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UNDERSTANDING AND IMPLEMENTING TRUSTS IN FINANCIAL AND ESTATE PLANNING WORKSHOP

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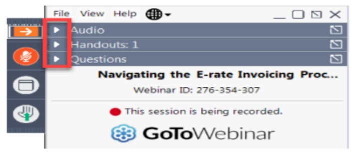

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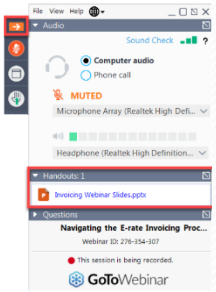

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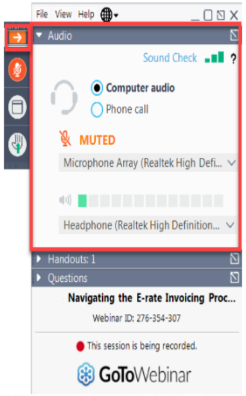

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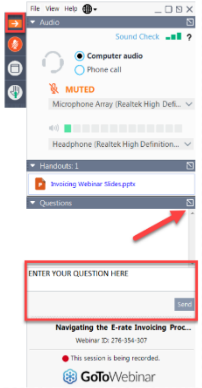

Today’s Instructor

Arthur Joseph Werner, JD, MS (Taxation), is the president and is a shareholder in the lecture firm of Werner-Rocca Seminars, Ltd. Mr. Werner’s lecture topic specialties include business, tax, financial and estate planning for high net worth individuals.

Art received his B.S. in Accounting and his M.S. in Taxation from Widener University. He holds a J.D. in Law from the Delaware Law School.

Art lectures extensively in the areas of Tax Planning and Compliance as well as Estate and Financial Planning, Financial Planning to CPAs, EAs, and other tax professionals, and has presented well in excess of 2500 eight-hour seminars over the past twenty-five years as well as numerous webinars and video presentations. Mr. Werner has been rated as having the highest speaker knowledge in his home state of Pennsylvania by the Pennsylvania Institute of Certified Public Accountants, was awarded the AICPA Outstanding Discussion Leader Award in the State of Nevada, the Florida Institute of CPAs Outstanding Discussion Leader Award, and the South Carolina Association of CPAs Outstanding Discussion Leader Award.

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Day 1 –
Understanding and Implementing Trusts in Financial and Estate Planning

Definition

- What is a Trust?
  - Device of protection
    - Protect assets
    - Protect current beneficiaries
    - Protect future beneficiaries

The “Players”

- The Trustor
  - a/k/a Settlor or Grantor
- The Trustee
  - Can be human or non-human
- The Beneficiaries
  - Must equal 100 % of the eventual distribution of the trust corpus

Notes

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The “Three Questions”

- All trusts can be specifically defined and classified by asking three specific questions of them
- Understanding these three questions can best help you understand the purpose of the trust and the technique or techniques that it is being used for

Question #1

- How is the Trust created? (Trusts can be created in only in one of two ways.)
  - Inter-vivos (a separate legal document)
  - Testamentary (within a Last Will and Testament)

Question #2

- Can the Trust be changed, altered, amended, or revoked?
  - Yes (Trust is revocable)
  - No (Trust is irrevocable)

Caveat

- Can you have a revocable inter-vivos trust?
- Can you have an irrevocable inter-vivos trust?
- Can you have a revocable testamentary trust?
- Can you have an irrevocable testamentary trust?

Question #3

- For Federal Income Tax purposes, how is the Trust classified?
  - Grantor
  - Simple
  - Complex
- So – WHAT IS INCOME?????

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Probate

- What is "Probate"?
  - Legal definition: The act of proving that an instrument purporting to be a Last Will and Testament was executed in accordance with legal requirements and of determining its validity thereby. In addition a Probate Court is a special court of law having specific jurisdiction of proceedings incident to the settlement of a decedent's estate.

Problems of Probate

- Higher Costs
- Delays
- Publicity
- Retainage of Assets
- Court Supervision
- Additional Professional Fees

Tax Considerations in Trusts

- Income Tax Issues
- Estate and Gift Tax Issues
- Basic Planning Techniques

Income Tax Issues

- Grantor Trust Rules
  - A "Grantor Trust" is a trust that for income tax purposes does not exist. All income in a Grantor Trust is properly reported on the Trustor's 1040.
  - All Revocable Trusts are Grantor Trusts
  - Some Irrevocable Trusts are Grantor Trusts
    - IRC §§671 – 678 define when the terms of an Irrevocable Trust create a Grantor Trust for income tax purposes

Income Tax Issues (cont.)

