About the Author

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The author of over 40 articles for various tax and estate planing professional publications, Jim incorporates the analysis of all of these articles here, and adds forms which the attorney may consider in responding to his or her clients' estate planning goals and needs.

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Chapter 1

The Goal of Optimum Estate Planning

The word "optimum" means "most likely to lead to a favorable outcome." And in the estate planning context, that favorable outcome is for our clients to be able to have their cake, and eat it too. Clients want to minimize taxes for themselves and for their families, but they also want to protect their assets from lawsuits and to retain as much control as possible - both in themselves and in their family members. The objective of optimum estate planning is to create conditions for our clients which will most likely achieve all of their estate planning goals, not just some or most of them.

Too often today we are forced to "settle" as estate planners. For example, ever since 1986 Congress has imposed unfair and outrageous income taxes on trusts, so for this reason we tend either to use trusts less often or, when we do utilize them, direct in the trust document that all trust income be distributed to the trust beneficiary. This is often contrary to the clients' wishes that the unused income of the trust be controlled and protected from estate taxes, lawsuits, rights of a divorced spouse or of a spouse the beneficiary may remarry,

minor, young or otherwise spendthrift children, special needs children, etc., as well as from all issues associated with second marriage situations.

We also avoid establishing protective trusts for a surviving spouse or children because Congress tells us that the underlying assets of these trusts will not receive a "stepped-up income tax basis" at the spouse or other beneficiary's death. Is this even true? The surviving spouse in a community property state receives a full income tax basis step-up when the first spouse dies, but surviving spouses in non-community property states do not. Can something be done about this unfairness?

The growth in a non-qualified portfolio of investments escapes income tax in the hands of the heirs after the owner's death, but the recipients of IRAs and other forms of qualified plan benefits and non-qualified annuities not only pay income tax on the same after the owner's death, but they do so at ordinary (normally higher) income tax rates. Again, is there any way to avoid this unfairness?

Through the release of several private letter rulings the Internal Revenue Service steers planners towards leaving all IRA and qualified plan benefits either outright to individuals, or to so-called "conduit trusts" (which basically amount to the same thing as outright, in the long run), even though the owner's preference may be that these amounts be protected for his or her spouse and/or children. Is there any way to achieve the owner's objectives that these benefits be eligible for income tax deferral and also be protected from lawsuits and estate taxes?

An individual receives a charitable income tax deduction when he or she donates to charity during his or her lifetime, but generally there is no income tax deduction when he or she donates under his or her will? Is there a way to obtain a deduction?

When an individual makes lifetime gifts to his or her children of an interest in a closely-held business or real estate, the children take the donor's income tax basis in the same, yet when the same individual gives the stock or real estate to his or children at death, the children receive a "stepped-up" income tax basis. Is it possible to receive an income tax basis step-up for business and real estate interests which are gifted to children during the donor's lifetime?

And is it possible to transfer control over the clients' business to their children, but retain in the clients the ability for them to change their minds?

These are just some of the examples of the myriad of unfair tax laws and traps in the estate planning area which this book is intended to address, and then solve. Although as mere advisors we hesitate to cast invectives at Congress and the Internal Revenue Service when they seem to be continually "out for" our estate planning clients and their families, our reticence should not prevent us from taking positive action to estate plan around this inherent unfairness.

We don't need to act as legal sans-culottes, but we do need to avoid a state of indifference in our planning and drafting. As mentioned at the outset of this chapter, we want our clients to "have their cake, and eat it to." We want them to enjoy all of the estate planning benefits of trusts which are

available under the law, while minimizing all of the potential negatives.

Optimum estate planning also means that our estate plans today need to be flexible. The one thing we all learned over 15 years ago, with the passage of President's Bush "estate tax repeal bill" in May of 2001, was that the future of the estate tax laws were no longer certain, and that, through the use of independent trustees or trust protectors, our trust documents now needed to incorporate flexibility to deal with future tax law and other changes. The results of the 2016 Presidential, Senate and House elections serve only to heighten the need for flexibility in our estate planning, given the now very real possibility of federal estate tax repeal in the not too distant future.

Finally, optimum estate planning is also about retaining control for our clients, both during their lifetimes and after their deaths, as well as for the clients' children at an appropriate time after the clients' deaths.

This is an intermediate level book intended for the experienced estate planner who has become frustrated in not being able to accomplish all of his or her clients' estate planning objectives within a single estate plan. Asset protection and preservation concerns must be sacrificed in order to lower income taxes, while income tax savings must be sacrificed in order to protect and preserve assets. It's all become a vicious circle, due primarily to the punitive manner in which Congress has chosen to tax trusts.

In short, optimum estate planning concerns itself with achieving *all four* of these desirable results, but with no risk,

and with a minimum level of complexity:

- **Asset protection** - both during the client's lifetime and for the client's heirs after his or her death.

- **Income tax protection** - both during the client's lifetime and for the client's heirs after his or her death.

- **Estate tax protection** - both at the client's death and at the death of the client's heirs.

- **Maximum control** - both for the client and for the client's heirs.

A simple example involving the spousal portability election (also discussed later in Chapter 3) will illustrate. Because of the election, it is often said that traditional bypass or credit shelters trusts are no longer necessary, nor advisable. The trusts are not necessary because the surviving spouse already receives the deceased spouse's unused estate tax exemption, and they are not desirable because the trust is taxed at high income tax rates and further the assets of the trust will not receive an income tax basis step-up at the surviving spouse's death.

The problem with this approach to estate planning for married couples is that it is risky, and inaccurate. One significant concern with relying on the spousal portability election - at least in potential taxable estate situations - is that the surviving spouse loses the portability amount if he or she remarries and his or her new spouse again predeceases.

Relying on the portability election also exposes the "ported" assets to the surviving spouse's creditors, including the potential claims of a new spouse. Even more concerning is the fact that assuming all of this increased risk is oftentimes unnecessary. As we will discuss in Chapter 3, it is actually possible to structure a bypass or credit shelter trust so that its income is not taxed at a high rate, and also so that income tax basis step-up at the surviving spouse's death is achieved.

The surviving spouse would thus have control over and an economic interest in the bypass or credit shelter trust's principal and income, as trustee and beneficiary, but the trust corpus and income will now be protected from potential creditor claims against the survivor, as well as from potential claims by a new spouse. The trust assets are *guaranteed* to be removed from the survivor's taxable estate, and with little or no potential adverse income tax consequences as compared to proceeding under the portability election route. The decedent spouse also retains a level of control regarding the ultimate disposition of the trust assets. All is accomplished with zero risk and only a minimal level of added complexity.

This book with not inundate the experienced estate planner with basic concepts he or she already utilizes on a daily basis. Rather, for the most part at least, this text is intended to provide the reader with some "fresh perspectives" on how he or she might go about applying all of the above-outlined principles to develop an optimum estate plan for his or her client, in all of the most common estate planning situations, e.g., planning for married couples, planning for children and other non-spouse beneficiaries, planning for retirement benefits, planning for business owners and professionals, and lifetime gift planning.