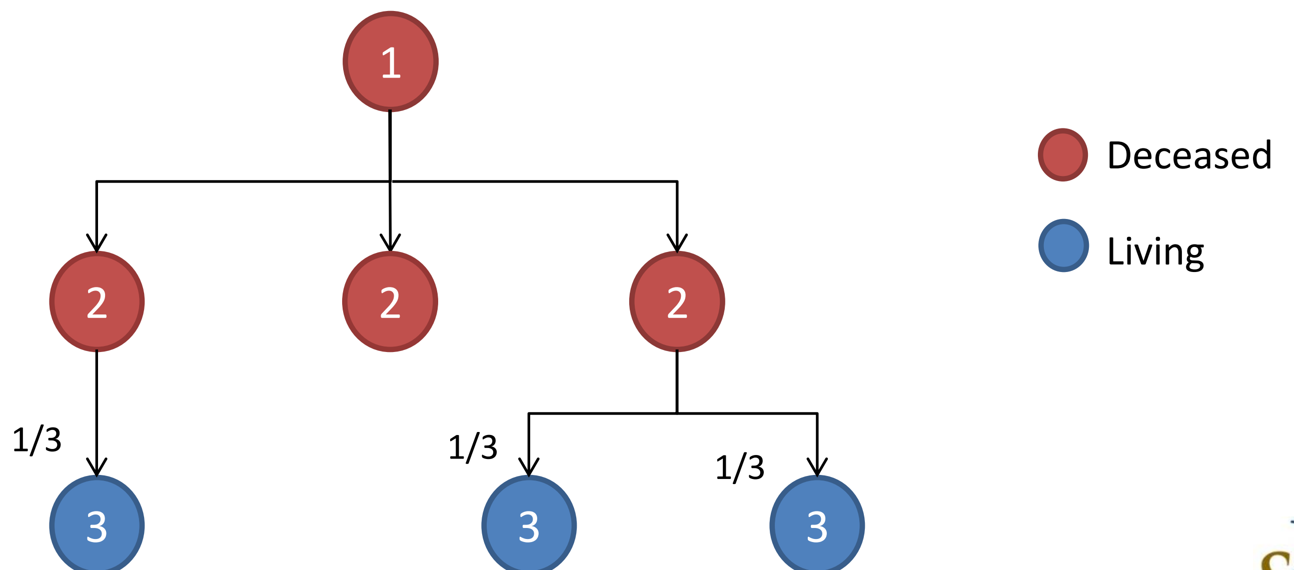
Legal Principles & Definitions

– *Per Capita by Representation* – splits the number of shares equal to the number of descendants in the first surviving generation



Legal Principles & Definitions

- Definitions regarding distribution:
  - *Per Capita by Representation*
    - Now consider if none of the children survive



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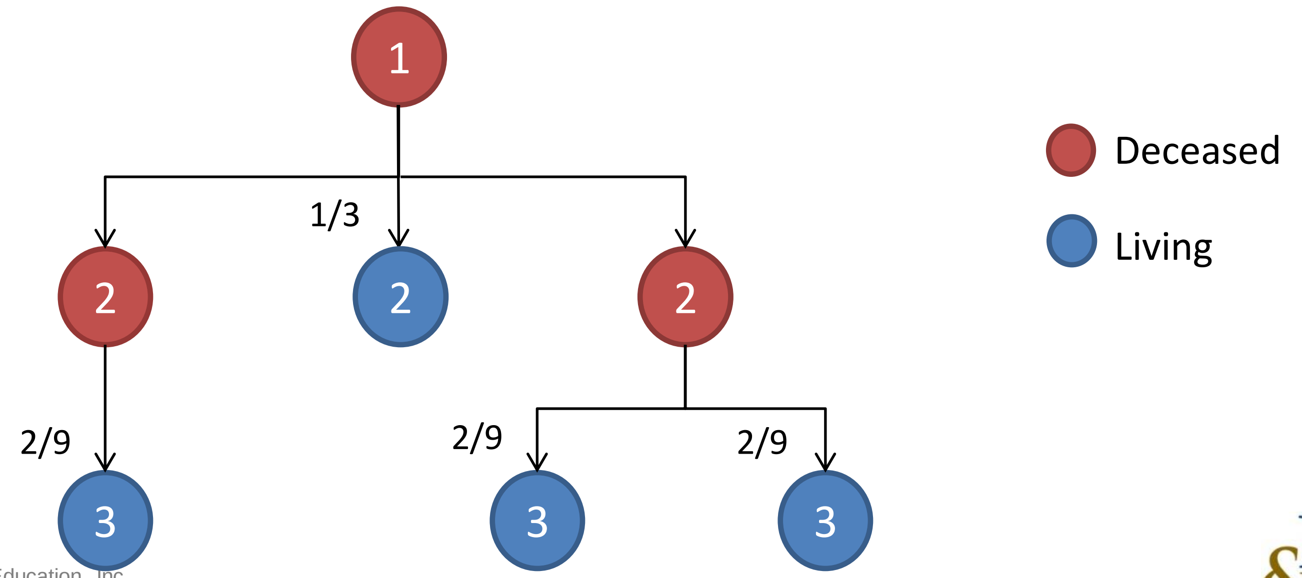
Legal Principles & Definitions

- Definitions regarding distribution:
  - *Per Capita at Each Generation*
    - Changes the per capital by representation definition to create equal shares for each following generation



Legal Principles & Definitions

- General Definitions:
  - *Bequest* – gift by will of personal property;
  - *Legacy* – gift by will of personal property;
  - *Devise* – gift by will of real property;
  - *Legatee* – a person to whom a legacy is given

Legal Principles & Definitions

- General Definitions:
  - *Specific Bequest* – gift of all property of a certain class or kind
    - "I leave all my sports memorabilia to Bobby"
  - *Pecuniary Bequest* – gift denominated in money rather than by property
    - "I leave $1,000 to Bobby"

Legal Principles & Definitions

- General Definitions:
  - *Residuary Bequest* – gift of the remainder of the testator's estate
    - "I leave all my sports memorabilia to Bobby and <u>everything else to my wife</u>"
    - "I leave $1,000 to Bobby and <u>everything else to my wife</u>"

Legal Principles & Definitions

- General Definitions:
  - *Executory Bequest* – gift of a future, deferred or contingent bequest
    - “I leave $1,000 to Bobby <u>if he is age 25 or older at my death</u>”
  - *Conditional Bequest* – a gift which takes effect if a certain event occurs or does not
    - “I leave all my sports memorabilia to Bobby <u>if he is under 25 at my death</u>”

Legal Principles & Definitions

- Formula Bequests / Dispositions:
  - *Pecuniary* – gift denominated in money rather than by property; often uses formula where the amount of the gift equals a certain amount (such the estate tax exemption amount)
    - "I leave the maximum amount which will result in no estate tax to the Family Trust and the residue to the Marital Trust."
    - Pecuniary bequests are treated as a sale or exchange of the asset distributed and causes a recognition event for the estate. *Kenan v. Comm*, 114 F.2d 217 (2d Cir. 1940); Rev. Proc. 64-19.

Legal Principles & Definitions

- Formula Bequests / Dispositions:
  - *Fractional* – gift by a formula which splits property by value between two takers
    - "I leave to my spouse the residue of my estate multiplied by fraction with a numerator equal to smallest amount which will result in no estate tax and the denominator equal to the entire value of the residue."
    - Gain or loss is not recognized upon the distribution of property to satisfy a fractional disposition.

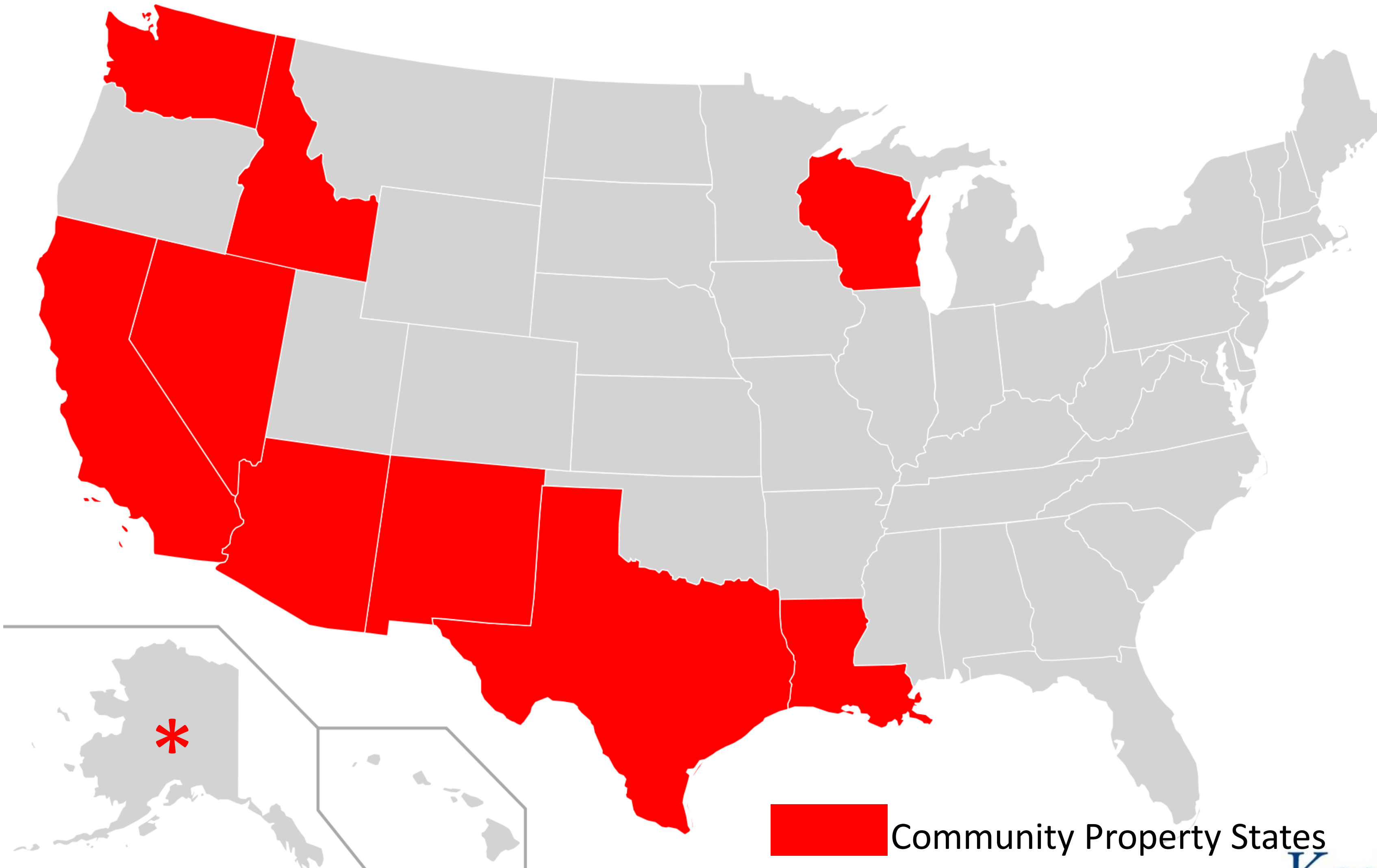
Legal Principles & Definitions

- Ownership Rights of Spouses
  - Community Property States
    - Based on the premise that husband and wife are in partnership and should share accordingly
    - Property acquired during the marriage is pooled and equally shared;
    - Unclassified property is generally presumed to be marital property
    - Property acquired before the marriage or by gift or inheritance generally remains separate property

