BESSEMER TRUST

ACTEC 2020 Summer Meeting Musings

June 2020 Meeting

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This summary reflects brief highlighted individual observations of Steve Akers from the seminars at the 2020 Summer Meeting and does not purport to represent the views of ACTEC as to any particular issues.

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Important Information Regarding This Summary
This summary is for your general information. The discussion of any estate planning alternatives and other observations herein are not intended as legal or tax advice and do not take into account the particular estate planning objectives, financial situation or needs of individual clients. This summary is based upon information obtained from various sources that Bessemer believes to be reliable, but Bessemer makes no representation or warranty with respect to the accuracy or completeness of such information. Views expressed herein are current only as of the date indicated, and are subject to change without notice. Forecasts may not be realized due to a variety of factors, including changes in law, regulation, interest rates, and inflation.

Introduction

Some of my observations from the 2020 ACTEC Summer (Virtual) Meeting Seminars on June 22-25, 2020 are summarized below. The seminars were available online to meeting registrants. (At the request of ACTEC, the summary does not include any discussions at Committee meetings.) This summary does not contain all of the excellent information from the seminars, but merely includes selected issues. The summary is based on the presentations at the seminars, but the specific speakers making particular comments typically are not identified.

Items 1-7 are observations from the seminar at the Summer Meeting: Insecure about SECURE? More on Retirement Planning and Trusts with a Focus on Disabled and Chronically Ill Beneficiaries by Deborah J. Tedford and Steven E. Trytten

1. Overview of Beneficiary Planning Issues Under SECURE Act

Some of the following overview of planning implications of the SECURE Act is based on presentations and resources from Natalie Choate (Boston, Massachusetts) at the 2020 Heckerling Institute on Estate Planning. For a more detailed overview of changes in planning for beneficiary designations in light of the SECURE Act, see Item 3 of Heckerling Musings 2020 and Estate Planning Current Developments found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights**.

a. **Overview – Limits on "Stretch" Planning.** The SECURE Act (H.R. 1994, Setting Every Community Up for Retirement Enhancement Act of 2019) was signed by the President on December 20, 2019. The Act includes a number of provisions regarding retirement plans, but important for estate planners is that the SECURE Act:

- Changes the age that determines the required beginning date (RBD) for minimum distributions (April 1 of the following calendar year) from 70½ to 72, effective for individuals who reach age 70½ after December 31, 2019 (the effect is that no one will have his or her RBD in 2021); and
- Eliminates the prohibition on contributions to an IRA after age 70½ (but the $100,000 limit on qualified charitable distributions from an IRA would be correspondingly reduced [observe that changing the age for required minimum distributions from 70½ to 72 will not change the age at which qualified charitable distributions from IRAs will be permitted]). See Item 1.j below for a discussion about IRA charitable rollover planning.

Most important for estate planners, the SECURE Act **substantially limits "stretch" planning** for distributions from defined contribution plans (and IRAs) following the death of the plan owner (referred to as the "participant"). Under prior law, following the participant's death, plan benefits (including IRA benefits) could be paid over the life expectancy of a "designated beneficiary" (DB), to stretch the receipt (and, therefore, the income taxation) of retirement benefits, but the SECURE Act mandates that distributions to a designated beneficiary be made within 10 years following the death of the participant, with exceptions for five categories of "eligible designated beneficiaries" (EDBs). Distributions from the plan are typically taxed as ordinary income, so the ability to stretch the receipt of those benefits as long as possible defers the time that the income tax must be paid. (Throughout this discussion of the SECURE Act, references to a "plan" or "plan benefits" will include an IRA.)

b. **Brief Overview of Post-Death Minimum Distribution Requirements Under Prior Law.** A grasp of the prior law minimum distribution requirements following the death of the participant is essential to understand the impact of the changes made by the SECURE Act. Most of this prior law is retained under the SECURE Act (except for the 10-year rule for designated beneficiaries, with special rules for the five categories of eligible designated beneficiaries). The rules are based on regulations proposed in 1987 and 2001 and finalized in 2002, almost 20 years ago. A simplified summary of the prior law follows [provisions impacted by the SECURE Act are briefly noted in italicized comments in brackets].

The treatment varies based on whether or not the beneficiary is a DB, meaning any individual but not an entity such as the participant's estate, a charity, or a trust that is not a "see-through" trust (described below).

(1) **Beneficiary Not a Designated Beneficiary.** If the beneficiary is not a DB (Non-DB), benefits must be paid within 5 years if the participant died before his or her required beginning date (RBD) or over the participant's remaining life expectancy (this is sometimes referred to below as the "ghost LE") if the participant died on or after the RBD. [*This does not change under the SECURE Act*.] The RBD was April 1 of the year after the participant reached age 70½ [*changed to age 72 in the SECURE Act*].

(2) **Beneficiary Is a Designated Beneficiary Other Than a Surviving Spouse.** If the beneficiary is a DB and is not the surviving spouse, the benefits are paid over the DB's life expectancy (if a see-though trust is the beneficiary, over the oldest beneficiary's life expectancy). (If the participant's remaining life expectancy is longer, that period may be used. Reg. §1.401(a)(9)-5, A-5(a)(1).) [*The SECURE Act changes this to a maximum 10-year payout instead of the DB's life expectancy; whether the Act changes from allowing the participant's life expectancy if that is longer is unclear if the beneficiary is a DB*.]

(3) **Beneficiary Is the Surviving Spouse.** If the beneficiary is the participant's surviving spouse, the DB rule described above can apply (that would be applicable, for example, if the beneficiary is a standard QTIP trust that does not mandate that all distributions must pass to the spouse), but even more favorable alternatives may also be elected in some circumstances. If the spouse is the sole beneficiary, the Single Life Table is used, but the life expectancy is recalculated annually.

Better still (in most circumstances), if the spouse chooses to treat the decedent's IRA as his or her own IRA (spousal election) or elects to roll over the decedent's IRA into the spouse's IRA (a spousal rollover), several significant advantages result. (1) Distributions do not need to begin until the spouse reaches his or her RBD. (2) Distributions are made at a slower pace because the Uniform Life Table may be used (which is based on the joint life expectancy of the individual and someone who is 10 years younger). Under the new tables that apply beginning in 2021, the life expectancy of a 72-year old person under the Single Life table is 17.1 years, and under the Uniform Life table is 27.3 years, so using the Uniform Life table allows taking withdrawals from the plan at a substantially slower rate. (3) The surviving spouse can designate his or her own beneficiary, and at the spouse's death, the remaining benefits (which may be much reduced if the spouse has lived to near his or her life expectancy) may be paid over the life expectancy of a DB. [*The SECURE Act dramatically alters this third advantage.*]

See Item 7 below for further discussion of planning considerations for a spouse as beneficiary of plan benefits.

c. **Trust Recipients.** The trust rules described below have not been changed by the SECURE Act (but the importance of which category applies to a particular trust may be impacted dramatically by the SECURE Act.)

(1) **See-Through Trusts.** Although DBs must be individuals, trusts that meet five requirements are classified as "see-though trusts." The individual beneficiaries of a see-though trust are treated as DBs of the plan or IRA (with a special rule as to which such individual's life is used to determine the life expectancy payout period). The five requirements are: (1) the trust must be valid under local law; (2) the trust is irrevocable or becomes so at the participant's death; (3) the beneficiaries are identifiable; (4) certain documentation is provided to the plan administrator; and (5) all trust beneficiaries must be individuals (but "mere potential successor beneficiaries" don't count, which generally means that only the initial remaindermen are counted, not remote successor remaindermen). See Letter Ruling 202035010, discussing the requirements for a trust to be recognized as a see-through trust. While the individual beneficiaries are treated as DBs, two special rules do not apply for beneficiaries of a see-though trust – the trust cannot be treated as having separate accounts each having its own beneficiary, and spousal rollovers are not available for any trust, even a see-through trust.

