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## SPOUSAL LIFETIME ACCESS TRUST (SLAT)

One very effective type of trust which married couples should consider for minimizing the imposition of federal estate taxes upon the death of the second spouse to die is a Spousal Lifetime Access Trust (SLAT).

Through the establishment of a SLAT, the creator of the SLAT (which is commonly called the Grantor) would be making a completed gift to fund the trust. The SLAT would typically be structured so that the assets comprising the trust would be used for the benefit of the Grantor's spouse as well as for the benefit of others, such as the children and more remote lineal descendants (e.g. grandchildren and great grandchildren of the Grantor). Moreover, the spouse can be provided with a testamentary non-general power of appointment exercisable by that spouse's Will, should the spouse predecease the Grantor, whereby the spouse would be able to direct that SLAT is to be maintained for the benefit of the Grantor for the balance of the lifetime of the Grantor.

A SLAT can be funded with any type of asset appropriate for a trust, such as marketable securities, real estate, cash or even life insurance on the Grantor's life. Many Grantors, however, prefer to fund these trusts with equity interests in closely-held entities, income producing stock or real estate, which typically require an appraisal to determine the value of the gift. The Grantor will file a United States Gift (and Generation-Skipping Transfer) Tax Return (IRS Form 709) reporting the completed gift, which will start the three (3) year statute of limitations running, commencing upon the later of the due date of that return or the date the return is filed, for the IRS to challenge the valuation of the assets gifted to the SLAT. Depending on the nature of the asset gifted to the SLAT, the value of the gifted assets can be discounted to reflect gifts of a minority (non-controlling) interest as well as due to a lack of marketability. The gift can be structured to use the Grantor's remaining lifetime gift exemption and under the correct circumstances, to allocate Generation-Skipping Transfer Tax exemption (which also equals the lifetime gift exemption in 2021) to allow the assets comprising the SLAT to escape being subjected to federal estates upon the death of your children or even more remote descendants. Because of how the SLAT may be structured, the SLAT assets and any appreciation in the value of such assets will be excluded from the gross estates of both the Grantor and the Grantor's spouse at death. Moreover, with proper planning, the assets comprising the SLAT can also be

excluded from the gross estate of your children, grandchildren, and even more remote descendants.

SLATs are taxed as Grantor trusts for income tax purposes because the SLAT is held for the benefit of the Grantor's spouse. Therefore, the Grantor will pay the income taxes on income earned by the SLAT, thereby, in essence, making an additional tax-free gift to the trust's remainder beneficiaries because the value of the assets comprising the SLAT will not be diminished by the income taxes on the income earned by the SLAT from time to time.

Under the Grantor trust rules, we frequently draft SLATs to include "swap" or "exchange" powers, which permit the Grantor to exchange (or buy) assets owned by the SLAT assets and "substitute" in the SLAT assets of an equivalent value as provided in Section 675(4)(c) of the Internal Revenue Code of 1986 (the "Code"). This is an estate tax neutral transaction, as the same value remains in both the trust and Grantor's estate. The appreciated assets purchased by the Grantor, will qualify for an income tax basis step-up at the death of the Grantor, thus eliminating the unrealized appreciation in the assets held in the SLAT. These powers, therefore, can provide significant flexibility to maximize income tax basis goals.

To maximize the flexibility of a SLAT, you should consider having an independent trustee. My use of the term *independent trustee* means an individual or financial institution having trust powers who is not a beneficiary of the trust and who is not related or subordinate to the Grantor within the meaning of Section 672(c) of the Code. A person is considered related or subordinate if such person is the spouse of the Grantor (if such spouse and the Grantor or living with one another), the parent, descendant (child, grandchild, great grandchild, etc.) or sibling of the Grantor, or an employee of the Grantor or a business in which the voting equity owned by the Grantor and the SLAT are considered significant, or a subordinate employee of a business in which the Grantor is an executive. Otherwise, trust distributions should be subject to an ascertainable standard, such as distributions for a beneficiary's health, education, maintenance, or support only (commonly referred to as a "HEMS standard"), thus the lack of flexibility.

Please note that the Grantor and adult beneficiaries of a SLAT can be provided with the power to remove and replace the trustee with another independent trustee.

Moreover, equity interests in a business entity (corporation, limited liability company, limited partnership, etc.) are conveyed to a SLAT, the business entity can still be managed by the Grantor or family members of the Grantor.

Furthermore, the trust agreement governing the SLAT can provide for the appointment of an investment agent, which could be the spouse of the Grantor.

With respect to the establishment of a SLAT, the Grantor may gift assets to the SLAT, sell assets to the SLAT or gift some assets to the SLAT and sell some assets to the SLAT. Because the SLAT is a grantor-type trust for federal income tax purposes, no gain or loss is recognized on a sale by the Grantor to the SLAT created by the Grantor.

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