Legal Principles & Definitions

- Ownership Rights of Spouses
  - Common Law States
    - Ownership generally determined by legal title
    - Property acquired during the marriage generally remains the property of the person who acquired it
    - Gifts and jointly held property are common

Legal Principles & Definitions



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Legal Principles & Definitions

- Rule Against Perpetuities (RAP)
  - General Rule: Interest is valid if it actually vests either within a life or lives in being plus 21 years or within 90 years
  - Prevents perpetual unalienable ownership of property
  - Varies substantially by state:
    - Some have the general rule
    - Some have no rule
    - Some have an extremely long period – 300 years +
    - Some provide the ability to elect out of the rule

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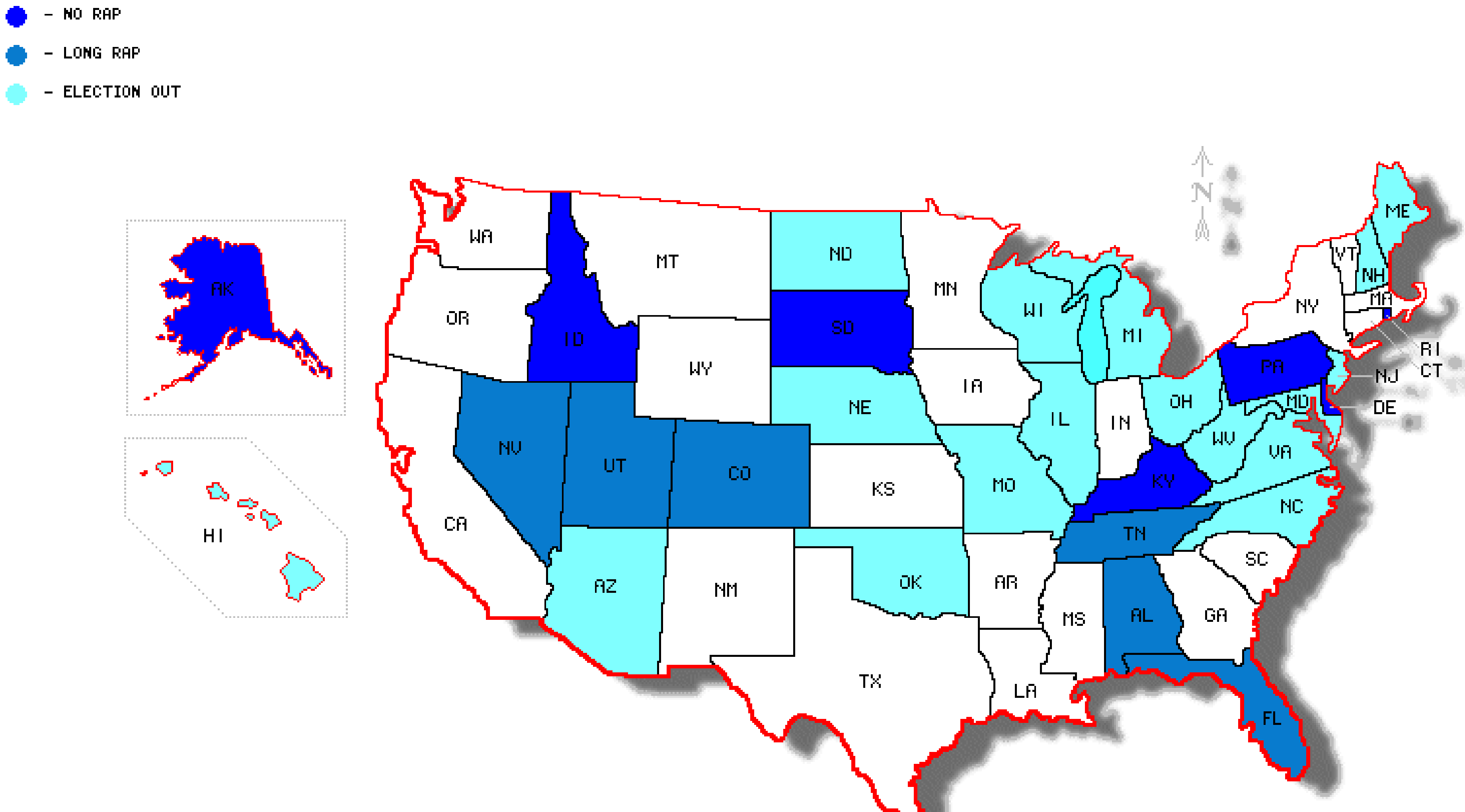
Legal Principles & Definitions

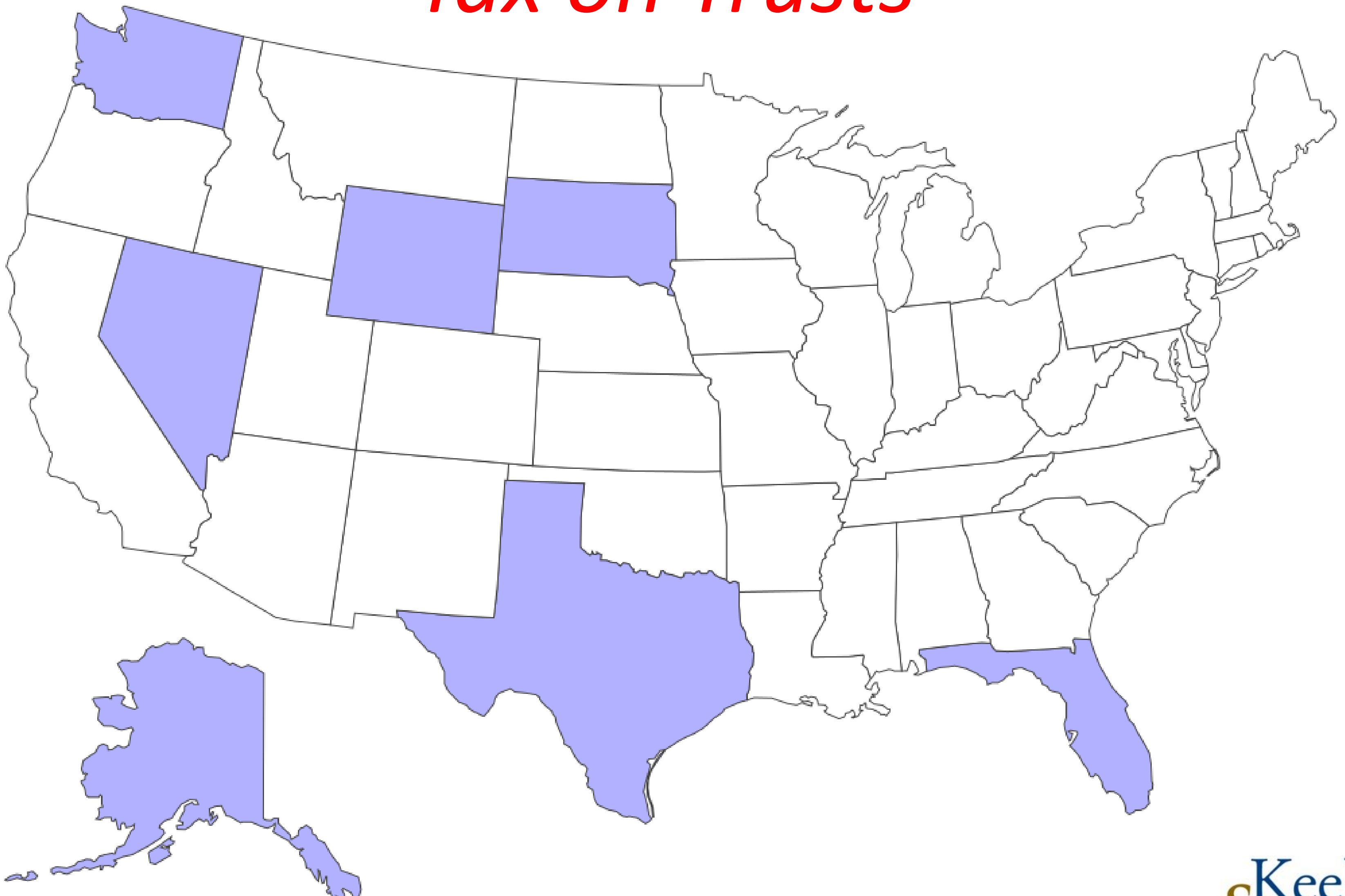


Map largely based on Attorney Howard Zaritsky's 50 State Survey of the Rule Against Perpetuities published by ACTEC; refer to Mr. Zaritsky's original work for further clarification; the map is merely meant to illustrate the substantial differences between jurisdictions, it omits many details and may be out of date. Any error is not attributable to Mr. Zaritsky.

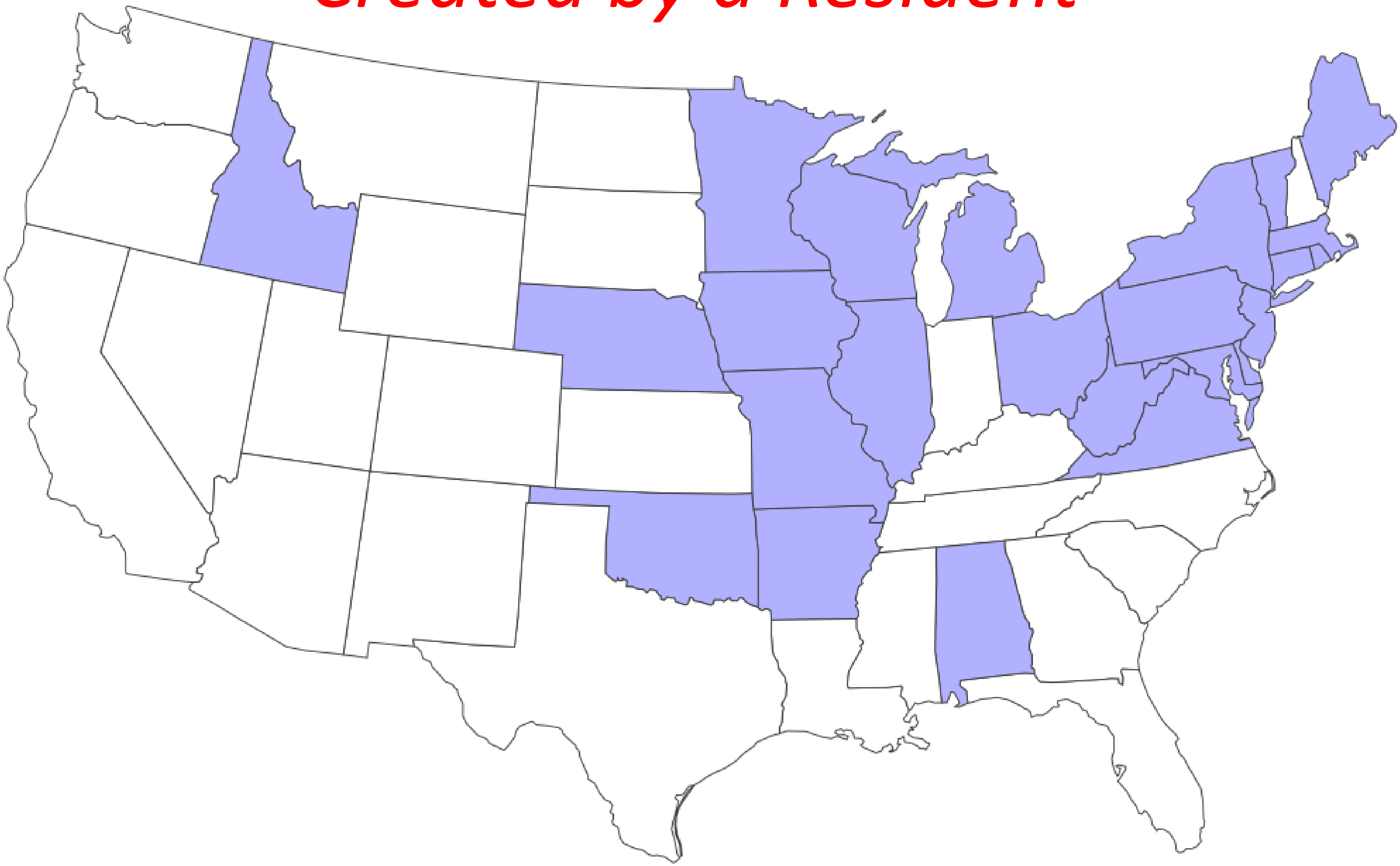
Legal Principles & Definitions

- State Income Taxation of Trusts
  - Justifications (i.e. reasons) states assert to tax the income generated by assets held in trust are as follows:
    - If the trust was created by the will of a resident
    - If the trust was created by a living resident
    - If the trust is administered in the state
    - If the trustee is a resident of the state
    - If a non-contingent beneficiary is a resident of the state