Two types of trust that can qualify as see-through trusts if they meet the five requirements (including that all beneficiaries are individuals) are conduit trusts and accumulation trusts.

(2) **Conduit Trusts.** A conduit trust is the nickname (not formally called that in the regulations) of a trust that has one individual beneficiary, and the governing instrument requires that all plan or IRA distributions to the trust must be distributed from the trust to the individual beneficiary. The distributions are deemed paid "to" the individual beneficiary, and the beneficiary is considered the sole beneficiary of the trust and the plan or IRA for minimum distribution purposes, regardless who receives any benefits if the beneficiary should die before all plan assets have been distributed to the trust (and to the beneficiary). Conduit trusts are straightforward to draft; they just require that plan distributions to the trust are distributed forthwith to the single beneficiary.

(3) **Accumulation Trusts.** An accumulation trust is a trust that is not required to distribute all plan benefits as received, but permits the accumulation of distributions within the trust. All beneficiaries (except "mere potential successor beneficiaries") who might ultimately receive such accumulations are considered for purposes of the minimum distribution rules (and the oldest such beneficiary's life expectancy is used as the relevant payout period). These restrictions have led to considerable complexity in drafting accumulation trusts to assure that some older beneficiary or entity might not be a trust recipient, including under the possible exercise of a power of appointment.

d. **Overview of Changes; ACTEC Comments.** The SECURE Act minimum distribution provisions retain the current Code structure as much as possible. These provisions are in Section 401(a) of the SECURE Act (unfortunately, confusingly similar to the Section number of the Code (§401(a)) that contains the rules for qualified retirement plans).

Section 401(a)(9) of the Code contains the provisions about required distributions from qualified retirement plans (including IRAs). The SECURE Act adds a new §401(a)(9)(H), which includes six clauses.

- (i) and (ii) – **10-Year Rule for DBs, Except for EDBs.** These clauses say, rather obtusely with various cross references, exceptions, and special rules layered over the existing provisions, that if the beneficiary is a DB, the plan assets must be distributed within 10 years of the participant's death unless the beneficiary is an "eligible designated beneficiary" (EDB). A modified life expectancy payout applies as long as the beneficiary is an EDB.
- (iii) – **Death of or Otherwise Ceases to Be EDB.** If an EDB dies or otherwise ceases to be an EDB before the plan has been entirely distributed, the exception for EDBs will no longer apply, but the plan must be distributed within 10 years after such EDB's death or cessation as an EDB (even if the next successor beneficiary is an EDB at that time).
- (iv) and (v) – **Special Rule for Trusts for Disabled or Chronically Ill Beneficiaries.** Special rules apply to multi-beneficiary trusts if at least one of the beneficiaries is a disabled or chronically ill individual (these provisions are discussed in Items 4 and 6 below); and
- (vi) – **Applicable to Defined Contribution Plans, Not Defined Benefit Plans.** These rules apply to defined contribution plans (including IRAs and Roth IRAs), but not defined benefit plans, i.e., pension plans.

Section 401(a)(9)(E) is amended to describe five categories of EDBs.

Section 401(b) of the SECURE Act has effective date provisions. The provisions generally apply to plans and IRAs for which the participant dies after 2019, but some effects may result even when participants have died before 2020.

That's it. Otherwise, all the minimum distribution rules stay the same. The distribution rules have not changed if the beneficiary is not a DB. Determining if a beneficiary is a DB has not changed. The various trust rules (for what is a see-through trust, a conduit trust, or an accumulation trust) have not changed.

(1) **ACTEC Comments.** These provisions of the SECURE Act create many uncertainties. ACTEC filed comments with the IRS on July 14, 2020 and July 29, 2020 identifying various uncertainties and making various recommendations for IRS guidance. American College of Trust & Estate Counsel, Letters to Department of Treasury and IRS titled Request for Guidance from Treasury on Section 401 of the SECURE Act, Part 1 (July 14, 2020) and Part 2 (July 29, 2020). These extremely detailed comments include recommendations regarding various issues regarding (i) the 10-year rule and the effective date in Part 1, (ii) trusts for DBs other than EDBs, (iii) trusts for spouses, (iv) EDB issues generally, (v) minor child beneficiary and age of majority issues, (vi) disabled and chronically ill EDBs, (vii) applicable multi-beneficiary trusts, and (viii) the "not more than 10 years younger" EDB category in Part 2. The comments are available from the "Legislative and Regulatory Comments by ACTEC" webpage of the ACTEC website, found **here**.

(2) **Ten-Year Rule.** The SECURE Act applies its 10-year rule for making distributions to a DB by cross reference to the 5-year rule that applies for non-DBs (if the participant dies before his or her RBD), thus engrafting the body of regulatory law that applies for the 5-year rule. This has the effect of clarifying several issues.

(a) **Proportionate Distributions Not Required.** Distributions do not have to be made proportionately over the 10-year term; they could be made all in a lump sum at the very end of the term (which would have the effect of deferring recognition of the income, but would also result in "bunching" the income, possibly into a high income tax bracket). For Roth IRAs, deferral until year 10 would likely be the most effective strategy.

(b) **December 31 Due Date.** Distributions must be made by December 31 of the calendar year that contains the tenth anniversary of the relevant person's death. See Reg. §1.401(a)(9)-3, A-2. (Presumably that same December 31 due date will also apply to the new 10-year rule.)

(c) **Eleven Calendar Years for Payments.** The actual payout period could extend over 11 taxable years (if death occurs in 2020, the final payment must be made by December 31, 2030, so payments can be made in 2020-2030, or over 11 years). Spreading payments over more years increases the chances that lower tax brackets may apply.

(3) **Eligible Designated Beneficiaries.** New Code Section 401(a)(9)(E)(ii) describes the five categories of EDBs. They are (i) the surviving spouse, (ii) a participant's child who "has not reached majority," (iii) a disabled individual, (iv) a chronically ill individual, and (v) an individual not described above who is not more than 10 years younger than the participant. These beneficiaries qualify for a modified life expectancy payout.

Status as an EDB is determined at the participant's death. A DB who later satisfies one of the five categories of EDBs does not become an EDB for purposes of being able to use an adjusted lifetime payout rather than being subject to the 10-year rule. §401(a)(9)(E)(ii)(last sentence). (A special rule applies for minors – if the minor is disabled upon reaching majority, the minor exception continues through the period of disability.)

e. **Application of SECURE Act to Pre-2020 Deaths.** The anti-stretch provisions of the SECURE Act generally apply to participants who die after 2019, EXCEPT that if the initial DB dies after 2019 and before the plan assets have been totally distributed, the remaining benefits must be paid within 10 years of when such DB dies (even though the participant died before 2020). (Under prior law, when the DB died, the DB's beneficiary could continue to receive benefits over the DB's remaining life expectancy.)

The effective date provisions are unclear about what happens if the participant had multiple DBs. For example, the beneficiary may have been an accumulation trust with various individuals as permissible current or remainder beneficiaries, and each of them is a DB, even though only the oldest DB's life expectancy is used to determine the payout period. Does the 10-year rule kick in when the oldest DB has died? When any DB has died? Or when all of the DBs have died? Natalie believes the provision should be interpreted to say that the 10-year rule begins to apply only when all DB's have died (in part because the minimum distribution trust rules have no concept of a "primary"

beneficiary, just countable or non-countable beneficiaries). But Natalie notes, "My opinion is worth a lot to me, but I don't know how far it will get you."

f. **General Client Triage Approach.** The anti-stretch provisions of the SECURE Act are interesting in that they constitute a major broad tax change, but they affect everybody differently based on specific client situations and goals.

(1) **Little or No Impact.** The new provisions will have little or no impact on planning beneficiary designations in many situations.

