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**Estate Planning For The 2020 Election Should Start In 2019: Planning Procrastinators May Lose**

[**Martin Shenkman**](https://www.forbes.com/sites/martinshenkman/)Contributor <https://www.forbes.com/sites/martinshenkman/2019/10/12/estate-planning-for-the-2020-election-should-start-in-2019-planning-procrastinators-may-lose/#74193dfb2ae9>

[Retirement](https://www.forbes.com/retirement) *I write about charitable giving and estate planning ideas.*

Don't close your eyes to planning. Waiting to do estate planning until after the 2020 election could be a mistake.

**Waiting to See What Happens in 2020 May be Unwise**

No one can predict the 2020 election but if the Democrats sweep seems pretty likely harsh estate tax, and perhaps wealth tax, legislation will follow. Smart folks, and not just the uber wealthy, are planning now. Most folks are planning procrastinators. “Let’s see what happens with the election.” “If the Dems win let’s see if they can even pass an estate tax law.” Wait and see may prove to be more like “You snooze you lose.” Let’s consider why:

·      What might the effective date of new legislation be? Might the effective dates result in your planning not working? For example, often new legislation permits existing plans, say a trust, to be respected (called “grandfathered”) if new legislation is enacted. But what date will be selected? Its smarter to get our planning in place now as it may increase (but not guarantee) the odds of it being effective.

·      There are distinct advantages to doing planning over a longer period of time. So planning now, in 2019, may not only increase the likelihood of your planning working, but it may make your planning less risky or more secure. That is the focus of the discussion following.

**Start Planning in 2019 to Make Planning Safer**

For many planning techniques time is your friend. If you have more time to implement a plan, that plan might be safer.

**Wait and See Example**: Jane is single and a physician. Although she is very careful in all she does, she always stresses over the risks of malpractice concerns. Her estate is worth about $4 million. Jane realizes that her estate is likely to grow over her future working years, and her investments will also grow, so that under the $3.5 million exemption the Dems have proposed she is worried she will face an estate tax.  She has a modest retirement account, a $500,000 condo and say $3.5 million in investment assets.  If the Dem proposals are enacted the gift tax exemption could be reduced to $1 million from the current $11.4 million. That could make it very difficult for Jane to move assets out of her estate into a protective trust. Jane could wait and see. So, if the Dems win in 2020 and propose new estate tax legislation she could begin exploring the planning process in early 2021. She might then set up a self-settled domestic asset protection trust. That is a trust of which Jane is a beneficiary. This is critical to Jane since as a single individual she needs to rely on herself for her financial security and she may need access to the assets she transfers to that trust.  Jane will have to rush through the planning if that happens, compress the time to complete work, perhaps short cutting some of the steps she takes. That could make the success of her plan riskier. Further, with limited time Jane will have to transfer the assets she wants to protect into the trust at one time. Say that amount is $2.5 million of her $3.5 investment portfolio. That is a large single transfer and may expose her to greater risk of a claimant arguing that the $2.5 million transfer was a fraudulent conveyance. That means that she transferred the assets to hinder, delay or defraud a creditor. That could jeopardize her entire plan.

**Start Planning Now Example**: Jane consults with her professional advisor team now. She weighs the benefits of waiting versus starting her planning now in 2019. The most compelling factor she realizes is that she is concerned about malpractice exposure far more than estate tax risks and that the longer she waits to plan the longer her assets will be at risk. Her advisers also helped her understand that by planning now, in 2019, she might reduce the risk of a fraudulent conveyance challenge that she faced in the wait and see approach. So Jane sets up a self-settled domestic asset protection trust (“DAPT”) in October 2019. Before any assets are transferred she has her CPA create a personal balance sheet showing that she is solvent and will remain so even after all planned transfers. Jane’s wealth adviser creates a financial forecast showing how Jane’s wealth with grow over the years, and how, that even with the planned transfers to her trust, she will continue to have adequate resources for any possible needs. Jane, because there is ample time (in contrast to the last minute rush that might occur if she waits to see what happens) Jane’s lawyer has lien and judgement searches completed to corroborate that there are no current known claims. All of this might help deflect a later challenge by a creditor.  Jane also opts to fund the trust with gifts of $150,000 per month starting in November 2019. By March 2021 when it is anticipated that if there is a Dem sweep they might have tax legislation in the hopper, Jane will have gifted to the trust $150,000 x 17 months = $2,550,000. But these gifts will have been made in small increments over 17 months. Perhaps midway through the process Jane has her advisers update all of the protective steps outlined above as that may further enhance her ability to deflect a later challenge that she endeavored to defraud a claimant. This all may enhance the potential for Jane’s plan succeeding for both tax and asset protection purposes.

Bottom line, planning now, may make your planning safer and more effective.

**Reciprocal Trust Doctrine Challenge Might be Deflected By Starting Your Plan in 2019**

**Example**: A couple wants to create spousal lifetime access trusts (“SLATs”) to which each will gift $2 million to use some of their temporary exemption before it might be reduced by future legislation. The rationale for this plan is that each of the spouses may be a beneficiary of the trust the other spouse creates (and if appropriate all their descendants and others as well).  That might be a great plan in that it may provide asset protection from creditors, remove the gifts and all future appreciation from your estate, and yet you still may have the ability to access the assets given away. But there is a risk that you face when spouses create SLATs for each other. Starting your planning in 2019 may help you reduce this risk.

The creation of SLATs by one spouse for the other may raise the issue of what is called the “reciprocal trust doctrine. Under this doctrine, if the first spouse creates a trust for the second spouse, and the second creates a nearly identical trust for the first, then the two trusts will “un-crossed” and treated for tax purposes (and perhaps even for asset protection purposes) as if each spouse had created a trust for himself or herself. The logic behind this treatment is that reciprocal trusts leave the two settlors in approximately the same economic position as they would have been if they had created trusts naming themselves as life beneficiaries The plan will fail.