States Which Do Not Impose Income Tax on Trusts



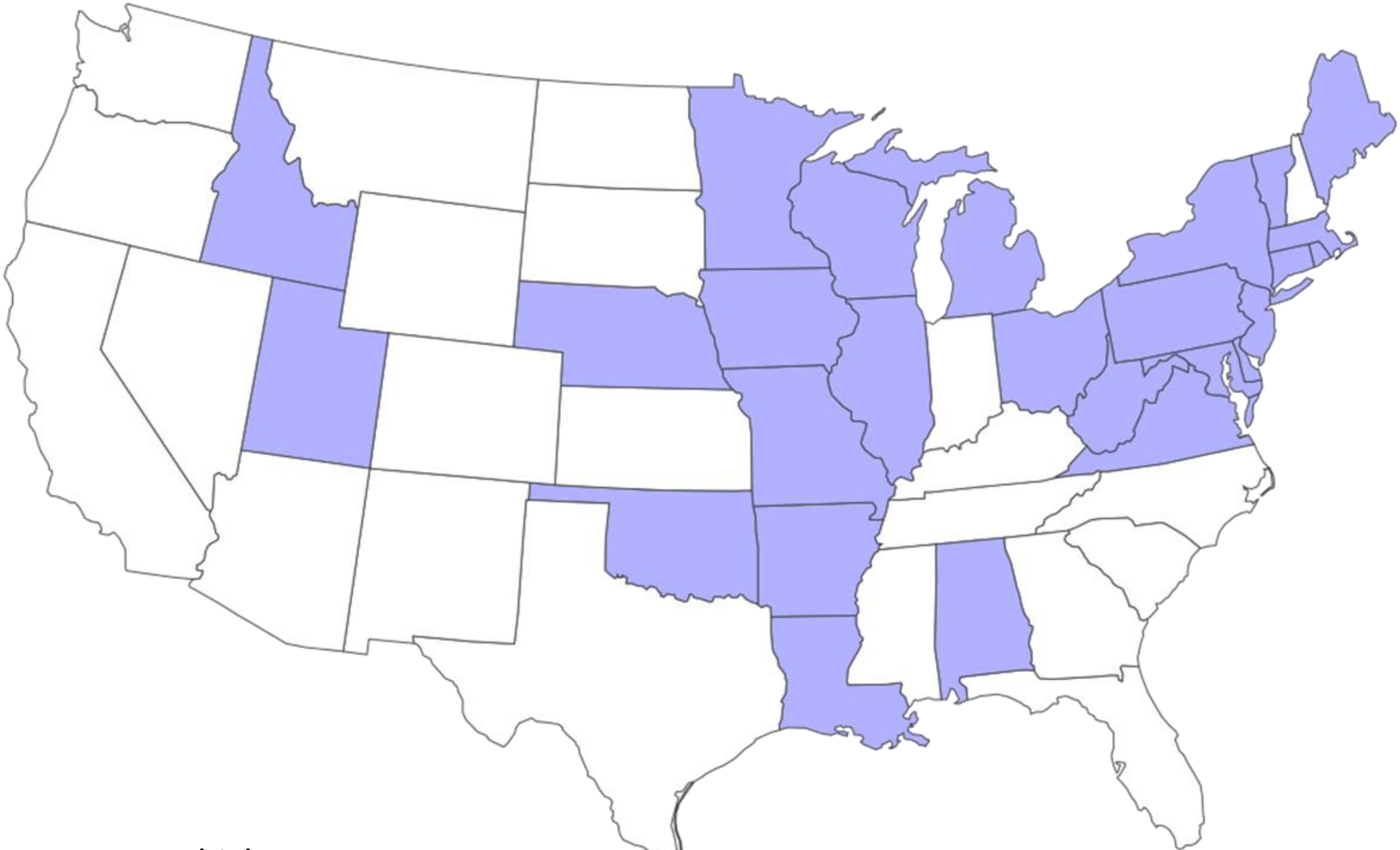
Inter Vivos Trust Created by a Resident



States which tax such trusts

Map based on the 2013 work of *Richard W. Nenno of the Wilmington Trust Company.*

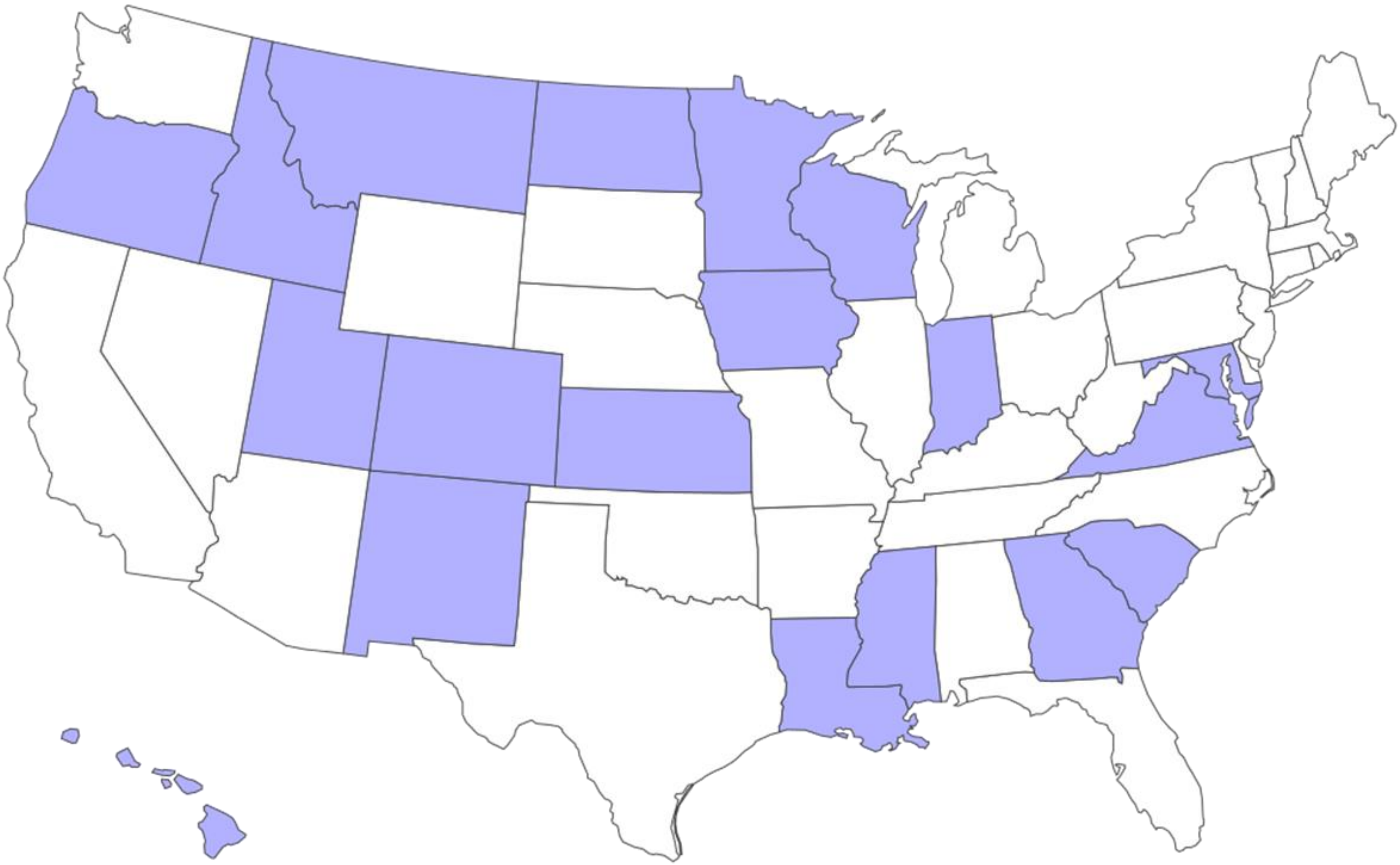
Trust Created By Will of Resident



States which tax such trusts

Map based on the 2013 work of *Richard W. Nenno of the Wilmington Trust Company.*