- Many clients and their families have small enough plans and assets outside of plans that deferring the receipt of money otherwise available for living expenses is the least of their concerns.
- Most retirement plan beneficiaries are not making plan withdrawals only at the minimum rate permitted. The preamble to the proposed regulations containing the new life expectancy tables for determining life payout rates from retirement plans indicates that only about 20% of individuals required to take RMDs make withdrawals at the minimum required level. Most (or at least a substantial portion) of the remaining 80% of plan beneficiaries will not be affected by the SECURE Act's 10-year rule.
- For married couples, naming the surviving spouse as the outright beneficiary of the retirement plan is the most common arrangement. The same rules apply for the surviving spouse as in the past (except that the 10-year rule will apply as to any benefits still in the plan at the spouse's subsequent death, but the likelihood that substantial assets will remain in the plan after making life payments to the surviving spouse may be relatively small).
- If the participant has no surviving spouse, clients with substantial assets in retirement plans are likely to have adult (rather than minor) children and many individuals name their adult children as the outright beneficiaries of the plan assets following the deaths of both spouses (favoring simplicity over the benefits of trusts for receiving retirement benefits).
- A charity may be named as beneficiary, in which event the SECURE Act has no impact.

(2) **Emergency Impact.** For some clients, immediate emergency action is required. Individuals who have wanted to maximize the stretch planning may be using plans to stretch the receipt of taxable benefits over the life expectancies of young children or grandchildren. Those plans often entail naming a conduit trust for the young beneficiary, leaving the trustee and not the young recipient with the power to decide whether large withdrawals would be made from the plan. The individual likely anticipated that relatively small annual distributions would be made to the trust (and distributed from the trust to the beneficiary) annually. Instead, under the SECURE Act the entire plan value will be distributed within 10 years and distributed from the trust to the beneficiary (unless the beneficiary is an EDB). Natalie Choate's conclusion: "Almost invariably, conduit trusts will not work the way the client anticipated or wants."

(3) **Slight Tweaks Needed.** For some clients, relatively minor tweaks may be needed in light of the SECURE Act. For example, an individual might tweak the type of QTIP trust that is used for a surviving spouse. A classic QTIP trust (that does not mandate that all retirement plan distributions be distributed immediately to the surviving spouse) qualified for payout over the spouse's life expectancy under the old rules but would be subject to the 10-year payout requirement under the SECURE Act. An individual might prefer to tweak that plan to require the distribution to the spouse of all amounts received from the plan so that the QTIP trust would be a conduit trust and qualify for payments over the spouse's life expectancy (Single Life Table, recalculated annually).

Giving an independent trustee of an accumulation trust a broad distribution standard may facilitate the ability to make distributions to avoid taxing income at compressed trust tax rates.

If disabled or chronically ill persons are plan beneficiaries, tweaks may be needed if plan benefits are left to special needs trusts for them. See Item 6.c below. In addition, accumulation trusts may qualify for special treatment, without the need for conduit trust provisions.

g. **Conduit Trusts.** The use of a conduit trust as the beneficiary is especially sensitive under the SECURE Act.

(1) **Conduit Trusts Needed for Certain EDBs.** In some situations, using conduit trusts will be very important if a client wants to use a trust for a beneficiary – for example to qualify for EDB treatment (and a modified life payout) for a surviving spouse, a minor child of the participant, or someone not more than 10 years younger than the participant. (Accumulation trusts can be used for disabled or chronically ill individuals and still qualify for EDB treatment.)

If a conduit trust is used for a minor child of the participant, the planner should take into consideration that the entire account will have to be distributed outright to the child at the latest ten years after the child "reaches majority." The planner should weigh the advantage of the added period of deferral against the fact that all of the account would be distributed to the child within 10 years of reaching majority.

(2) **Conduit Trusts Will Not Generally Be Used in Other Situations; Can Be Disastrous in Some Situations.** In other situations, using conduit trusts may be disastrous. For example, if the client wanted to have benefits paid over the life of a young child, the client likely wanted to use a trust for the young beneficiary for management purposes. Conduit trusts were much simpler than accumulation trusts in the past because subsequent beneficiaries and permissible appointees are not relevant for purposes of determining the relevant life expectancy payout period. Conduit trusts were often used in the past because of their relative simplicity. (For example, if an accumulation trust were used and if the contingent beneficiary were older than the young beneficiary, the contingent beneficiary's life expectancy would have been used rather than that of the young beneficiary.) Under the SECURE Act all plan benefits must be paid within 10 years, and with a conduit trust, those benefits are paid immediately to the beneficiary. Therefore, the deferral advantage of using a very young beneficiary is largely lost (benefits must be distributed within 10 years regardless of the beneficiary's age), and all of the nontax benefits of trusts (including preserving assets, protecting from a beneficiary's squandering of the assets, and protecting from creditors) will be available for only up to 10 years. Using a conduit trust as the plan beneficiary for an individual beneficiary who is a spendthrift could lead to the individual's squandering funds after the plan and trust distribute all plan assets to the individual within 10 years.

Again, Natalie's axiom applies: **"Almost invariably, conduit trusts will not work the way the client anticipated or wants."** But conduit trusts can be helpful if they result in EDB treatment for the beneficiary with a payout over the beneficiary's life expectancy until the EDB status ends.

Locating and identifying clients with conduits trusts will be challenging. Firms do not keep track of clients who are using conduit trusts as plan beneficiaries. Contacting past clients with a message to contact the attorney if the client has a "conduit trust" will not work because most clients have no idea what a conduit trust is. (Furthermore, Natalie quips, "clients never read anything you send them anyway.")

h. **Accumulation Trusts Will Become More Common.** In most cases going forward (other than needing to qualify for EDB treatment for spouses, minor children, or beneficiaries not more than 10 years younger than the participant), plan benefits that are being paid to trusts will pass to accumulation trusts. The complexity of structuring accumulation trusts in the past is no longer applicable because the life expectancies of the primary beneficiary and successor beneficiaries are no longer relevant – plan benefits must be distributed within 10 years regardless. Hopefully regulations will eventually clarify that the oldest potential beneficiary or appointee under a power of appointment does not have to be identifiable. Excluding beneficiaries who are older than some specified age will no longer be necessary. The only requirement, for the trust to be a designated beneficiary, is that non-human beneficiaries are excluded as potential beneficiaries. (If the accumulation trust is not a designated beneficiary, the traditional non-DB rules apply.)

The terms of accumulation trusts perhaps can be simplified to delete complicated restrictions (for example to assure that no older beneficiaries are possible under the trust). Accumulation trusts going forward must merely prohibit any non-individuals as permissible beneficiaries. For example, Mickey Davis (Houston, Texas) indicates that unless future regulations provide otherwise, his trust forms for trusts designed to accept retirement plan benefits as an accumulation trust will remove references to age and life expectancies of beneficiaries and will provide in essence, "if I die before my RBD, or after my RBD when my life expectancy is less than 10 years, this trust will not have any entities as beneficiaries or permissible appointees." An alternative is giving a "trust protector" the authority to revise the terms of the accumulation trust by the September 30 "finalization date" of the year of the owner's death to eliminate unneeded restrictions in accumulation trusts based on IRS guidance available at that time.

IRS guidance eventually may clarify that the trust does not have to include provisions making it a non-DB to take advantage of a possible slightly longer payout that might be permitted for non-DBs, in case the participant dies after the RBD and has a remaining life expectancy longer than 10 years. Comments filed by ACTEC, described in Item 1.d.(1) above, recommend that Treasury allow a DB "to use the longer of the 10 Year Rule or the Deceased Employee's Remaining Life Expectancy Method, while preserving the existing At Least As Rapidly Rule for EDBs." ACTEC Letter to Treasury dated July 14, 2020, at 12-13, available from the "Legislative and Regulatory Comments by ACTEC" webpage of the ACTEC website, found **here**.

Having broad distribution standards with an independent trustee in accumulation trusts may be helpful to provide more income-shifting flexibilities by making trust distributions (because almost all undistributed trust income is taxed at the highest marginal bracket).