- General Rules
  - For the most part, Subchapter J of the Internal Revenue Code is very similar to the parts of the Internal Revenue Code dealing with Individual Income Taxation.
    - There are four tax brackets (10%, 24%, 35%, and 37%), however, the brackets are compressed compared to individual rates (ex: for 2023, the 37% tax bracket becomes effective when income exceeds $14,450)

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1041 Income Tax Rate Schedule – 2023 (with compressed tax brackets)

Income Amount	Marginal Rate
0 - $2,900	10%
$2,901 - $10,550	24%
$10,551 - $14,450	35%
$14,451 and above	37%

(Note: The 12%, 22%, or 32% brackets that apply to individuals do not apply to fiduciary entities!)

Affordable Care Act Taxes

- Estates and Trusts are subject to the 3.8% surtax on the lesser of:
  - Undistributed net investment income, or
  - the amount by which adjusted gross income exceeds the top bracket for estate and trust income taxation.

Income Tax Issues (cont.)

- General Rules
  - Income Distribution Deduction
    - All income that is properly distributed from the trust is deducted from trust income
    - Simple Trust: All income must be distributed (potential for a "deemed distribution")
    - Complex Trust: Trustee has certain discretion (potential for 65 day election)

Transfers with Control

- Revocable Trust
  - No taxable gift because transfer was not complete
  - Upon the death of the Trustor, however, the assets of the Revocable Trust are a part of the taxable estate of the Trustor (Internal Revenue Code §2038

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IRC § 2038

- **Gratuitous Transfers in Which the Decedent Retained the Right to Alter, Amend, or Revoke the Gift**
- The gross estate includes the value of any interest in property transferred by decedent during lifetime, if the enjoyment of the interest was subject to any change through the exercise of a power by the donor to alter, amend, revoke or terminate.

IRC § 2038 (cont.)

- The underlying rationale for inclusion of the transferred property in the gross estate is based upon the fact that the decedent actually retained control over the ultimate beneficial enjoyment of the property transferred.
  - A transfer of property which is subject to revocation and reclaiming by the transferor is not considered a completed transfer.
  - Note that the transferor need not actually exercise his power to alter, amend, revoke or terminate; he need only possess any such power in order for the property to be includable in his gross estate.

IRC § 2038 (cont.)

- A prominent example of this type of transfer is the revocable inter-vivos trust

Transfers with Control (cont.)

- Transfers within three years of death
  - Applies to transfers of life insurance policies to Irrevocable Life Insurance Trusts
  - The transfer of ownership of a life insurance policy from an individual who dies within three years of said transfer to anyone else (including a trust) where the insured is the transferring individual will cause the death benefit of the policy to be a part of the taxable estate (IRC §2035)

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IRC § 2035

- **Certain Property Transferred Gratuitously Within Three Years of Death**
- Three Year “Look-Back” Rule
- Under IRC §2035(d), if an insured person transfers an insurance policy and dies within the 3-year period following the transfer, the entire policy proceeds will be includable in the insured's gross estate.

Transfers with Control (cont.)

- Transfers with retained life interests
  - Applies to transfers of an asset where the transferor retains the use and enjoyment of the transferred asset for the remainder of his or her life (IRC §2036)
  - Trusts that are susceptible to this IRC section are GRITs, GRATs, GRUTs, and QPRTs

IRC § 2036

- **Gratuitous Lifetime Transfers Where the Decedent Retained the Income or Control over the Income**
- This Code section requires the inclusion in the gross estate of property which the decedent, while living, had transferred as a gift but in which he retained for himself a beneficial interest to last for the rest of his life.

Transfers with Control (cont.)

- Transfers conditioned upon surviving the decedent
  - Applies to transfers of an asset where the transferor places a condition that if the recipient of the asset dies before the transferor of the asset, then the asset is returned to the (IRC §2037)

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IRC § 2037

- **Gratuitous Lifetime Transfers Conditioned on Surviving the Decedent**
- This Code section requires the inclusion in the gross estate of property which had been transferred by gift during lifetime if
  - Possession or enjoyment of the property by the transferee can be obtained only at or after the transferor's death, or (next slide.......)

IRC § 2037 (cont.)

- The decedent retained a possibility that the property, other than the income alone, would return to the decedent or his estate or would be subject to a power of disposition by him, and such reversionary interest had a value, immediately prior to decedent's death, in excess of 5 percent of the total value of the property.

- The value of a reversionary interest is determined in accordance with recognized valuation principles for determining future or conditional interests in property as set forth in Treasury regulations.