Trust Administered in State



States which tax such trusts

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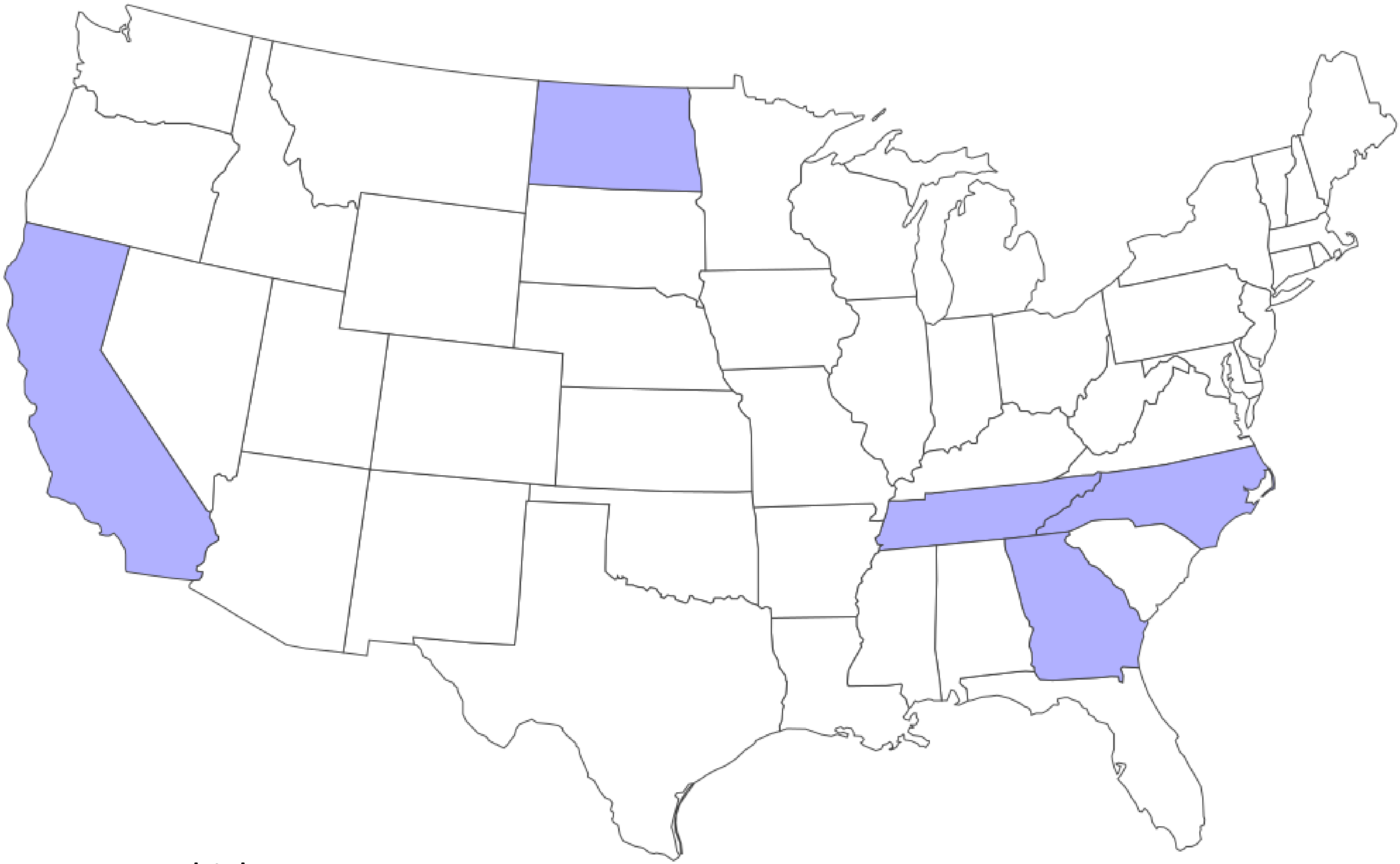
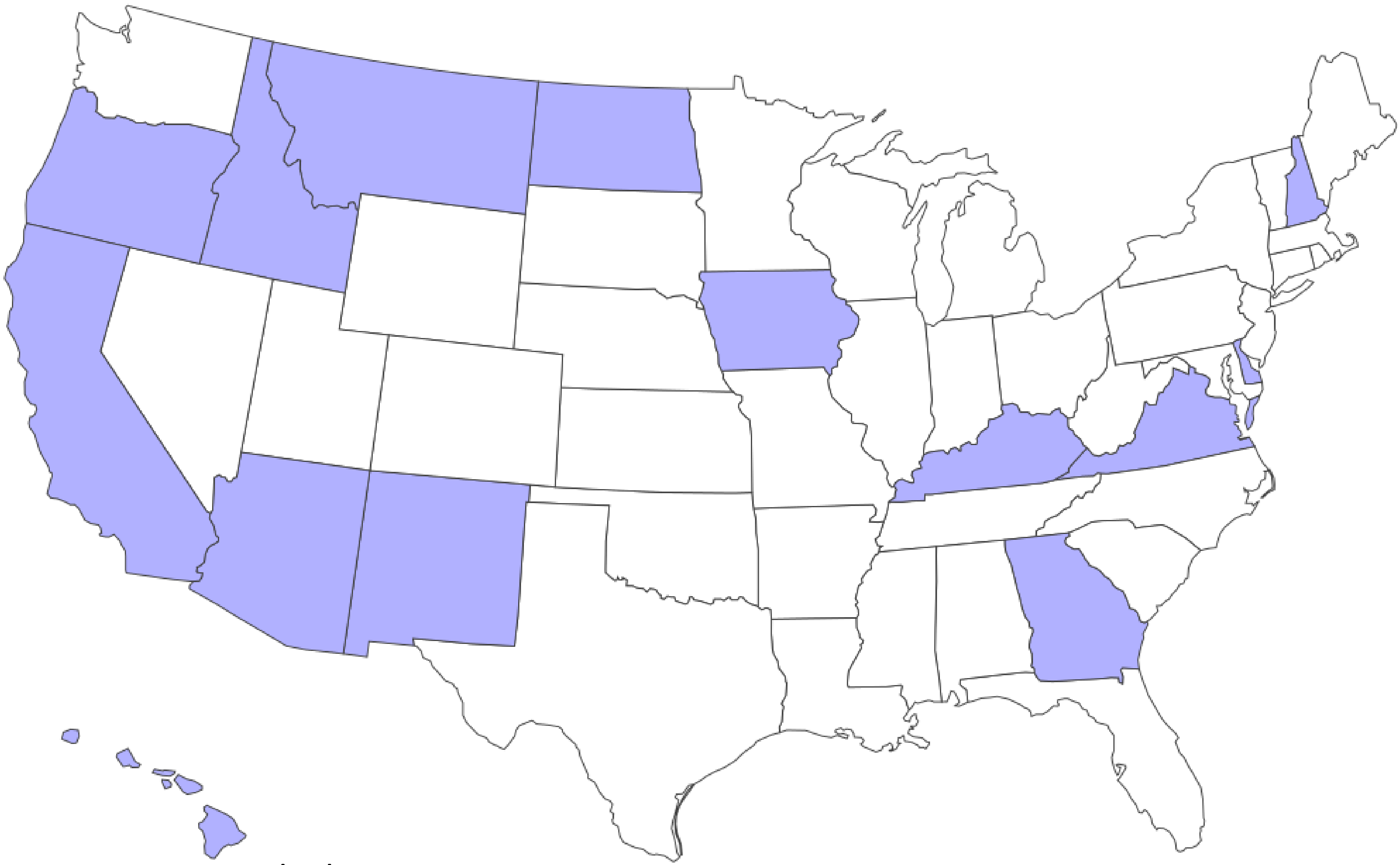
Resident Non-contingent Beneficiary



States which tax such trusts

Map based on the 2013 work of *Richard W. Nenno of the Wilmington Trust Company.*

Resident Trustee



States which tax such trusts

Map based on the 2013 work of *Richard W. Nenno of the Wilmington Trust Company.*

Legal Principles & Definitions

- State Estate & Inheritance Taxation

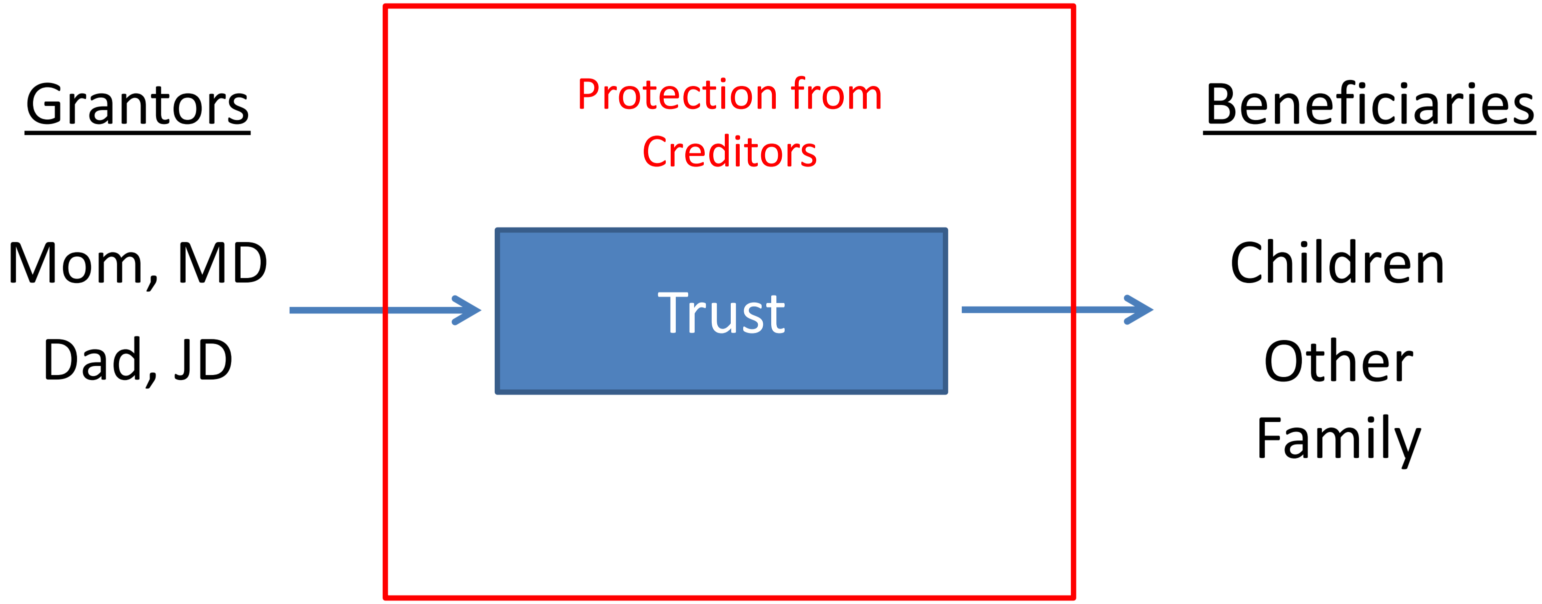
*Map Source: Minnesota House Research Department

Legal Principles & Definitions

- Reasons to Create and Fund Trusts
  - Avoid probate
  - Greater protection against family infighting
  - Shift burden of managing assets to the trustee
  - Dead-hand control; e.g. the grantor can control how/when funds are used
  - Charitable purposes
  - Creditor protection
  - Tax savings

Legal Principles & Definitions

- Reasons to Create and Fund Trusts
  - Creditor Protection



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Legal Principles & Definitions

- Reasons Not to Form Trusts
  - Loss of control and access to assets
  - Bank, brokerage, trustee, & legal/accounting fees
  - Additional complication in general

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Legal Principles & Definitions

- Definitions specific to trusts
  - *Trust* – A fiduciary relationship in which one party gives another party the right to hold title to property for the benefit of a third party
  - *Settlor, grantor, transferor, or trustor* – property owner who creates and funds a trust
  - *Testator* – a person transferring assets with a will to a trust, individual, or otherwise

Legal Principles & Definitions

- Definitions specific to trusts:
  - *Trustee*
    - also known as a fiduciary
    - person responsible carrying out the intent of the grantor
    - holds legal title of the property in trust
    - fiduciary duty - legal and ethical duty to the *Principal* (i.e. beneficiary) to:
      - Prudently manage the property
      - Loyalty to the beneficiaries
      - Provide accountings
      - Disclose material facts concerning administration

Legal Principles & Definitions

- Definitions specific to trusts:
  - *Trust Protector* – a person with power to fire and hire a trustee, appoint successor trust protector, and or, the power to amend the trust
  - *Beneficiary* – Those who benefit from the trust property in accordance with the settlors directives; holds equitable title

Legal Principles & Definitions

- Definitions specific to trusts:
  - *Corpus* – the property held in trust; aka trust estate or principal
  - *Declaration of Trust, Trust Document, Trust Instrument* – document signed by the grantor showing intent to create a trust and which provides terms to administer the trust