Furthermore, when accumulation trusts are used for disabled or chronically ill persons, a life expectancy payout applies, and if a person older than the disabled or chronically ill person is a remainder beneficiary (other than a mere potential successor beneficiary), that older person's shorter life expectancy might be used for determining the payout period. For example, the trust might provide that if the trust has a disabled or chronically ill person as beneficiary, within the meaning of §401(a)(9)(E)(i), no portion of the trust for that person shall ever pass under the terms of the trust or under the exercise of any power of appointment to any person who is older than the beneficiary.

i. **Rethinking Beneficiary Planning – Brief Summary.**

(1) **Favor Simplicity; Example – Outright to Children.** A participant may prefer the simplicity of leaving plan benefits directly to children, rather than having the benefits paid to trusts for grandchildren (ostensibly to have benefits paid over their long life expectancies), since the benefits must be paid within 10 years in any event.

(2) **Combo Approach.** A portion may go outright to a child (among other things, to take advantage of the child's lower income tax brackets), and a portion might go in trust for the child (for the nontax advantages of trusts). Or one child's portion may be outright and another child's portion may be in trust.

(3) **Consider Income Tax Effects.** Estate planning focuses a great deal on the 40% estate tax, but keep in mind that the income tax is also almost 40%, and trusts reach the top bracket after only $12,950 of taxable income. Even if trusts would be helpful for nontax purposes (such as creditor protection, especially if the beneficiary's state does not recognize a creditor exemption for IRA benefits), consider that the trust may pay a 37% income tax whereas individual beneficiaries may be in much lower brackets. (This is also a consideration for what distributions can and should be made out of trusts for income shifting purposes.) If a trust is being used primarily for creditor protection, consider whether the creditor protection is worth the potential income tax cost, and whether that protection might be better afforded by other means (such as an umbrella liability policy where it covers the major creditor risk).

(4) **BDOT Planning to Minimize Income Tax Effects.** As an alternative for using a trust as beneficiary but avoiding taxing trust income (including IRA benefits) at the highest marginal rate, consider using a Beneficiary "Deemed-Owner" Trust (BDOT) as the recipient. A BDOT is

structured to provide that the beneficiary can withdraw all taxable income each year, and the taxable income of the BDOT should be reported by the trust beneficiary under §678(a) and be taxed at the beneficiary's rates rather than at the trust's high rate. For an excellent discussion of the income tax issues facing accumulation trusts and the use of BDOTs, see Ed Morrow, *Using BDOTs for Optimal Asset Protection and Income Tax Minimization After Passage of the Secure Act*, LEIMBERG INC. TAX PL. NEWSLETTER #192 (Feb. 18, 2020).

(5) **Conduit Trusts.** Any individuals using conduit trusts should review the plan and confirm that it is still appropriate under the SECURE Act, understanding that all plan benefits would be paid to the beneficiary within 10 years of the participant's death unless the beneficiary is an EDB, in which event a conduit trust may be required for EDB treatment to use an adjusted life payout for a surviving spouse, minor child (until reaching majority), or person not more than 10 years younger than the participant. For a minor child, the planner should not knee-jerk into using a conduit trust, but should weigh the advantage of the added period of deferral against the fact that all of the account would be distributed to the child within 10 years of reaching majority. ACTEC comments to Treasury and the IRS have requested whether an accumulation trust for a surviving spouse, minor child, or person not more than 10 years younger than the participant can also qualify for EDB treatment.

(6) **Accumulation Trusts.** In most cases going forward, plan benefits that are paid to trusts will pass to accumulation trusts (again, unless the trust primary beneficiary is an EDB for whom a conduit trust is needed to qualify for the adjusted life payout).

(7) **Disproportionate Allocation of Benefits to EDBs, Particularly Lower Bracket EDBs.** A plan or IRA owner might leave plan benefits disproportionately to a disabled beneficiary or a sibling with modest income, and leave other non-taxable assets to other beneficiaries in high income tax brackets.

(8) **Charity.** The only way to beat having to pay income tax on retirement benefits is to leave the benefits to charity. The charity is a tax-exempt entity and pays no income on receiving the benefits. Alternatively, a charitable remainder trust could be used to avoid paying income tax on receipt of the plan benefits and payments could be made to an individual beneficiary for life. However, significant value must be left to the charity, so the participant must have some charitable intent for this arrangement to make sense.

j. **IRA Charitable Rollover.** The SECURE Act does not eliminate the IRA charitable rollover, but the $100,000 limit on qualified charitable distributions from an IRA that can be excluded from income will be correspondingly reduced by any contributions to IRAs after a person has reached age 70½. Changing the age for required minimum distributions from 70½ to 72 will not change the age at which qualified charitable distributions from IRAs will be permitted.

Particularly for nonitemizers, donors over age 70½ should consider making their charitable donations with IRA charitable rollovers at least up to the amount of the minimum required distribution and up to a maximum of $100,000 per year. Even though the nonitemizer donor does not get an income tax deduction, the donor will avoid recognizing income on the distributions. Especially if the donor has reached the RBD (April 1 of the year after reaching age 72 if the person had not reached age 70½ in 2019), the donor will avoid recognizing income on the required distributions from the IRA.

(1) **Reporting.** Box 1 of Form 1099-R from the IRA custodian will show the total amount of distributions from the IRA. The Form 1099-R does not reflect which of the distributions are "qualified charitable distributions." The taxpayer reports the full distribution amount on line 4a of Form 1040, and reports the taxable distributions (for example, the amount that is not a qualified charitable distribution) on line 4b of Form 1040, and should enter "QCD" next to line 4b. The qualified charitable distribution amount cannot be deducted and will not be entered on Lines 11 or 12, Schedule A of Form 1040.

(2) **Cannot Use Donor Advised Fund.** An IRA qualified charitable distribution cannot be made to a donor advised fund (or to a supporting organization or private foundation).

2. Basic Planning Options for Non-EDB Beneficiary (Such as an Adult Child Who Is Not Disabled)

What are the options for leaving retirement plan benefits to adult children, particularly if the owner is concerned with a child "receiving too much, too soon"? There is no way to beat the 10-year rule (without using a charitable remainder trust, which requires substantial charitable intent), so the SECURE Act has made the retirement plan less valuable to the beneficiary than under prior law.

a. **Outright.** The child would be a DB, so the 10-year rule would apply. Distributions will be taxed at individual income tax rates (rather than the compressed trust income tax rates). No limits exist on who can be recipients of the benefits at the child's death.

b. **Conduit Trust.** Using a conduit trust is more protective than leaving benefits outright to the child, because the trustee decides when to withdraw assets from the plan. The conduit trust is a DB, so the 10-year rule would apply. Benefits are taxed at individual income tax rates. No limits apply on who could be recipients of a power of appointment (as may apply for accumulation trusts).

c. **Accumulation Trust.** The accumulation trust would limit trust beneficiaries to DBs. The accumulation trust is more protective than outright or a conduit trust, because the trustee decides when distributions will be made from the trust to the child. The trust is a DB and the 10-year rule applies; the trustee must withdraw all assets from the retirement plan within 10 years. Assets may be accumulated in the trust, but undistributed income from accumulated trust assets will be taxed at the compressed trust income tax rates. Limits may apply on who can be the recipients of a power of appointment (though the IRS may relax this requirement).

d. **Non-DB Accumulation Trust.** Assets could be left to a trust that is not a valid "see-through trust," and therefore is not a DB. (For example, the trust may allow charitable recipients of a power of appointment.) The 5-year rule/"ghost LE" rule applies instead of the 10-year rule. But that is not as big a disadvantage as when the comparison was 5-year rule/"ghost LE" vs. the child's life expectancy prior to the SECURE Act.

e. **Multiple Beneficiaries.** If the owner has multiple adult children, for example, different approaches could be used for different children or a "pot" trust could be used for all of the children.

3. Basic Planning Options for Minor Child

a. **Minor Child as an EDB.** One of the EDB exceptions is for a minor child *of the participant*, not a grandchild or any other person's child (such as a niece or nephew).

