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SPOUSAL LIFETIME ACCESS TRUST "SLAT"

Securing the Tax Credit Exemption

The 2018 Tax Reform Act has increased the estate and gift tax exemption to $11.2 million per person from the current $5.6 million. Under the tax act it is due to "sunset" at year end 2025, and reverts back to the current level. Whether or not this will remain or revert is a political issue and therefore uncertain.

To secure the exemption a common estate planning concept is the "SLAT". With a SLAT, one spouse (donor-spouse) makes a gift to an irrevocable trust using the donor-spouse's gift tax exemption. The SLAT names the non-donor spouse (beneficiary-spouse) as a current beneficiary, which allows the trustee to make distribution of trust funds to the beneficiary-spouse during his or her life. Unique to a SLAT is the ability to remove the assets from estate tax inclusion, while still having lifetime enjoyment of the SLAT assets.

SLATs, by their very nature (i.e. benefiting the grantor's spouse), are taxed as grantor trusts for income tax purposes. Thus, the grantor bears the income tax burden on trust earnings. This permits the trusts to effectively grow tax-free, thereby enhancing the estate tax and asset protection benefits.

SLAT's can include provisions that create potential opportunities for your spouse to remove/receive assets from the trust without causing him/her to be treated as their owner for tax purposes. The trust won't provide these opportunities to any other beneficiaries during your spouse's lifetime.

Your spouse may be given some opportunities to take money out of the trust without anyone else's consent. They include an annual option to receive all of the trust's income, and an annual option to withdraw the greater of $5,000 or 5% of the trust's assets.

If the trustee is "independent" he/she/it can be given unlimited discretion to distribute trust assets to your spouse. In fact, an independent trustee's discretion could potentially be used to distribute ALL the trust's funds to your spouse, and for this reason SLAT's have sometimes been referred to as the "Family Bank Trust".

When funding a SLAT, it is important that the grantor use his or her own separate property. SLATs can provide meaningful asset protection from potential claims of creditors and other predators.

Giving up control of one's assets is not easy and a SLAT does have its risks. It requires a particular conviction in the enduring nature of one's marriage. Divorce removes even indirect access to the property in the trust and could also mean supporting one's estranged spouse for life. However, there is a remedy as the SLAT can be written so that the spouse is a general term and not a specifically identified person.

Where there is a desire to create two SLATs the caveat to the strategy is the "reciprocal trust" doctrine which essentially states that if Person A creates a trust for B, and B creates an identical trust for A, that the courts can "uncross" the trusts and treat the situation as though each person created a trust for his/her own benefit. Careful drafting and planning can avoid this.

In the event the spouse dies prematurely the trust assets would pass to the next generation (children) and the donor-spouse would then lose the benefits of the trust income and assets. Typically, a properly designed life insurance strategy between donor and trust can result in the replacement of the asset loss, additional estate tax reductions, as well as providing additional lifetime tax-free income for the donor-spouse.