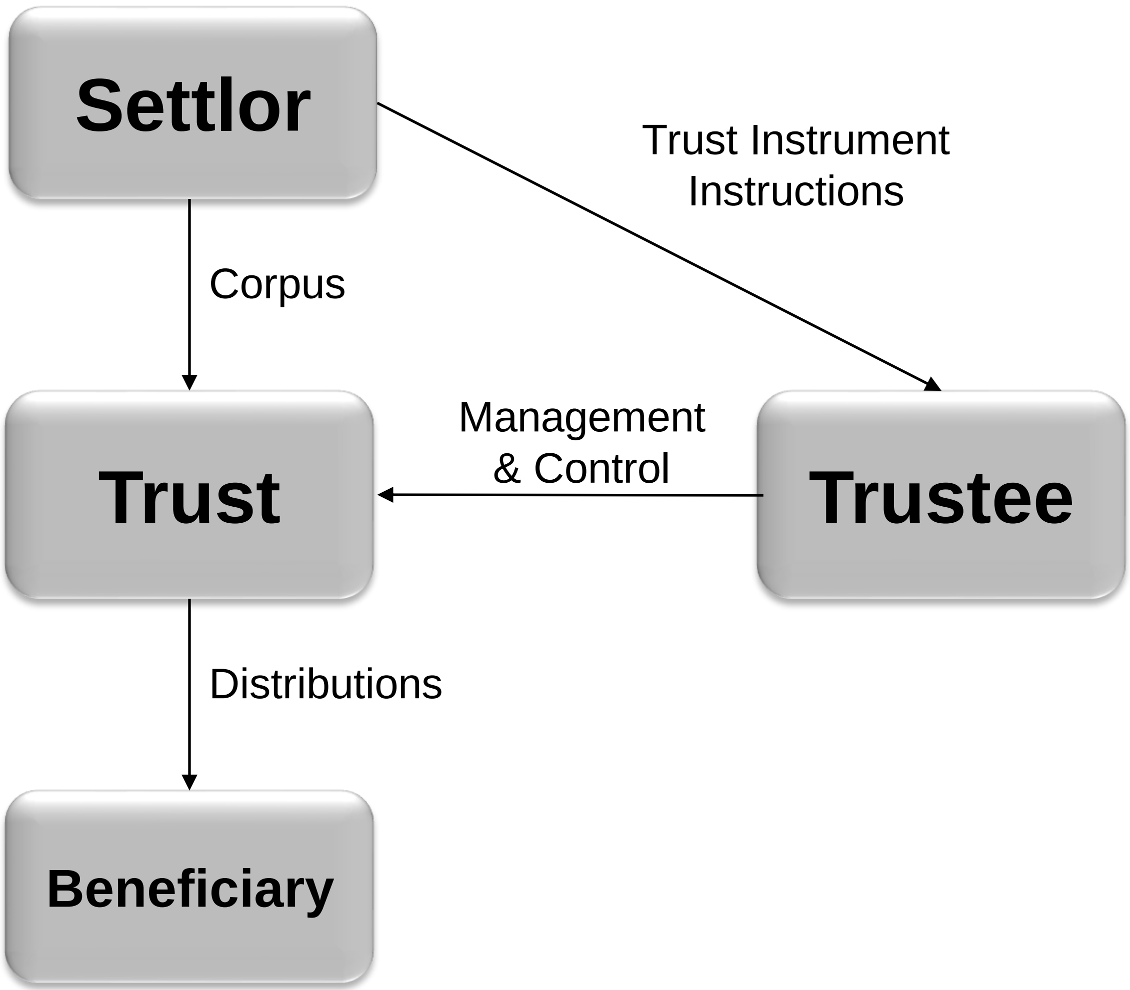
Legal Principles & Definitions

- Definitions specific to trusts:
  - *Decanting* – the act of distributing assets from one trust to a new trust with different terms
  - *Reformation* – an action to modify the language of a trust to correct an error or mistake or to meet the settlor's intent; can be judicial or non-judicial
  - *Judicial Interpretation (Construction)* – process by which courts interpret and apply legal documents

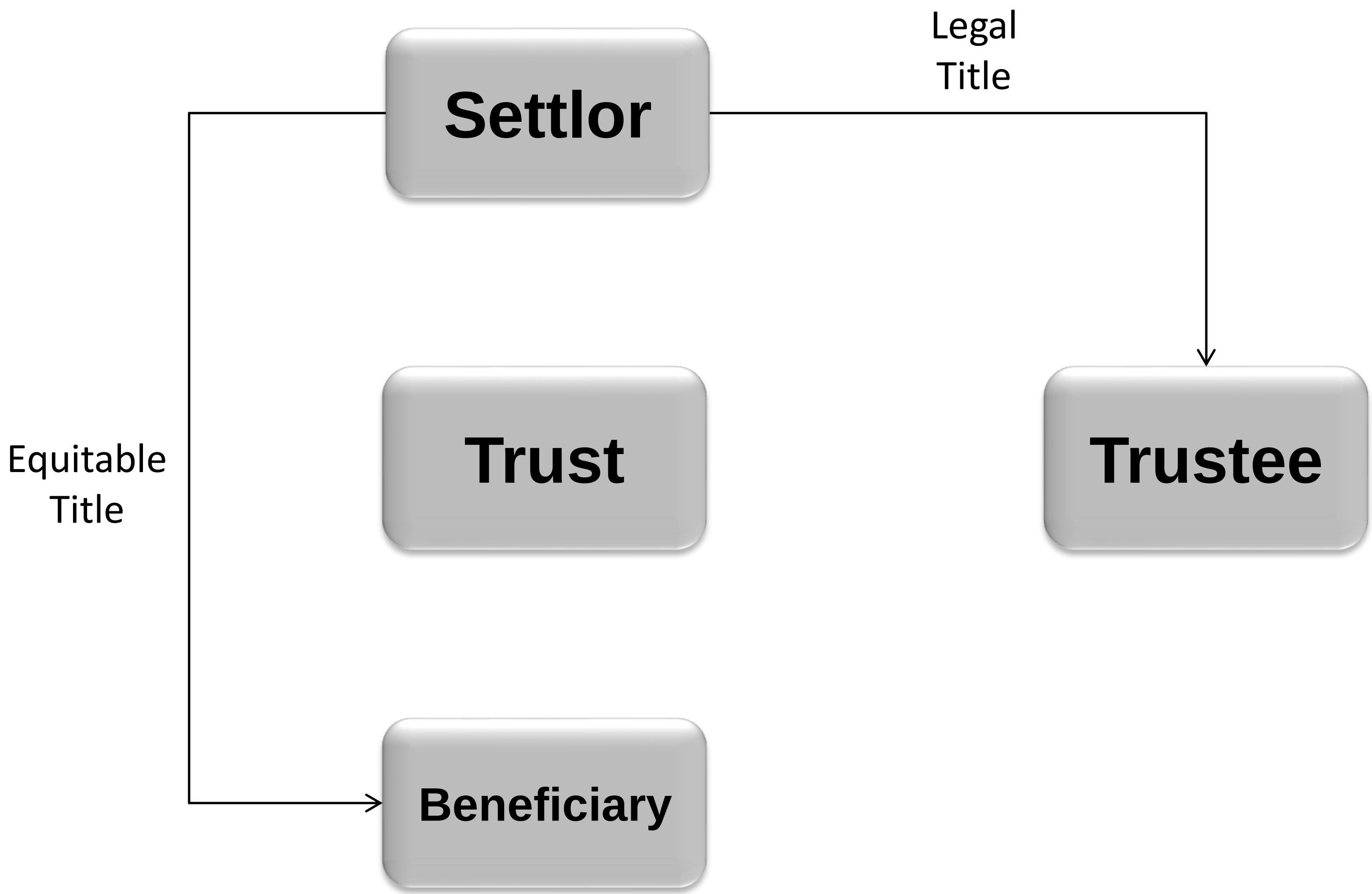
Legal Principles & Definitions

- Requirements to Form a Trust
  - *Intent*
  - *Trustee*
  - *Beneficiary*
  - *Property*
  - *Terms*
  - *Grantor*

Legal Principles & Definitions



Legal Principles & Definitions



Types of Trusts

Types of Trusts

- Two Broad Types of Trusts
  - *Revocable / Living Trust*
    - Can be altered or revoked entirely by the grantor
    - Primarily used to avoid probate
    - Any income is reported as the grantor's
  - *Irrevocable Trusts*
    - Cannot be altered or revoked after creation
    - Primarily used to manage estate tax liability and for asset protection
    - Income is reported as the grantor's or is reported separately as the trust's

Types of Trusts

- Types of Trusts by Time of Funding
  - *Inter vivos trust*
    - trust created during the life of the grantor
    - can be revocable or irrevocable
  - *Testamentary trust*
    - trust created at the death of the grantor
    - irrevocable because the grantor is deceased

Types of Trusts

- Types of IRA Trusts by Distributions
  - *Accumulation Trust*
    - can accumulate RMDs
  - *Conduit Trust*
    - distributes all RMDs received to beneficiaries

Types of Trusts

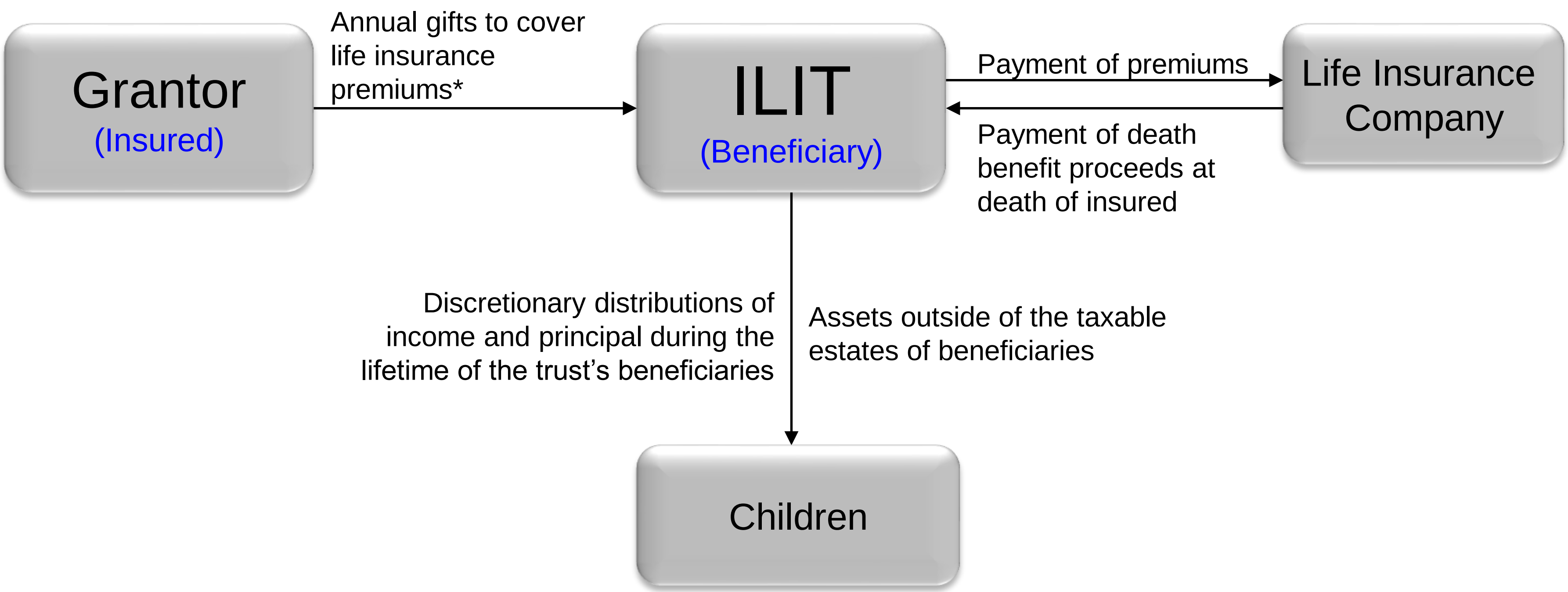
- Common Types of Trusts by Purpose
  - *Asset Protection Trusts*
    - a trust created to protect assets from creditors
    - often an irrevocable trust with situs in a state with certain favorable trust code provisions
  - *Special Needs Trusts*
    - a trust created to provide for a disabled person that does not effect eligibility for government programs

Types of Trusts

- Common Types of Trusts by Purpose
  - *Irrevocable Life Insurance Trust (ILIT)*
    - a trust to pay the premiums and receive the death benefit of a life insurance policy
    - often funded with annual exclusion "*Crummey*" gifts
  - *Dynasty Trust*
    - an irrevocable trust meant to transfer wealth to future generations
    - allocated GST exemption
    - formed in a jurisdiction with a favorable trust code, favorable tax code and a favorable or no rule against perpetuities

Types of Trusts

ILIT



*** <u>NOTE</u>: Gifts to the ILIT will use grantor's annual gift exclusion and/or lifetime gift exemption.**

Types of Trusts

Dynasty Trust

Parent → Gift* → Dynasty Trust

No transfer tax paid.