The exception applies until the child "reaches majority" within the meaning of a specified unrelated provision (an obscure ERISA rule), which has a regulatory provision treating the child as not having reached majority if the child has not "completed a specified course of education" and is under the age of 26. The 10-year rule applies, beginning when the child "reaches majority." Therefore, this exception could possibly extend to age 36. The meaning of a "specified course of education" is unclear.

In addition, if a minor child becomes disabled before reaching majority, the minority status continues as long as the child is disabled. Reg. §1.401(a)(9)-6, A-15.

This exception applies if the minor child is the outright beneficiary or is the beneficiary of a conduit trust (but not an accumulation trust).

b. **Outright.** Leaving benefits outright to the minor child is simple, but may require a legal guardian or custodian under the Uniform Transfers to Minors Act (UTMA). (If the beneficiary designation names a minor outright as the beneficiary of the plan, Section 7(a) of the UTMA appears to allow the plan to make the distribution to a custodian for the minor.) The distributions would be taxed at individual rates rather than at the highly compressed trust tax rates, but an outright distribution is not ideal for a 3-year old.

Distributions could be made over the child's life expectancy as long as the child is an EDB (this also applies if a conduit trust is the beneficiary). Withdrawals over the minor's life expectancy will result in *very* slow withdrawals (and an additional 10 years after the minor child is no longer an EDB).

Under the new Single Life Table (effective for distributions on or after January 1, 2021), for example, a 15-year old has a life expectancy of 69.9 years, so the initial withdrawals would be about only 1/70th of the account, or 1.43% of the plan assets. The withdrawal would likely be much less than the interest and dividend income produced by the account, and the account would likely continue to grow during the period the minor qualified for EDB treatment. After the minor "reaches majority," further withdrawals from the account could be halted for 10 years, at which time the entire account would be withdrawn. That could possibly last until the "minor" child is 36 years old before most of the account balance would have to be withdrawn from the plan.

c. **Conduit Trust.** A conduit trust for the child qualifies as for the EDB exception. The trust agreement could include facility of payment provisions, allowing the trustee to use plan distributions for the benefit of the child rather than having to distribute them directly to the minor child. Distributions could be made to a custodial account, to parents, or to guardians. (Whether a Section 529 Plan for the minor would qualify is uncertain.) Benefits would be taxed at individual rates (because any withdrawals would immediately be distributed from the trust to the beneficiary). Benefits could be withdrawn very slowly from the plan (minimizing distributions from the trust to the minor child) until the beneficiary "reaches majority" (up to age 26) plus another ten years. But at that time, all plan benefits would be withdrawn by the trust and distributed to the child.

   Whether the exception extends to a conduit trust with multiple "minor children" or to a conduit trust with multiple beneficiaries, only some of whom are "minor children" is unclear even if the trust must be separated into separate conduit trusts for the children at the participant's death. (It is hoped that regulations will provide relief; having four separate conduit trusts for four minor children would make no sense.) Some planners have suggested providing that a conduit trust for a minor child could flip to an accumulation trust after the child reaches majority, but existing trust rules for retirement plan benefits do not clearly sanction that approach.

d. **Accumulation Trust.** If a trust is used for a minor, accumulation trusts will be used more often than conduit trusts (to avoid having large distributions to the child at some point when the child is between age 28 and 36 (depending on how long the child was in school). The 10-year rule will likely apply (pending IRS guidance allowing an accumulation trust to qualify for EDB treatment for a minor child). The trustee can accumulate funds, but income would be taxed at the compressed trust tax rates.

4. Disabled or Chronically Ill Individuals as EDBs – Overview

The most helpful of the five categories of EDBs is that a modified life expectancy payout applies if the DB is disabled or chronically ill, thus providing favorable treatment for special needs trusts.

a. **Definitions of Disabled and Chronically Ill.** The SECURE Act provides cross references to definitions of disabled (§72(m)(7)) or chronically ill (§7702B(c)(2)) individuals. For example, a person who qualifies for Social Security disability benefits qualifies for this exception. The definitions of both disabled and chronically ill are difficult to apply to minors.

b. **When Status Is Determined.** The beneficiary's status as an EDB is determined at the participant's death. §401(a)(9)(E)(ii)(last sentence). If a DB later becomes an EDB (i.e., is later disabled) before all distributions have been made from the plan, the plan cannot switch to EDB status.

c. **Certification.** Section 72(m)(7) requires proof of disability and §7702B(c)(2) requires certification as chronically ill by a licensed health care practitioner. When such certification must be given is unclear. Rumors surfaced that the IRS might take the position that such certification must be in place at the time of the retirement plan participant's death. ACTEC filed comments with representatives of the Treasury and IRS on March 31, 2020, recommending that no such certification should be required before a reasonable time has passed after the issuance of long-term guidance on the issue, and "that either interim or long-term guidance should provide that no certification will be required until a reasonable and specified amount of time has passed after the death of the employee who has designated the beneficiary, provided of course that the certification confirms that the beneficiary was in fact disabled or chronically ill as of the death of the employee."

d. **Applicable Multi-Beneficiary Trusts (AMBTs).** At the 11th hour of the negotiations in Congress, the need to do more to help disabled and chronically ill individuals who need special needs trusts that can accumulate assets was recognized. A special provision under §401(a)(9)(H)(iv)-(v) for "applicable multi-beneficiary trusts" (or AMBTs) applies if (i) the trust has more than one beneficiary, (ii) all of the beneficiaries are designated beneficiaries, and (iii) at least one of the beneficiaries is disabled or chronically ill.

Some of the special benefits afforded disabled and chronically ill beneficiary EDBs under the AMBT provisions are: (i) A mandated division at the participant's death is given effect, contrary to the result described for retirement plan distributions generally in Reg. §1.401(a)(9)-4, A-5(c) (for example, if some of a single pot trust is divided into a separate trust for a disabled or chronically ill child, that separate trust would qualify for this exception); (ii) A single trust with multiple disabled or chronically ill individuals as beneficiaries qualifies for the exception; and (iii) An **accumulation trust** for disabled or chronically ill beneficiaries qualifies for the exception (whose life expectancy is used in that case is not clear, and the conservative approach, until the IRS gives further guidance, is to have remainder beneficiaries who are no older than the disabled or chronically ill current beneficiary or beneficiaries).

Special rules that apply to AMBTs are discussed below in Item 6.

e. **Changed Planning Approach**. Prior to the SECURE Act, planning was arranged so that retirement benefits would not pass to disabled children. Now they may be the favored beneficiaries because healthy beneficiaries would generally have a 10-year payout requirement, whereas long-term deferral is possible for disabled beneficiaries. The people that benefit from this changed approach may include the non-disabled beneficiaries who receive other assets that are not subject to income tax (so additional assets may be left to the disabled person to account for this difference).

5. Disability Planning Issues Generally

a. **General Discussion of Disability Planning Issues.** For a general discussion of planning considerations for disabled individuals, see Item 33 of Heckerling Musings 2020 and Estate Planning Current Developments found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights** and see Items 50-57 of the ACTEC 2011 Fall Meeting Musings summary found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights**.

b. **Medicaid.** Eligibility for Medicaid is no more restrictive than the requirements for Supplemental Security Income (SSI), for which the asset limit is $2,000. Qualifying for Medicaid is especially important because many programs essential to disabled or chronically ill individuals are only available to those who qualify for Medicaid.

Transfer restrictions are severe for SSI qualification; a 5-year look-back period applies, and the 5-year penalty period does not begin until the applicant has spent all of his or her assets, is "otherwise qualified for Medicaid," and has made a formal Medicaid application.

