

FLEXIBILITY AND CORE PRACTICES: CONSIDERATIONS IN ESTATE PLANNING FOR CLIENTS BELOW THE EXEMPTION AMOUNT

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INTRODUCTION

When working with clients whose overall assets fall below the increased estate tax exemption amount, attorneys should give consideration to ensure flexibility in the overall planning and to give careful focus on the client’s core estate planning documents when working with clients in this changing tax landscape. Below is a discussion of these important considerations.

HYPOTHETICAL SCENARIO: MIDDLE AGED COUPLE WITH TOTAL ASSETS BELOW THE EXEMPTION AMOUNT

We will explore these considerations through the use of a hypothetical. Assume that Husband (“H”) and Wife (“W”) ages 48 have been married 20 years and have 3 children (“C”) ages 18, 15 and 13. It is a first marriage for both and their assets total approximately \$13 million. These include the following:

Asset	Value
Home	\$1,000,000
H’s Retirement	\$1,500,000
W’s Retirement	\$1,500,000
Joint Brokerage (stocks, bonds)	\$5,000,000

W’s Gifts and Inheritance from Parents (“Inheritance”)	\$4,000,000
Total	<u>\$13,000,000</u>

Their total assets are well below the combined exemptions of \$22.4 million. H and W have typical wishes for devolution of their estate: They would like the other to benefit in the event of death and then have the property pass down to C with distributions by way of separate trusts for C’s benefit. H and W are fine with C having a right of withdrawal, at certain ages, over C’s trust.

THE IMPORTANCE OF FLEXIBLE PLANNING: PORTABILITY AND ITS ALTERNATIVES

With the increased exemptions and given the make-up of the assets, the core planning becomes much more important. Attention should be given to income tax planning and overall flexibility. H and W desire to attain a step-up in basis on the assets at each of their deaths. Under the present scenario H and W could have a joint trust with each possessing a general power of appointment during their lives over the property contributed. H and W could rely on portability at the first death.

If the assets were largely in one spouse’s name (e.g. W’s gifts are inheritance), H and W could still rely on portability but might consider utilizing planning that would provide flexibility for use of the marital deduction and ultimate step-up in basis upon the death of the survivor. For example, if W wanted H to benefit during his lifetime from her “Inheritance” she could, at death, utilize a single trust that would qualify for QTIP treatment. The fiduciary could make a QTIP election or not and would have the power to

divide the trust, thereby allowing use of the exclusion amount if it made sense. Alternatively, a disclaimer technique could be used for H, allowing him “to wait and see” whether it makes sense under the laws in effect at the time to disclaim to a credit shelter trust. Another technique would be to utilize a Clayton QTIP trust and if the QTIP election is not made (within 15 months after death), the amount not elected for QTIP treatment will pass to the credit shelter trust.

W, however, may want to be sure the Inheritance is not diverted from her lineal descendants at her death. She could leave the Inheritance to a credit shelter trust at her death, of which H and C are beneficiaries. There could be sprinkle powers among the beneficiaries. Because there could be substantial appreciation of the assets within the credit shelter trust, it may be desirable to try and attain an adjusted basis in those assets at H’s subsequent death. A trust protector could have the power to distribute principal to H for tax reasons and to provide H with a general power of appointment (e.g., to the creditors of H’s estate).

If W, during her lifetime, wants to ensure she is able to use some of the higher exemptions and is concerned perhaps about a subsequent decrease in the exemptions, W could make a completed gift of all or part of the Inheritance to an irrevocable trust of which H would be a beneficiary. Given that the use of the exemption will not be clawed back at her death, this could allow W to use her increased exemption, yet still retain some benefit in the future if necessary. Again, flexibility within the trust agreement could be

built-in so that a trust protector could make distributions for tax reasons (in addition to typical discretionary standards), to provide powers of appointment, and generally modify or terminate the trust if beneficial.

BACK TO BASICS: A FOCUS ON THE CORE ESTATE PLAN

H and W should also focus on the basics of their planning. Titling of assets within a revocable trust or other manner to avoid a probate estate may be desirable and given strong consideration. For example, should the home be (or remain) titled as joint tenants with rights of survivorship? Should the home be titled in the revocable trust? Providing certainty for funding of trusts through proper beneficiary designations cannot be discounted. With H and W’s retirement assets, it is likely each will want the other to be the primary beneficiary to provide the greatest flexibility; however, do not ignore the contingent beneficiary designation. With young children, H and W will likely want their trust to be the contingent beneficiary for the benefit of C. Careful attention should be given so that the trust qualifies as a designated beneficiary and that distributions may be stretched out over C’s life expectancy.¹

Focusing on the client’s powers of attorney is important. Do the client’s advanced directives reflect their wishes with regard to health care and end-of-life decisions? Should the agent under a general durable power of attorney have “hot” powers? H and W may want their agent to have the power to disclaim assets, create or modify a trust, add property to a trust, and

¹ With potential changes in retirement plan distributions under the SECURE Act (H.R. 1994 “Setting Every Community Up for Retirement

Enhancement Act”), careful consideration will need to be given to naming a trust as a beneficiary of retirement benefits.

make gifts that are beneficial for tax purposes. Careful attention to these basic – yet essential documents is more important than ever.

CONCLUSION

By focusing on flexibility and giving careful consideration to the planning basics, estate planners working with clients below the exemption amount will create greater opportunities to protect the client's assets and provide real value for families. As such, attorneys will need to embrace such flexibility in drafting and implementing documents and not overlook the importance of the basic, yet essential, documents that comprise a well-thought-out estate plan.