Discretionary Distributions to Children for Life

No transfer tax paid.

Discretionary Distributions to Grandchildren for Life

No transfer tax paid.

Discretionary Distributions to Great-Grandchildren for Life

No transfer tax paid.

Future Generations

Advantages

- Creditor protection
- Divorce protection
- Estate tax protection
- Direct decedent protection
- Spendthrift protection
- Consolidation of capital

*** Gift should take advantage of any remaining Unified Credit / GST exclusion remaining.**

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Types of Trusts

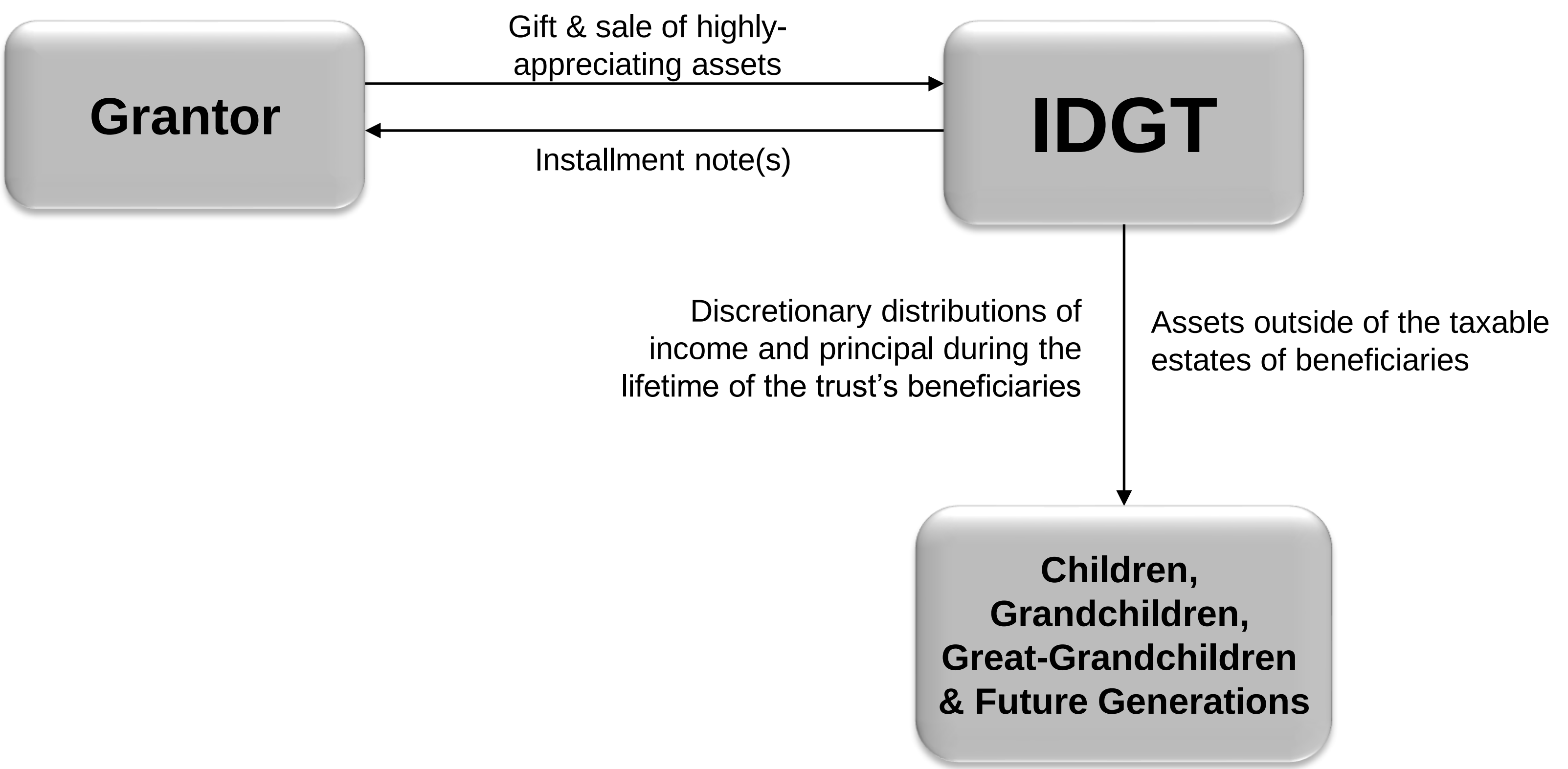
- Common Types of Trusts by Estate Tax Planning Technique
  - *Crummey Trust*
    - Grantors often want to give large sums via trusts with restrictive distribution rights, however only present interests qualify as annual exclusions gifts
    - Therefore, the drafting attorney will include a *Crummey* Power which allows the beneficiary to withdraw the gift from the trust without restriction for a certain period of time thereby creating a gift of a present interest
    - *Crummey* is the name of the taxpayer who won the Tax Court case approving the strategy
    - *Crummey* Gifts and *Crummey* Interests refer to the same

Types of Trusts

- Common Types of Trusts by Estate Tax Planning Technique
  - *Intentionally Defective Grantor Trust (IDGT)*
    - A trust intentionally made defective for income tax purposes; i.e. the grantor pays any income tax due to yield or capital gain attributable to trust assets
    - Beneficial because payment of the trust's tax is not a taxable transfer for gift or estate tax purposes & sales to the trust are not a recognition event for income tax purposes

Types of Trusts

IDGT – Example of a Sale to the Trust

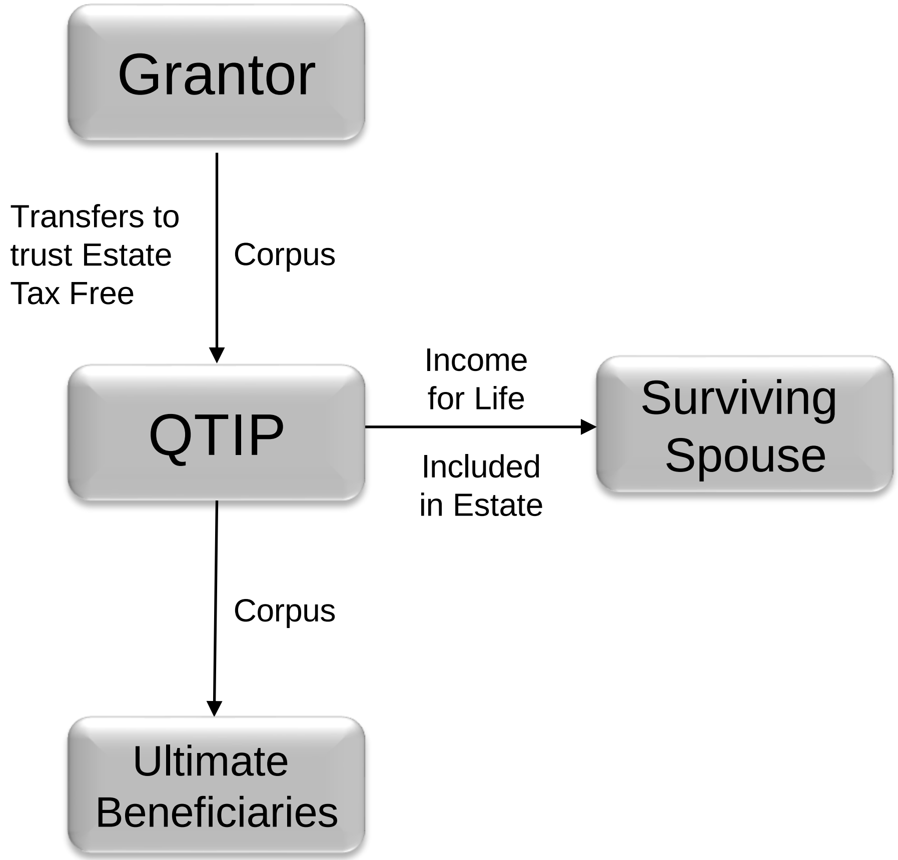


Types of Trusts

– *Qualified Terminable Interest Property Trust (QTIP)*
  - Enables a grantor to provide for a surviving spouse while maintaining control of the disposition of the assets after the spouse's death
  - Qualifies for the marital deduction (for estate tax) and therefore no estate tax is incurred with respect to QTIP until the second death
  - Surviving spouse receives all income from the trust for life and reports it on their personal tax return

Types of Trusts

QTIP



Types of Trusts

– *Qualified Personal Residence Trust (QPRT)*

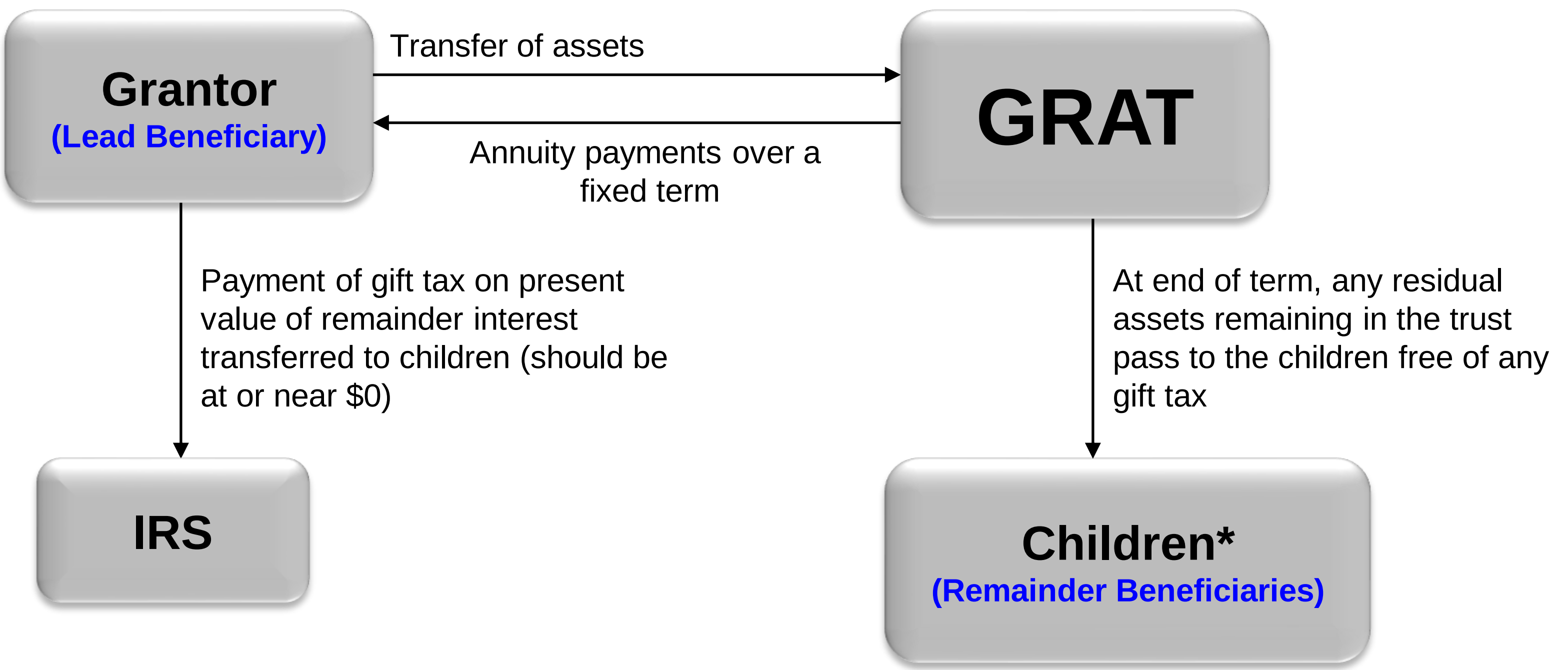
- Used to transfer a grantor's house out of their estate at a low gift value
- Irrevocable split interest trust
- Grantor retains the right to live in the house for a number of years rent free and then the remainder beneficiaries become fully vested
- Grantor pays rent after the remainder beneficiaries are vested