Trusts may or may not be considered a resource. The Social Security Administration Program Operations Manual System ("POMS") contains the policies of the Social Security Administration, and covers eligibility for SSI (and eligible SSI recipients are eligible for Medicaid). The POMS has extensive new rules on trusts that are being applied by federal courts for Medicaid and related benefits cases.

c. **First Party Special Needs Trusts.** Self-settled special needs trusts (created by the beneficiary) must meet several requirements in order for the trust assets not to be counted as resources, as listed in 42 U.S.C. §1396p (d)(4)(A). The requirements include that (i) the beneficiary is under age 65, (ii) the trust is for the sole benefit of the settlor-beneficiary, and (iii) at the beneficiary's death, any trust assets must be used to repay any Medicaid assistance received (excess assets may pass to successor beneficiaries). Including a reimbursement provision is essential in self-settled special needs trusts but is not needed (and generally should not be included) in third party trusts.

d. **Third Party Supplemental Needs Trusts.** Whether assets in a third party trust count as resources for SSI and Medicaid qualification purposes depends on state trust law concepts, federal programs, federal regulations, and state policy rules. "If the individual has the right, authority or power to liquidate the property … it is considered a resource." A third party (created by someone other than the beneficiary) special needs trust does not need to include the three requirements mentioned immediately above for first party trusts.

   Three keys to drafting third party special needs trusts are (i) do not impose a duty on the trustee to support the beneficiary (the preference is to give the trustee total discretion as to whether to distribute assets), (ii) do not give the beneficiary the power to access trust principal, and (iii) clearly express the settlor's intention to supplement, but not supplant, means-tested public assistance.

e. **Qualified Disability Trust.** A special type of third party trust that qualifies for certain federal income tax benefits is a qualified disability trust (sometimes referred to as a "QDisT"), as described in §642(b)(2)(c). All current trust beneficiaries must be disabled and have been disabled before the age of 65, and the trust must be funded by a third party (not the beneficiary). The trust remaindermen need not be disabled. The qualifying trust qualifies for a $4,300 exemption for federal income tax purposes (compared to $100 for complex trusts and $300 for simple trusts, and $600 for estates). Most third party supplemental needs trusts can be structured to meet the requirements of QDisTs. The QDisT provisions apply only if the current beneficiaries are disabled, not including chronically ill individuals.

f. **ABLE Accounts.** ABLE accounts were authorized in 2014 legislation. They are tax-advantaged accounts (income on the account is not taxed) that can make distributions for "qualified disability expenses" of the beneficiary, which is limited to individuals with a disability whose disability began before turning 26 years of age. The key is that the account funds are generally not treated as a resources for purposes of SSI and Medicaid eligibility.

   Final regulations regarding ABLE accounts under §529A were released October 1, 2020. T.D. 9923, IR-2020-227 (Oct. 1, 2020). The final regulations address a wide variety of requirements, including requirements for establishing ABLE accounts, requirements to be a qualified designated beneficiary elements, contributions (including limitations on the amount and investment of contributions), changes of the designated beneficiary, and rollovers and program-to-program transfers from one ABLE account to another. The final regulations also provide guidance about the gift and GST tax consequences of contributions, the income, gift, and estate tax consequences of distributions from, and changes in the designated beneficiary of, an ABLE account, and about the recordkeeping and reporting requirements of a qualified ABLE program.

   Limits apply to the amount of annual contributions that are allowed (generally $15,000, indexed) and on the overall account size (generally $100,000, but some states have higher limits).

   The practical advantage of the ABLE account is that the account can afford a degree of self-control and personal autonomy because the beneficiary can pay directly for some expenses from the account without having to involve the trustee of the special needs trust for every expense that comes up. High-functioning disabled beneficiaries will enjoy that freedom.

6. Planning Issues With Applicable Multi-Beneficiary Trusts (AMBTs)

a. **Rule I: Mandated Divisions Given Effect.** Generally, if a trust that is the beneficiary of a retirement plan (or IRA) benefit divides into separate trusts at the owner's death, they are not treated as "separate accounts" for purposes of determining the applicable distribution period unless the separate subtrusts were each named as beneficiary of the plan benefits. Therefore, all of the beneficiaries of the single trust are considered in determining the payout period (and if the life expectancy payout method applies, the oldest beneficiary's life expectancy is used). Reg. §1.401(a)(9)-4, A-5(c).

   Rule I overrides that general rule for the interests of disabled and chronically ill beneficiaries of AMBTs. If the AMBT, by its terms, is to be divided immediately on the owner's death into separate trusts for each beneficiary, the payout rules "shall be applied separately with respect to the portion

of the employee's interest that is payable to" any disabled or chronically ill EDB. §401(a)(9)(H)(iv)(I), (v). This apparently means that the beneficiary designation may list a single AMBT that divides at death into separate trusts for disabled and chronically ill individuals and for other DBs. Perhaps the trust could allow the trustee to make a non pro rata division of plan and non-plan assets at the time of the division. Guidance should clarify whose life to use for purposes of the determining the life payout that is allowed to disabled or chronically ill beneficiaries of the divided trust. Guidance on these and other issues is needed regarding the effect of Rule I.

b. **Rule II: Only Disabled or Chronically Ill Individuals Are Current Beneficiaries During Their Lives.** If the terms of the AMBT provide that no one other than a disabled or chronically ill individual has a right to plan benefits until the death of all disabled or chronically ill beneficiaries, then the AMBT may use the life expectancy payout method instead of the 10-year rule. However, the Act is not clear as to whose life governs. The worst case is that the oldest DB (including beneficiaries after the lives of disabled or chronically ill beneficiaries) governs under the traditional see-through trust rules. However, guidance may allow the life expectancy of the older disabled or chronically ill beneficiary to be used.

Drafting Tip: Pending more guidance, use an age restriction or other means to limit the ages of all trust beneficiaries of the AMBT, including DBs who are not disabled or chronically ill beneficiaries.

c. **Special Needs Trusts.** Further IRS guidance is needed with respect to various issues for special needs trusts. Until further guidance is provided, consider revising special needs trusts to exclude (i) backstop provisions (allowing distributions to other beneficiaries of amounts that would cause the disabled beneficiary not to qualify for government assistance programs), (ii) provisions allowing excess assets to be distributed to non-disabled beneficiaries (for tax planning in light of the high rates applied to undistributed trust income or if the special needs beneficiary no longer qualifies for public benefits), and (iii) provisions allowing the payment of travel expenses of a travel companion for a disabled beneficiary. Include a statement that the settlor intends the trust to qualify as an AMBT. Consider allowing the trustee or some person to reform or amend the trust so that it qualifies as an AMBT in light of future IRS guidance. As discussed in the Drafting Tip above, consider specifying that all remainder beneficiaries are younger than or close in age to the special needs beneficiary. An outstanding resource regarding planning for the disabled and chronically ill EDB category (and in particular, planning for special needs trusts in light of the SECURE Act) is Nancy Welber, *Security for Disabled and Chronically Ill Beneficiaries*, TRUSTS & ESTATES 40 (April 2020).

7. Surviving Spouse as EDB

a. **Requirements for Surviving Spouse to Qualify as EDB.** To qualify for the spouse exception, the benefits must be payable "to" the surviving spouse, which likely requires that the beneficiary is the surviving spouse outright, or a conduit trust for the surviving spouse (because the conduit trust rules treat the conduit beneficiary as the owner of the trust and plan for purposes of the minimum distribution rules).

b. **Conduit Trust as Beneficiary.** If a conduit trust for the spouse is a beneficiary (or if the spouse is the outright beneficiary), the spouse could take advantage of special spousal rules delaying beginning distributions until the end of the year in which the deceased participant would have turned age 72 (§401(a)(9)(B)(iv)(I), as amended by the SECURE Act) and using the Single Life Table but recalculating the life expectancy annually (Reg. §1.401(a)(9)-5, A-5(c)(2) (first sentence, A-6). If the spouse dies before all benefits are paid, the required minimum distribution for the year of death must be based on the recalculated life expectancy by the end of the year (if it had not previously been distributed that year), and the balance must be paid within 10 years of the spouse's death. (Before the SECURE Act, the benefits could be paid over the spouse's remaining life expectancy, with no recalculation following his or her death.)