How Can You Reduce The Risk Of A Reciprocal Trust Challenge?

Consider steps to make each trust and plan different. Some of the following might all help.

·      The spouses should not be in the same economic position following the creation of the two trusts.

·      Incorporate different distribution standards in each trust.

·      Use different trustees.

·      Give one spouse a special power of appointment, but not the other in the second trust.

·      Have each trust give the spouse/beneficiary different powers of appointment in each other’s trusts. These are rights to appoint trust assets. For example, give spouse one the broadest possible special power of appointment, and spouse two a more limited (a so-called “special” power of appointment) exercisable only in favor of a narrower class of permissible appointees, such as issue.

·      Vary the beneficiaries between the trusts. For example, add your mother-in-law as a beneficiary of your trust but not of your spouse’s trust.

·      And here’s the big reason to start your planning in 2019 and not wait. Create the trusts at different times. In one court case, Lueders’ Estate v. Commissioner, the husband and wife each created a trust for the other spouse, but the trusts were created 15 months’ apart. The court  held that there was no consideration, or quid pro quo, for the transfers.

**Example**: Spouse 1 creates a trust for spouse 2 in November 2019. The trust gives spouse 2 a limited or special power to appoint assets to a limited class of people. The trust was formed in Nevada with an institutional trust company based in Nevada. The assets given to the trust included life insurance, securities and an interest in a family business. Spouse 1’s mother is named a beneficiary. In October 2020 Spouse 2 creates a trust for spouse 1. The trust gives spouse 1 a broad limited or special power to appoint assets to anyone other than Spouse 1, Spouse 1’s creditor, estate or estate creditors. The trust was formed in Alaska with an institutional trust company based in Alaska. The assets given to the trust included only securities. Spouse 1’s mother is not named a beneficiary. While a number of steps were taken to differentiate each trust from the other, an important distinction might be having create the trusts 11 months apart and also in different tax years. If you wait until after the election both trusts might be created in 2021 on the event of new tax legislation being enacted. You might also lose the flexibility to separate the creation and funding of the trusts with much time. Plan now!

**Step-Transaction Challenge Might be Deflected By Starting Your Plan in 2019**

The step-transaction doctrine might be applied by the IRS to torpedo a wide range of tax planning techniques. The concept is based on the idea that if you compressed several different steps into one, the result of what the transactions might achieve may be different (and worse for you as the taxpayer).

**Example**: Wife owns 100% of the shares of a Family Business valued at $25 million. Wife Transfers 50% of the shares to Husband on March 1, 2020 after a new administration in Washington proposes harsh new estate tax legislation. On March 2 Husband establishes a non-reciprocal spousal lifetime access trust (“SLAT”) for Wife. Wife establishes a non-reciprocal SLAT for Husband. On November 3, 2016 each spouse transfers a 35% non-controlling interest in Family Business stock to their respective trust. They value each 35% interest at $5,250,000 [$25 million enterprise value x 35% shares transferred x (1-.40 assuming a 40% aggregate discount for lack of control and marketability)]. There is a risk that the IRS may challenge this plan, on among other issues, a step-transaction theory. The IRS might assert that Wife actually funded both trusts and that there was no economic significance to the transfer from Wife to Husband followed by a transfer from Husband to his SLAT. The IRS might argue that if the various steps are aggregated the net result is equivalent to the Wife having gifted the stock to both trusts. The concept underlying the step-transaction doctrine is that the stock merely passed through Husband’s hands as part of an overall transfer plan by Wife.

Certainly the longer the time span between each step or component of a plan, the more each step in a plan can stand independently on its own. So if you are planning such transactions make the equity transfers now so that there is an opportunity for more time to pass before other transfers are consummated. If wife gave husband shares in November 2019, and Husband does not fund his SLAT with the shares until December 2020, that is both time and a tax year intervening between the steps. If instead you wait until legislation is proposed after the election (assuming a change in control in Washington) there may be inadequate time to militate against a step transaction challenge.

Other factors might affect the application of the step-transaction doctrine.

·      Are there independent economic events that occur between transfers? A loan negotiated with a third party lender, a dividend declared, a new shareholders agreement negotiated and signed, may be relevant.  The more events that occur, the more significant and independent they are, the more the facts might deflect such a challenge. The more time between Wife’s gift to Husband and Husband’s later gift of the stock to his trust the greater the opportunity for events of independent economic significance to occur. So, plan now, don’t wait.

·      If there is a binding commitment from the outset to undertake each step in a plan the application of the doctrine might be more likely.

·      If the IRS can demonstrate that the various steps are really pre-arranged parts of a single transaction that may be used to challenge the plan.

·      The IRS may evaluate each step and try to demonstrate that certain steps are meaningless unless all other steps occur.

Again, the bottom line remains that it may be quite advantageous to begin your planning now, not to wait.

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[**Martin Shenkman**](https://www.forbes.com/sites/martinshenkman/)I am an estate planning attorney, author of 42 books, and more than 1,200 articles. I serve on the editorial boards of Trusts & Estates Magazine, CCH (Wolters Kluwer) Professional Advisory Board, CPA Magazine, and the CPA Journal. I’m active in many charitable and community causes and organizations and spend two months/year traveling the country educating professional advisers on planning for clients with chronic illness and raising both awareness and funds for many charities helping people face the challenges of chronic illness. I serve on the board of the American Brain Foundation Board, and its Strategic Planning Committee, and Investment Committee. I hold a BS degree in accounting and economics from Wharton School, an MBA in tax and finance from the University of Michigan, and a law degree from Fordham University School of Law.