Types of Trusts

- Common Types of Trusts by Estate Tax Planning Purpose
  - *Grantor Retained Annuity Trust*
    - "Freezes" the estate tax return value of assets transferred to the trust
    - Annuity is paid to the grantor annually or more frequently for a term of years
    - Income is reported by grantor during the term of the annuity
    - Income is usually reported by the trust after the term of the annuity is complete

Types of Trusts

Grantor Retained Annuity Trust



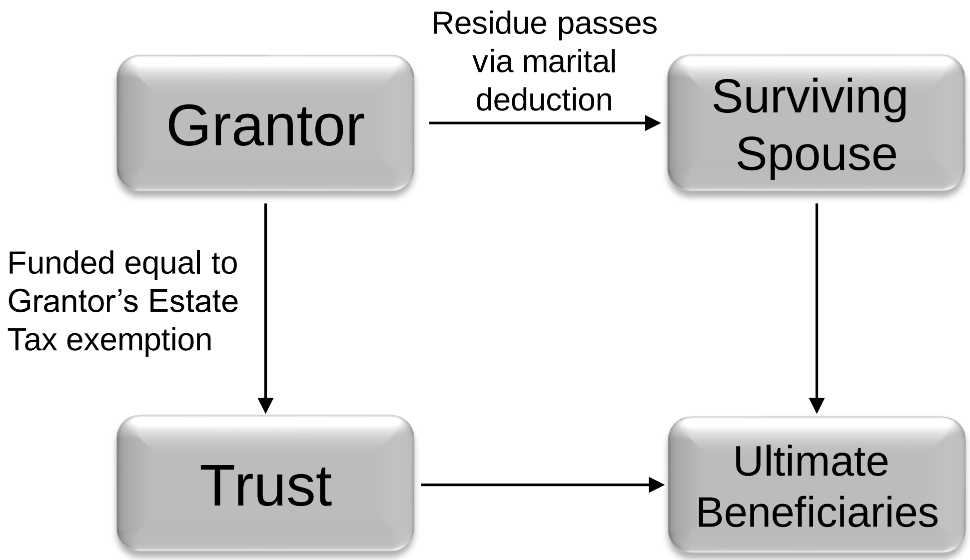
*Instead of naming the children as outright remainder beneficiaries of the GRAT, a grantor trust could be used (thus producing a greater estate tax benefit).

Types of Trusts

- Common Types of Trusts by Estate Tax Planning Purpose
  - *Bypass Trust*
    - Transfer of a portion of a married couple's property into a testamentary irrevocable trust for the benefit of children, typically, at the death of the first spouse
    - Designed to capture all or a portion of the estate tax exemption at the first death
    - More popular before portability was added, but it remains useful
    - Pays its own tax

Types of Trusts

Bypass Trust

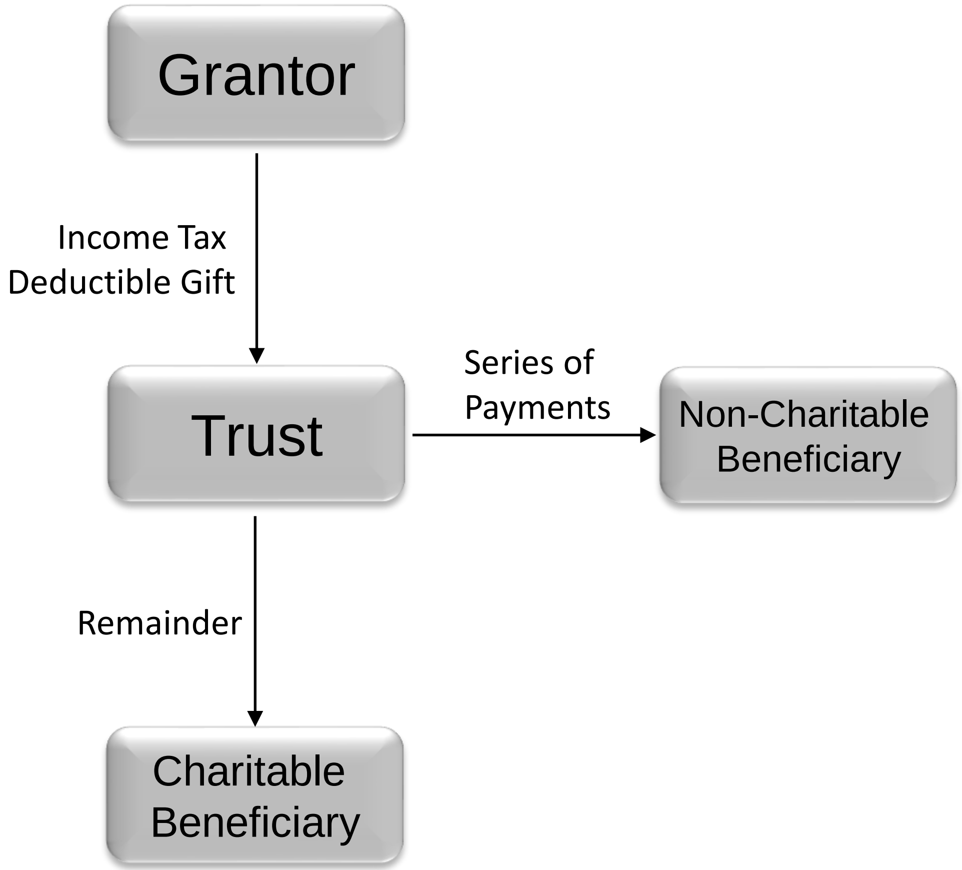


Types of Trusts

- Common Types of Trusts by Charitable Purpose
  - *Charitable Remainder Trust*
    - Distributes assets on an annual or more frequent basis to a non-charitable beneficiary
      - For a term of years or life
      - Unitrust or Annuity
    - Distributes remaining assets to charity
    - Can be used to manage income taxation, however charitable intent is almost always required

Types of Trusts

CRT

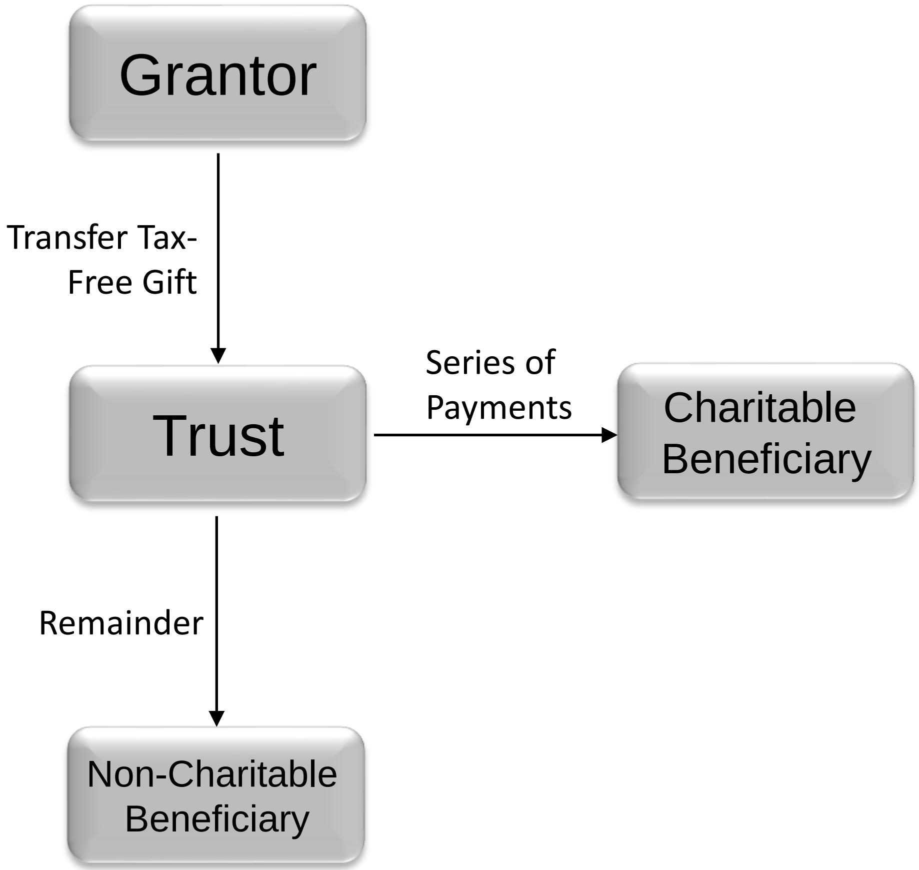


Types of Trusts

- Common Types of Trusts by Charitable Purpose
  - *Charitable Lead Trust*
    - Distributes assets on an annual or more frequent basis to a charitable beneficiary
      - For a term of years of life
      - Unitrust or Annuity
    - Distributes remaining assets to a non-charitable beneficiary (usually a younger family member)
    - Can be used to manage estate taxation, however charitable intent is almost always required

Types of Trusts

CLT



Types of Trusts

- Types of Trusts for Tax and Accounting Purposes
  – *Simple Trust*
    - Must pay out all income to the beneficiary
  – *Complex Trust*
    - Can accumulate income

*Terms refer to a federal tax designation only

Types of Trusts

- Types of Trusts for Tax and Accounting Purposes
  - *Grantor Trust*
    - Grantor reports and pays income tax on the yield of assets held in trust
    - Trust is ignored by the tax code
      - IRC §§ 671-679
      - Burnet v. Wells, 289 U.S. 670 (1933)
  - *Non-Grantor Trust*
    - Trust reports and pays its own income tax as a separate entity

Types of Trusts

- Types of Trusts for Tax and Accounting Purposes
  - *Qualified Subchapter S Trust (QSST)*
    - Irrevocable trust qualified to hold S corporation stock
    - Election required
    - All income must be distributed annually and only one beneficiary is allowed
    - Grantor trust with respect to the beneficiary
  - *Electing Small Business Trust (ESBT)*
    - Irrevocable non-grantor trust qualified to hold S corporation stock
    - Income can be accumulated and more than one beneficiary is allowed

Trust Accounting Concepts

Trust Accounting Concepts

- General Income Tax Rules
  - Trusts and estates are separate taxable entities which receive income and pay expenses
  - Taxable income computed similar to individuals
    - Exemption
      - $100 complex trust
      - $300 simple trust
      - $600 estate
  - Method of tax accounting
    - Trusts – Calendar year (i.e. Jan. 1st – Dec. 31st)
    - Estates – Fiscal or calendar year

Trust Accounting Concepts

- General Tax Rules
  - Income taxed to either the trust/estate or the beneficiary
    - If income is accumulated, then the income is taxed to the trust/estate
    - If income is distributed, then the trust/estate gets an income tax deduction and beneficiaries report taxable income

Trust Accounting Concepts

- Fiduciary accounting income
  - Governed by state law and the trust instrument
  - Determines the amount that may or must pass to the trust's or estate's beneficiaries
- Tax accounting income
  - Governed by federal income tax law
  - Determines who reports taxable income

Trust Accounting Concepts

- Uniform Principal and Income Act (UPIA)
  - A uniform act
    - is a proposed state law;
    - attempts to harmonize law between states;
    - enacted by individual states in whole or part
  - **The UPIA focuses on the determination of what is income versus principal for a trust or estate**
  - Created in 1931 and revised in 1962 and 1997 (Revised UPIA or RUPIA); amendments added in 2004, & 2008.