c. **Standard QTIP Trust (Accumulation Trust) as Beneficiary.** A standard QTIP trust, that does not require that all retirement plan distributions to the trust be distributed to the spouse, would not qualify for this spousal special treatment (at least pending further IRS guidance), even if it is a valid see-though trust, Reg. §1.408-8, A-5(a). Under the SECURE Act, a standard QTIP trust does not

qualify as an EDB and the 10-year rule would apply after the participant's death. A QTIP trust that also requires such distributions to the spouse of all plan distributions would constitute a conduit trust that is an EDB and would qualify for the spousal special treatment.

d. **Spouse as Outright Beneficiary.** If the spouse is the outright beneficiary, additional alternatives are available (in addition to the option described above if a conduit trust for the spouse is the beneficiary). The spouse can elect to treat the IRA as his or her own, or may roll over the plan benefits into the spouse's own rollover IRA. Advantages include a delayed starting date (until the surviving spouse reaches age 72) and a slower payout (using the Uniform Life Table, rather than the Single Life Table with recalculation). Under the SECURE Act the spouse would no longer have the ability to name a beneficiary who can receive payout based on the beneficiary's life expectancy, but the remaining benefits would have to be paid by the end of the year in which the tenth anniversary of the spouse's death occurs. If a beneficiary is an EDB at the time of the surviving spouse's death, the EDB rules should apply for that beneficiary (because the spousal rollover IRA is treated as the spouse's IRA, §§408(d)(3)(A), 408 (d)(3)(C)(ii)(II)).

Items 8-12 are observations from the seminar at the Summer Meeting: Where There is a Will, There is a Way – Trust Me! by Professor Karen E. Boxx, Andrew J. DeMaio, and Bruce Stone

8. Basic Execution Procedures

Planners have had to abandon standard procedures for signing documents while dealing with the coronavirus, and understanding the basic mandatory execution requirements is essential.

a. **Timing and Location of Witnesses.** The Uniform Probate Code does not require that witnesses sign at the same time as the testator, but can sign within a reasonable time later. The witness can just witness that the testator acknowledged signing the document. UPC §2-502.

b. **Self-Proving Affidavit.** The Uniform Probate Code version of the self-proving affidavit states that "each of the witnesses, in the presence and hearing of the testator, signed the will as witness." UPC §2-504. Therefore, if the witness cannot sign the will until later, it will not be a self-proved will.

9. Getting Creative; Workarounds

a. **Outdoor or "Window-Separated" Signing.** Some planners have supervised the signing of documents at outdoor tables. Alternatively, some have organized signings the witnesses watching the testator through a window. The National Notary Association issued guidance describing procedures for window-separated signings.

b. **Safeguards.** Possible signing safeguards during a pandemic include the following.

- Use a large room or open area.
- Wipe down surfaces before and after the signing.
- Use gloves and masks.
- Use separate pens.
- Minimize the handling of documents.
- Possibly use delayed signing by witnesses.
- Delay copying and distribution of signed documents.

c. **Holographic Wills.** To have the testator sign a very basic will quickly, consider using a holographic will if recognized in the state of the execution. Generally, all material provisions of the will and the signature of the testator must be in the handwriting of the testator.

d. **Harmless Error Rule.** Section 2-503 of the Uniform Probate Code provides that a writing can be admitted as an intended will even though it does not comply with all formalities. This provision has been enacted in only 10 states, however (and temporarily during the pandemic in Minnesota). A court proceeding is required to probate the will. The proponent of the document must establish by clear and convincing evidence that the testator intended the writing to constitute his or her will.

e. **Finding a Notary.** Possible notaries includes employees at banks, UPS, and FedEx stores. Another creative alternative is to have a process server watch the signer sign the document, notarize the document, and return the signed and notarized document to the planner. Powers of attorney for real property must be notarized in most states.

f. **Remote Signing of Retirement Plan Spousal Consents.** IRS Notice 2020-42 describes procedures for remotely signing spousal consents for retirement plan benefits.

10. Remote Notarization

a. **Remote Online Notarization (RON).** RON had been authorized by legislation in 23 states prior to the pandemic. Many of the state laws are patterned after the Revised Uniform Law on Notarial Acts (RULONA). The National Notary Association has another uniform act.

A RON provider's dedicated software platform must be used. Examples are notary.com and notarize.com. The platform satisfies the legislative requirements, including–

(1) video conference capability,

(2) multi-factor methods for verifying the identity of the signer relevant for remote online notarizations ([i] Knowledge Based Authentication, requiring answers to questions requiring personal knowledge of the signer, [2] credential analysis, such as driver's licenses or passports, and [iii] biometric measures, which is used much less often), and

(3) an electronic signing room allowing electronic signatures by the document signer and notary.

b. **Remote Ink-Signed Notarization (RIN).**

(1) **Procedures.** In a number of states executive orders have been issued to allow remote witnessing and notarization of documents. Procedures vary, but generally require direct remote interaction of the signer and witnesses **during the signing** via real time audio and video connections. Each of the signers have paper copies of the documents being signed. The identity of the signers and of the document being signed must be verified. After signing, the signers fax or email the document to the notary who signs the document. Electronic signatures may be used.

Most states have a recording requirement (and the recording must be retained for a specified period of time (examples are for 7-10 years in various statutes or executive orders). Zoom sessions may easily be recorded and maintained on the user's computer or in the Zoom cloud (but retaining the recording in the Zoom cloud is not recommended, see Item 11.c below).

Special certification of the remote notarization is also typically required.

(2) **RIN Tips.**

- Check lighting and the camera position to assure all are visible.
- Avoid virtual background (paper may not show up in virtual backgrounds).
- Remember to hit the "Record" button.
- Comply with geographic limitations; in some states, the notary and signer must be in the same state.
- Watch expiration dates of emergency orders.

11. Ethical Implications During a Pandemic

Various ethical issues apply in a pandemic environment under the Rules of Professional Conduct.

a. **Rule 1.1 – Competence.** The duty of competence includes overseeing the execution of documents in a manner that they will be enforced and carry out the client's wishes.

For example, an article in an online Washington State Bar Newsletter describes an actual fact scenario of the execution of a will for a client suspected of having COVID-19. The lawyer notarized the self-proving affidavit before arriving at the client's house for the signing ceremony. At the execution ceremony, witness were outside a window where they could see the client inside the house. The witnesses signed the document and passed the document to the client inside the house for her signature. This procedure was well intended, to avoid having the attorney and witnesses handle documents touched by the possibly infected client. But the documents did not satisfy the execution requirements under Washington law, and the Bar removed the article from the Newsletter for fear that it would mislead other planners.

For remote witnessing, the attorney not only must make sure that the state authorizes the remote notarization but should also take additional steps such as asking who is present including those outside the range of the camera, asking questions to assure that all signers are aware of what they are doing, and making an appropriate record.

In addition, the attorney must keep up to date on changing laws and procedures and must keep current regarding technology issues.

b. **Rule 1.3 – Diligence.** Comment 5 requires that lawyers must have a plan for their own incapacity or demise. Attorneys working from home are somewhat like sole practitioners. Make sure that staff personnel know where things are located and what is going on. Have a plan for internet outage during meetings.

c. **Rule 1.6 – Confidentiality.** The attorney must know who is within earshot of a client when talking with a client in Zoom sessions. Avoid discussing sensitive information during Zoom conferences, but use a telephone for discussing those issues.

