PLANNING IN A PERIOD OF UNCERTAINTY, INCLUDING USES OF DEFINED VALUE CLAUSES

Steve R. Akers

Bessemer Trust
300 Crescent Court, Suite 800
Dallas, TX 75201
214-981-9407
akers@bessemer.com
www.bessemer.com

The University School of Law
65th Annual Taxation Conference
2017 Stanley M. Johanson Estate Planning Workshop

December 15, 2017

Table of Contents

Table of Contents 2
1. Introduction 1
2. Legislative Developments 1
3. Estate Planning Considerations In the Face of Legislative Uncertainty and Potential Estate Tax Repeal 21
3. Structuring Trusts For Flexibility 33
4. Structuring Trusts and Other Planning to Protect Beneficiaries from Divorce Claims 48
5. Improving GRAT Performance 56
6. Installment Sales to Grantor Trusts; Settlement of *Woelbing* Cases 61
7. Self-Canceling Installment Notes (SCINs); *Estate of William Davidson*; *Estate of Johnson* 64
8. Defined Value Clauses 67
9. Family Limited Partnership and LLC Planning Developments; *Purdue, Holliday, Beyer, Powell* Cases 89
10. Creating Trust With Beneficiary As Deemed Owner Under §678, "Beneficiary Deemed Owner Trust" (BDOT); Application of Letter Ruling 201633021 105

Copyright © 2017 Bessemer Trust Company, N.A.

All rights reserved.

November 9, 2017

Important Information Regarding This Summary
This summary is for your general information. The discussion of any estate planning alternatives and other observations herein are not intended as legal or tax advice and do not take into account the particular estate planning objectives, financial situation or needs of individual clients. This summary is based upon information obtained from various sources that Bessemer believes to be reliable, but Bessemer makes no representation or warranty with respect to the accuracy or completeness of such information. Views expressed herein are current only as of the date indicated, and are subject to change without notice. Forecasts may not be realized due to a variety of factors, including changes in law, regulation, interest rates, and inflation.

Estate Planning in a Period of Uncertainty, Including Uses of Defined Clauses

Steve R. Akers, Bessemer Trust

1. Introduction

The possibility of tax reform and the repeal of the estate tax (or substantially increasing the exemption amounts) has resulted in a great amount of uncertainty in planning for clients, including testamentary planning structures and in transfer planning. After describing the current status of the legislative developments surround tax reform, suggestions of planning approaches during this period of uncertainty are highlighted including ways for maximizing flexibility. The desire to avoid paying gift taxes in an environment in which the estate tax may be repealed places increased significance on the use of defined value transfers. Planning concerns with FLPs and LLCs in light of the recent *Powell* cases are summarized. An intriguing new approach is described for structuring trusts as grantor trusts as to the trust beneficiaries (termed the "BDOT") that avoids many of the uncertainties and complexities of the "BDIT" plan.

2. Legislative Developments

a. **Presidential Election**. With the election on November 8, 2016, Republicans now hold the Presidency and majorities in the House and Senate, making tax reform a very realistic possibility for 2017. In light of the significant possibility of repeal of the estate and GST tax, estate planning considerations for clients were changed overnight on November 8.

b. **House Republicans and Trump Proposals Regarding Tax Reform (Including the Transfer Tax); Process for Tax Reform Changes**.

House Republican Blueprint (June 2016). The House Republican tax reform package is described in a document published on June 24, 2016 entitled "A Better Way" (and referred to as a Blueprint for Tax Reform"). The Report says that it is premised on addressing the broken tax code, the broken Internal Revenue Service, and the need for stronger economic growth. The tax reform measures include:

- Individual: Top rate-33%; capital gains and dividends-50% exclusion (equivalent to a top rate of 16 ½%); no itemized deductions except mortgage interest and charitable deduction; no AMT; no 3.8% tax on NII; "continue the current tax incentives for [retirement] savings;"
- Tax simplification for individuals, proposing a "Simple, Fair 'Postcard' Tax Filing:"

1. Wage and compensation income _____
2. Add ½ of investment income _____
3. Subtract contributions to specified savings plans _____
4. Subtract standard deduction OR [lines 5-6] _____
5. Subtract mortgage interest deduction _____
6. Subtract charitable contribution deduction _____

7. Taxable income _____
8. Preliminary tax (from tax table) _____
9. Subtract child credit _____
10. Subtract earned income credit _____
11. Subtract higher education credit _____
12. Total tax _____
13. Subtract taxes withheld _____
14. Refund due/taxes owed _____

- Business: Corporate top rate-drop from 35% to 20%; pass through business income top rate of 25% (with a requirement that "businesses will pay or be treated as having paid reasonable compensation to their owner-operators"); immediate write-off of business investments in tangible and intangible assets (but not land); no corporate AMT;
- Border adjustment provisions (taxing certain imports but not exports), which accounts for substantial revenue to offset partially the large tax cuts in other parts of the plan; replacing the "outdated worldwide tax system" with a territorial tax system; and
- Repeal estate and GST tax.

Trump Campaign Proposal. The Trump/Pence campaign website summarized the Trump tax reform campaign proposals, which include:

- Individual: Top rate-33%; capital gains and dividends-20%; cap itemized deductions at $200,000 (joint), $100,000 (single); no AMT; no 3.8% tax on NII;
- Business: Corporate top rate-drop from 35% to 15%; pass through business income top rate of 15% (in the first Trump plan); and
- Transfer tax: "repeal the death tax, but capital gains held until death and valued over $10 million [presumably that is per couple] will be subject to tax to exempt small businesses and family farms. To prevent abuse, contributions of appreciated assets into private charity established by the decedent or the decedent's relatives will be disallowed." (The last sentence presumably would eliminate the charitable deduction for gifts of appreciated assets to a private foundation created by the donor or the donor's family.) [Observe: That phrase about carryover basis or realization at death has not been repeated in any of the Trump administration's summary proposals about repealing the estate tax.]

  The proposal does not clarify whether the $10 million exemption is applied per couple or per individual. Also, the proposal is not clear as to whether it would impose capital gains at death or merely establish a carryover basis on gains. Informal reports are that the Trump campaign confirmed for one inquirer that the intent was to propose a carryover basis approach, not realization at death.

  Interestingly, Hillary Clinton also announced a rather startling proposal on September 22, 2016 regarding transfer taxes *and* gain realization for gifts and

UT LAW CLE THE UNIVERSITY OF TEXAS TEXASLAW

Find the full text of this and thousands of other resources from leading experts in dozens of legal practice areas in the UT Law CLE eLibrary (utcle.org/elibrary)

Title search: Planning in a Period of Uncertainty, Including Using Defined Value Clauses

Also available as part of the eCourse
2017 Stanley M. Johanson Estate Planning eConference

First appeared as part of the conference materials for the
2017 Stanley M. Johanson Estate Planning Workshop session
"Planning in a Period of Uncertainty, Including Using Defined Value Clauses"