Trust Accounting Concepts

- Uniform Principal and Income Act (UPIA)
  - Important because distribution rights are often dependent on the categorization of principal and income

Important Trust Clauses

Important Trust Clauses

- Powers of Appointment
  - *General Power of Appointment (GPA)*
    - power to direct assets to any individual or organization
    - generally the holder of a GPA is treated as the owner of the assets for estate and gift tax purposes (§ 2041)
  - *Limited Power of Appointment (LPA)*
    - power to direct assets to a certain class of beneficiaries
    - generally the holder of a LPA is not treated as the owner of the assets for estate and gift tax purposes

Important Trust Clauses

- Estate Tax Apportionment Clauses
  - Clause that apportions tax liability among beneficiaries
  - One of the most complex clauses; can sometimes effectively control the entire estate plan

Important Trust Clauses

- Defined Value Clause
  - defines the value of the transfer as opposed to the assets transferred
  - e.g. $100,000 of shares in the closely-held company; as opposed to saying 100 shares

Important Trust Clauses

- Defined Value Clause
  - Meant to reduce audit risk when transferring difficult to value property (usually into trust)
  - Can create finality issues
  - Different from a savings clause

Important Trust Clauses

- Defined Value Clause
  - If the value of the assets transferred is determined to be greater than the desired amount the excess is redirected to:
    - The transferor
    - Charity
    - A different entity; typically a trust or individual

Important Trust Clauses

- Defined Value Clause
  - *Wandry v. Commissioner* (T.C. Memo. 2012-88)
    - approved a clause which returned the value of a gift in excess of the desired value of the gift to the donor
    - language used: "that number of units which had a value equal to the taxpayers' remaining exemption amount"
    - IRS does not agree with the decision

Important Trust Clauses

- IRA Trusts – Requirements for a Trust to be a Qualified Designated Beneficiary:
    1. Trust is valid under state law

       Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(1)
    2. Trust is irrevocable upon death of owner

       Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(2)
    3. Beneficiaries of the trust are identifiable from the trust instrument

       Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(3)
    4. Documentation requirement is satisfied

       Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(4)

Important Trust Clauses

- Difficult to Pay IRD to Charity & receive a Charitable Deduction
  - Sample of language that <u>might</u> work:

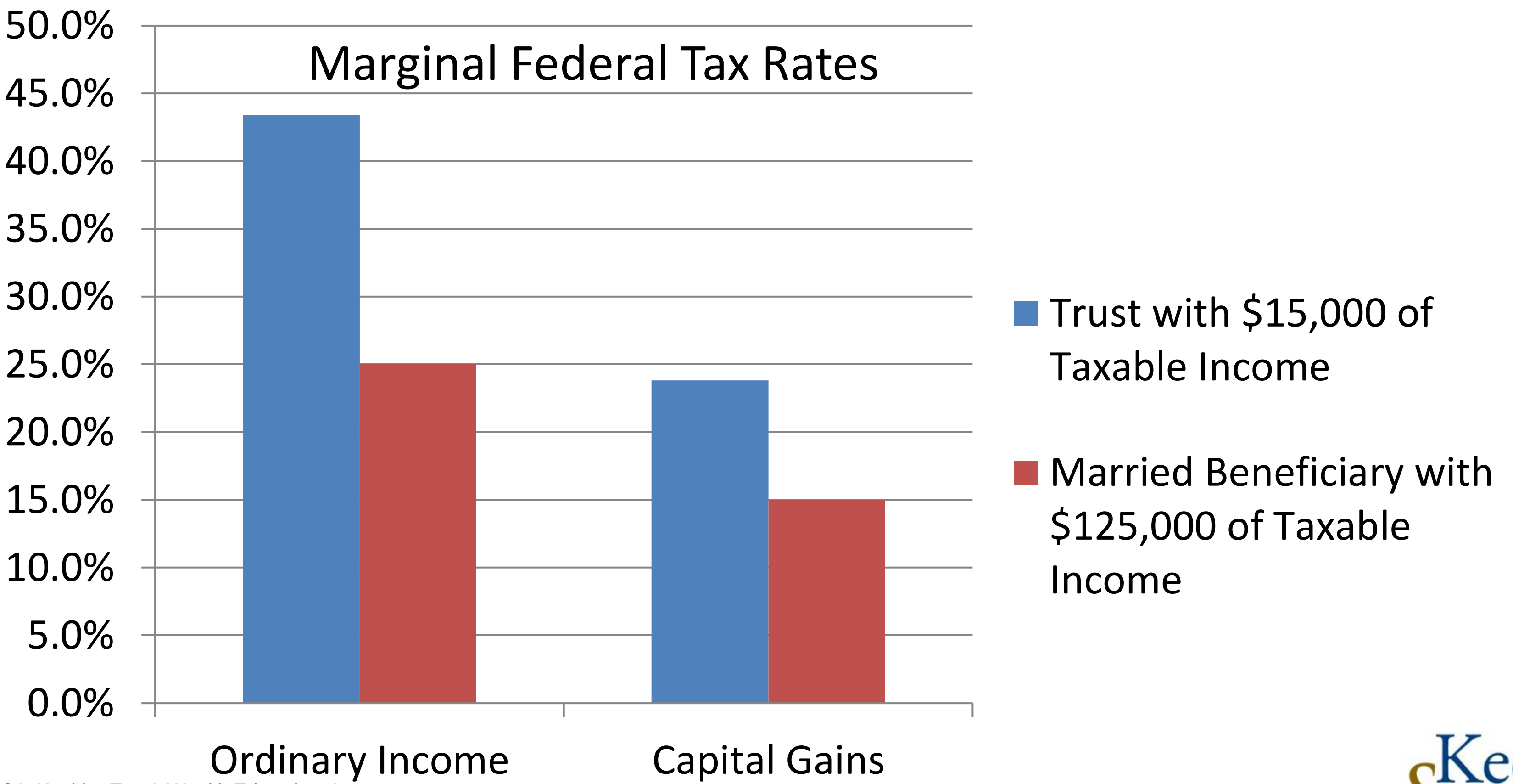
    I instruct that all of my charitable gifts, bequests and devises shall be made, to the extent possible, from "income in respect of a decedent" (as that term is defined under the U.S. income tax laws) included in gross income and shall qualify for a charitable income tax deduction under Section 642(c) of the Internal Revenue Code of 1986 and any corresponding future tax laws.

Important Trust Clauses

- Shifting Capital Gains to Beneficiaries
  - Shifting income from the trust to beneficiaries using distributions can be beneficial
  - Generally, IRC § 643 excludes capital gains from DNI
  - However, Reg. § 1.643(a)-3(b) provides that capital gains can be included in distributable net income pursuant to the trust document or state law.

Important Trust Clauses

- Shifting Capital Gains to Beneficiaries



Important Trust Clauses

- Shifting Capital Gains to Beneficiaries
  - Capital gains are considered DNI if also considered fiduciary accounting income
  - Capital gains could be considered DNI if allocable to income by exercise of a discretionary power
  - Capital gains could be considered DNI for certain "age of attainment" distributions

Important Trust Clauses

- Grantor Trust Clauses
  - Often a clause will express the intent of the grantor for the trust be treated as a grantor trust if certain powers are held by the grantor

Appendix – More on Grantor Trusts

Important Trust Clauses

- Grantor Trust Clauses
  - IRC 671-679
  - Created to eliminate income tax abuses involving lower trusts income tax brackets

Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 672: Definitions
    - Adverse
      - Any person having a substantial beneficial interest in the trust which would be adversely affected by the exercise or nonexercise of the power which he possesses respecting the trust. A person having a general power of appointment over the trust property shall be deemed to have a beneficial interest in the trust.
    - Nonadverse
      - Any person who is not an adverse party.
    - Related or Subordinate
      - Nonadverse party who is:
        - » Spouse if living with the grantor
        - » Grantor's father, mother, issue, brother or sister; an employee of the grantor; a corporation or any employee of a corporation in which the stock holdings of the grantor and the trust are significant from the viewpoint of voting control; a subordinate employee of a corporation in which the grantor is an executive

Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 672: Definitions
    - Spousal Attribution
      - Grantor shall be treated as holding any power or interest held by—
        - » Any individual who was the spouse of the grantor at the time of the creation of such power or interest, or
        - » Any individual who became the spouse of the grantor after the creation of such power or interest, but only with respect to periods after such individual became the spouse of the grantor.

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Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 673
    - The grantor shall be treated as the owner of any portion of a trust in which he has a reversionary interest in either the corpus or the income therefrom, if, as of the inception of that portion of the trust, the value of such interest exceeds 5 percent of the value of such portion.

Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 674: Power to Affect Beneficial Enjoyment
    - Grantor is treated as owner of any portion of the trust over which grantor controls beneficial enjoyment or corpus or income, exercisable by grantor or non-adverse party or both, without the consent of any adverse party

Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 674: Power to Affect Beneficial Enjoyment
    - Exceptions of 674(b):
      - Power to apply income to support of a dependent
      - Power affecting beneficial enjoyment only after occurrence of event
      - Power exercisable only by will
      - Power to allocate among charitable beneficiaries
      - Power to distribute corpus
      - Power to withhold income temporarily
      - Power to withhold income during disability of a beneficiary
      - Power to allocate between corpus and income

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Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 675: Administrative Powers
    - Power to deal for less than adequate and full consideration; or
    - Power to borrow without adequate interest or security; or
    - General powers of administration held in a non-fiduciary capacity without the approval of a person in a fiduciary capacity to vote stock, control investment of trust funds, or
    - The power to reacquire trust assets and substitute other property of equal value

Important Trust Clauses

- Grantor Trust Clauses
  - IRC Sec. 675: Administrative Powers
    - Power alone isn't sufficient
      - Facts and circumstances analysis
    - Grantor can release
    - Protector can re-grant

Important Trust Clauses

- Grantor Trust Clauses
  - “Wholly grantor” vs. “partially grantor” trust:
    - E.g., a retained power over income makes it a grantor trust as to the income but not as to capital gains
    - E.g., a power of revocation makes it a “wholly grantor” trust