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Estate Planning

- Marital Deduction / Unified Credit Trust
  - "A/B" Trust
  - Description / Explanation as to how trust works

IRC § 2056

- **Bequests to Qualified Surviving Spouses**
  - The Surviving Spouse and the Decedent must have been legally married (as per state law) immediately prior to the Decedent's death
  - The Surviving Spouse must be a citizen of the United States

Issues – Estate Taxation

- Maximum Estate Tax rate is now 40%
- The “ lifetime exclusion” is now $12,920,000 (for 2023)
- “Portability” is permanent
- Cost of living adjustments will continue

Issues – Gift Taxation

- 2023 annual exclusion - $17,000
  - $34,000 if non-donor spouse agrees to split
- Carryover basis + Gift Tax paid (**IRC §1015**)
- Tuition payments and medical payments not a gift (**IRC §2503(e)**)

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Portability Election (IRC §2010(c))

- When a decedent is survived by a spouse, the amount of the Estate Tax exclusion for that decedent's estate that is not used by that decedent's estate is "portable" – that is, it can be used for gift or estate tax purposes by the surviving spouse.

Portability Effect

The effect of Portability makes the unused "basic exclusion amount“ to pass to a surviving spouse.

The "basic exclusion amount" is thus similar to an exemption, and it is often referred to as an "exemption."

The “basic exclusion amount” applies to the total of estate and gift tax transfers.

The “basic exclusion amount” is subject to cost of living adjustments

Reasons NOT to Elect Portability

Second Marriages

Financial Immaturity

Lack of Trust in Surviving Spouse

Growth of Assets

Asset Protection Issues

Advantages of Trusts over Portability

- The use of trusts can offer a certain number of "safe harbors" that portability does not
  - Example: All future appreciation in the value of assets in a Credit Shelter Trust is sheltered from estate tax in the surviving spouse's estate, which is not true of assets that pass to a surviving spouse via portability
- A trust may be a better choice if the client is seeking asset protection to make certain that the proceeds from the estate last not just the lifetime of the surviving spouse but can also provide for the next generation.

Advantages of a Credit Shelter Trust

Asset protection (generally not available using DSUE)

Appreciation exempt from surviving spouse's estate (but no step-up)

GST protection

Statute of Limitations is not extended on first spouse's 706

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UPCOMING ART WERNER EVENT:

MASTERING CHARITABLE REMAINDER TRUSTS AND FORM 5227 COMPLIANCE

Thursday, August 31st, 2023, 2:00 PM - 4:00 PM ET

! EARLY BIRD PRICING !

Registration Link:

https://cpewarehouse.com/course/course-detail/mastering-charitable-remainder-trusts-and-form-5227-compliance

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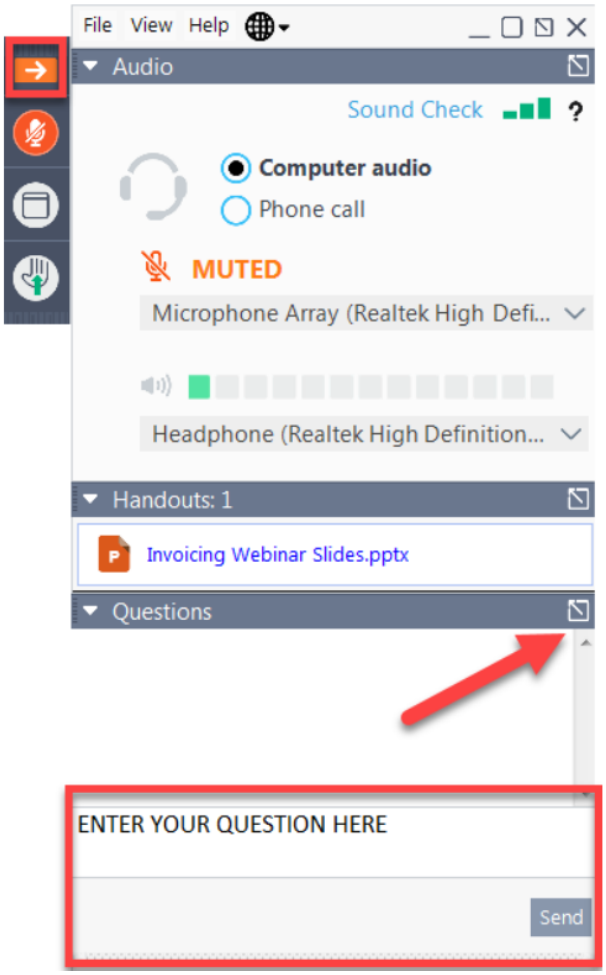

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