ADVANCED ESTATE PLANNING

Some clients can benefit from more complex estate planning strategies. There are a number of trusts that you can establish to help achieve your wealth transfer goals. Below is a basic description of some commonly utilized strategies.

BYPASS TRUST

A bypass trust is typically created through a provision in the grantor's living trust or will. The goal of a bypass trust is to utilize the grantor's full estate exemption by placing a portion of the grantor's assets (usually an amount equal to the federal estate exemption) into the bypass trust at the time of the grantor's death. Often, a surviving spouse will act as trustee and receive income from the trust for the remainder of their lifetime. They can also invade the principal if necessary. The balance of the trust remaining at the second spouse's death then passes to their designated heirs free from estate tax.

- **Removed from the spouse's gross estate** – The bypass trust is not included in the surviving spouse's gross estate, even if the trust increases in value during the surviving spouse's lifetime. Placing appreciating assets in the bypass trust can allow you to ultimately transfer a larger amount of wealth to your heirs tax-free.
- **Taxation** – The bypass trust will be a separate entity. All income and capital gains are taxed to the trust and not to the surviving spouse.

Many states (including Oregon) also impose an estate or inheritance tax. The use of a bypass trust can help minimize state taxes regardless of whether your estate is taxable at the federal level.

QUALIFIED TERMINABLE INTEREST TRUST

A qualified terminable interest trust (QTIP) is often utilized when the grantor wants to ensure specific heirs receive trust assets after the surviving spouse's death. Income from the trust is paid to the surviving spouse and any remaining value is included in the surviving spouse's gross estate at death.

- **Blended families** – Often a grantor's goals include providing for a current spouse but also protecting the inheritance of his/her children from a previous marriage. The QTIP trust creates this flexibility by providing the surviving spouse with income during their lifetime but allowing the grantor to control the beneficiary designation.
- **Reverse QTIP election** – If the grantor wishes for the remainder beneficiaries to be grandchildren, the generation-skipping transfer tax (GSTT) would usually apply. However, if the grantor's personal representative makes a reverse QTIP election on the estate tax return, the trust can take advantage of the grantor's GSTT exemption at the surviving spouse's death. Assets valued at or below the exemption amount can be transferred to the skip generation free of GSTT.

IRREVOCABLE TRUST

An irrevocable trust can be employed by clients who wish to take advantage of their lifetime gift exclusion but do not want their children or grandchildren to receive the gifted assets outright. In order to restrict the timing of asset distributions, an irrevocable trust can be created with the children and/or grandchildren as the beneficiaries.

- **Completed Gift** - When the trust is funded, a completed gift is made (it is irrevocable). The designated trustee manages the trust assets and makes distributions to the beneficiaries according to the terms of the trust.
- **Growth** – The trust assets can increase in value above the initial gift amount and there is no additional gift tax due from the grantor. The trust is taxed as a separate entity for income and capital gains.

IRREVOCABLE LIFE INSURANCE TRUST

An irrevocable life insurance trust (ILIT) is used to remove life insurance proceeds from the value of the grantor's estate, while still providing liquidity for beneficiaries or estate taxes. If you retain any incidents of ownership in the policy (or have owned the policy within the prior three years) the value of the policy will be included in your gross estate. For clients with taxable estates, it is often advantageous to move these life insurance policies outside of their estate to reduce or eliminate any estate tax liability. At the grantor's death, the life insurance proceeds are received by the named beneficiaries tax-free and can be used to pay estate tax liabilities without other estate assets being sold.

- **New policies** – If a new policy is being purchased, cash would be gifted to the ILIT and the trust would purchase the policy. The beneficiaries (usually the grantor's children) are given Crummy Powers annually that allow them to remove a certain amount of assets from the trust each year. Beneficiaries usually choose not to exercise this power and the cash is then used to pay the annual policy premiums. It is also important to note that the three year rule would not apply since the grantor would not have any incidents of ownership.
- **Existing policies** – Existing life insurance policies can also be gifted to the ILIT. The value of the gift for tax purposes is the cash surrender value at the time of transfer. The insured must also live at least three years after transferring a policy to the trust.

The ILIT will be the primary beneficiary of the life insurance policy. Once the insured dies, death benefits will be paid to the trust and administered according to the terms of the ILIT. Any trust assets remaining at the surviving spouse's death will be transferred to the named beneficiary and avoid estate tax.

CHARITABLE REMAINDER TRUST

A charitable remainder trust is established by clients who wish to leave a portion of their assets to a qualified charity. This is an irrevocable trust; once funded the grantor cannot revoke the trust. The grantor will receive an income stream annually from the trust and the remainder beneficiary is the charity.

- **Customized income stream** - The income stream can be customized in amount and term. Income can be provided for a certain number of years, for life of the grantor, or for the life of multiple recipients.
- **Tax deduction** - At the time the trust is funded, the grantor will receive a charitable tax deduction for the present value of the remainder interest.

There are two ways you can receive income from the trust: a fixed amount or fixed percentage of trust assets. If you have a charitable remainder annuity trust (CRAT), you receive a fixed dollar amount from the trust each year. This approach will allow you to receive the same amount even if the trust assets generate less income than anticipated. If you have a charitable remainder unitrust (CRUT), you receive a fixed percentage of the trust assets each year. This method will allow you to receive more or less income depending on the performance of the trust. In either event, you are required to receive at least 5% of the trust's value each year.

GRANTOR RETAINED TRUST

With a grantor retained trust, the grantor transfers property to a trust but retains certain rights to the property (usually an income stream). After the income period is over, trust assets are distributed to the designated beneficiaries. If the grantor dies during the trust term, the assets will be included in the grantor's gross estate. However, if the grantor survives the trust term, the assets will be excluded from the grantor's gross estate.

- **Taxable gift** – The present value of the property transferred to the trust minus the retained interest is considered a taxable gift in the year the trust is funded. This reduces the grantor's lifetime gift exclusion amount.
- **Trust variations** – There are many variations of grantor retained trusts. Grantor retained annuity trusts (GRAT), grantor retained unitrusts (GRUT), grantor retained interest trusts (GRIT) and qualified personal residence trusts (QPRT) are all examples of grantor trusts. A discussion of your goals and objectives will help us determine which type of grantor trust might be suitable for you.

FAMILY LIMITED PARTNERSHIP

A family limited partnership (FLP) is a partnership with a general partner and at least one limited partner. Typically, the general partner is the senior family member who transfers business ownership or investment assets to the partnership. The general partner remains in control of the business or investment assets. The FLP provides creditor protection for the limited partner(s) but not for the general partner.

- Gifting Interests – The general partner is able to make substantial gifts of limited partnership interests while still maintaining control of the partnership assets.
- Discounts – When limited partnership interests are gifted, a discount is usually applied due to the lack of control and lack of marketability of the limited interest. This allows the general partner to leverage the size of the gift, which reduces the transferor's gift and estate tax liability.
- Tax Considerations – The FLP is a pass-through entity. This allows the shifting of business income and future appreciation of the assets to other members of the family who may be in a lower tax bracket.

PLANNING

Many of these strategies can result in the reduction of transfer taxes while also achieving complex wealth transfer goals. We can help you determine the best combination of strategies for you and your family. We will also partner with your estate planning attorney to help you implement your estate plan. Additional strategies are also available and will be discussed if applicable to your specific situation.

This is an informational fact sheet and is not intended to be a specific recommendation. If you are interested in exploring these strategies to see if they are applicable to your specific situation, please contact us. The information contained in this fact sheet is accurate to the best of our knowledge.