Tips for Zoom Conferences to Maintain Confidentiality:

- Who is present?
- How secure is the conferencing platform?
- Use a password.
- Use a waiting room.
- Use a random meeting id number.
- Give the id number just to people invited to the meeting.
- All participants should have the Zoom app for Zoom calls (that is more secure).
- A recording of the Zoom meeting should be saved on the attorney's own computer and not posted to the Zoom cloud.
- Weigh the amount of security needed based on the sensitivity of the conversation (and for really sensitive issues, use a landline telephone).
- For multi-party negotiations, do not use the private chat, for fear it may not be hidden from others. Have a telephone handy for private text messages.
- Don't forget the mute button.

d. **Rule 5.1 – Supervising Subordinate Lawyers and Staff.** Supervising subordinate employees is more difficult when all are working from home. Assure that staff and any outsourcing resources are using secure communication procedures.

e. **Rule 4.3 – Communicating With Unrepresented Parties.** If the attorney is representing a fiduciary and communicating with beneficiaries, constantly remind the beneficiaries that they are not represented by the attorney. Communicating that clearly is more difficult in remote sessions.

f. **Rule 5.5 – Multijurisdictional Practice.** Under Rule 5.5(b) if an attorney is not admitted to practice in the state, the attorney cannot have a presence in the jurisdiction for the practice of law. What if the attorney is out of state at a vacation home and is working from that jurisdiction in representing clients in the home state, even though the attorney is not licensed in the vacation home state. This is probably not a big concern with bar associations. Rule 5.5(c) permits providing "legal services on a temporary basis" in certain cases, including situations "reasonably related to the lawyer's practice in a jurisdiction in which the lawyer is admitted to practice," but some states have not adopted that subsection or have altered it. The District of Columbia Court of Appeals issued an opinion applying the temporary exception to an attorney who is in the District because of the pandemic. Several cases (in Ohio and Oregon) have applied the temporary basis exception to attorneys awaiting acceptance to the bar of a new state under a reciprocal admission arrangement between states.

12. What Does the Future Hold?

Bruce Stone reminds of the Casey Stengel warning: "Never make predictions, especially about the future." Or the Yogism, "It's tough to make predictions, especially about the future."

For an excellent and thorough discussion of how lawyers must anticipate and plan for the future, see Fellow Jonathan Blattmachr's article expanding upon his Trachtman lecture delivered at the 2010 annual meeting: *Looking Back and Looking Ahead: Preparing Your Practice for the Future: Do Not Get Behind the Change Curve,* 36 ACTEC L.J. 1 (2010) (**http://www.actec.org/assets/1/6/Journal_V36_N1_Summer10.pdf**)

Things that were probably going to happen anyway are happening much faster as a result of the pandemic. We are fast-forwarding into the future.

A poll to Fellows received 796 responses about the practices in the pandemic. Some observations from that poll are summarized below.

a. **Online Meetings.** 95% of respondents in the poll have had online video meetings; 80% of them have had online client meetings. Two-thirds of respondents will continue to offer using online client meetings after the pandemic, and about one-third will continue online meetings but only if the client asks for an online meeting. (Five percent will not have online client meetings after the pandemic, but that may change if clients demand online meetings for their convenience.)

b. **Accepting New Clients.** About 80% of the poll respondents said they would be willing to accept a new client without first meeting the client in person if the circumstances are appropriate. Another 20% would be willing to meet with new clients in online meetings if there was at least one in-person meeting.

c. **Offices.** Will the need for office space diminish in the future? Many staff like working from home and have found it to be productive (no commute time, less interruptions, etc.) Potential negatives of remote working include a concern of lower productivity, distractions, loss of comradery, etc.

   Two studies suggest some unanticipated results of remote working. A 2014 IBM Software Technical Whitepaper drew these conclusions about teleworkers: They are happier about the job prospects, less stressed, believe that have more sharing of information, and enjoy as much teamwork and cooperation as office employees. Interestingly, though, part-time teleworkers are just as stressed as their office-bound co-workers.

   An article published in the Harvard Business Review on August 24, 2019 reinforces those conclusions. Concerns of managers are that remote employees work less, multi-task, mix personal responsibilities and work, and experience decreased communication and collaboration. The article recommends: Granting greater autonomy to enhance employee productivity; leveraging clusters of remote workers by funding periodic informal meet-ups; and keeping new employees in a central office with experienced peers long enough to benefit from informal learning. The article concludes

that remote employees who can perform their duties with little coordination with co-workers can experience productivity increases, and remote working for employees who work independently and know their job well can benefit both the company and the employee.

Bruce's predictions include–

- As law firm leases expire, either less space will be leased or existing space will be reconfigured to accommodate fewer in-office employees with more space for safety protocols.
- Many law firms will wind up with a rotation system for employees (both lawyers and nonlawyers).
- Recent trends toward sharing open space or office sharing will change if not end.
- The need for conference rooms will diminish with more online client meetings and remote execution of documents.
- As the demand for office space declines, office rents will drop.

d. **Attire.** Business-casual dress will become prevalent. "Casual Fridays" will become everyday occurrences when working from home. Attorneys must maintain their professional appearance, though, because unscheduled Zoom calls will occur periodically.

e. **Signing Documents.** Clients will embrace online execution of documents even if advisors resist. Only four states now allow online signing of electronic wills, but many states allow online notarization.

f. **Marketing.** Attorneys will establish new client relationships in the future in many situations without first having an in-person meeting. Word of mouth will still be especially important.

Using civic organizations as a marketing tool will not be as effective, but having an effective online presence on twitter or Facebook will be helpful.

Interviews with reporters can be helpful. Most attorneys hate unabashed advertising by lawyers, but tasteful advertising will become increasingly important for estate planning professionals.

g. **Private Dispute Resolution.** Dispute resolution hearings and most ADR can be conducted just as effectively through an online platform as in in-person conferences, and most clients will opt for the lower cost of online venues.

h. **Trials.** The workability of having (and testing the credibility of) live witnesses at trials is still unknown, but civil trials through online platforms eventually will become more commonplace. Evidentiary practices will have to adapt.

i. **Gender Assignment Roles.** If the traditional approach of responsibility for childcare and home care is not reallocated, women working from home will have additional burdens than those borne by men. The pandemic environment is an opportunity for reconsidering the balance of gender assigned duties. ACTEC can be a leader in addressing that in our field.

j. **Artificial Intelligence.** At some point, lay persons can get sophisticated estate planning done without ever leaving home or speaking live to an estate planning adviser. Do not think that ACTEC Fellows are immune from this phenomenon. It will be driven by cost savings.

Items 13-18 are observations from the seminar at the Summer Meeting: Charities in a Time of Crisis by Cynthia G. Lamar-Hart (moderator), Mary Beckman (Chief, Health Care and Fair Competition Bureau, Massachusetts Attorney General's Office, Boston, Massachusetts [and Mary stated that comments by her are her own and not those of the Massachusetts Attorney General's office and are not legal advice]), Erik Dryburgh, and Lawrence P. Katzenstein

13. Role of Attorney General

a. **Role.** The primary role of the attorney general (AG) is to protect the public interest. The AG enforces restrictions on charitable gifts and oversees fiduciaries who are responsible for the administration of assets.

In addition, the AG in some states exercises regulatory authority over charities, who must register with the AG's office and submit annual financial filings. (The secretary of state in some states performs this function.)

The means for enforcing charitable restrictions is through lawsuits and resolution of disputes prior to the filing of lawsuits.

The AG's authority for overseeing charities is traditionally exclusive (including the power to investigate allegations of wrongdoing for failure to abide by gift restrictions), and others do not have standing to enforce restrictions.

b. **Limitations on Role.**

(1) **No Ability to Substitute Judgment.** The AG does not substitute its judgment regarding decisions made by the charity, but merely assesses the reasonableness of decisions (even if the AG would have made a different decision).

(2) **No Power to Grant Relief from Restrictions.** Granting relief from charitable gift restrictions is up to the judiciary. In addition, the Uniform Prudent Management of Institutional Funds Act (UPMIFA) allows the modification of small funds without court action after notification to the AG.

(3) **Resources.** An important practical limitation is the allocation of limited resources of the AG staff.

14. Operational Issues for Attorney General Activities

a. **Allocation of Resources.** AGs get hundreds of complaints each week. The AG probably will not follow up on a complaint if a relatively small amount of charitable funds is at risk.

In Massachusetts, the AG generally does not take an active role in disputes if the parties are well represented. The AG monitors filings and will intervene if the AG thinks something is improper.

b. **Determining Reasonableness.** In determining the reasonableness of decisions, the AG balances the need to enforce the good performance of fiduciary duties against setting a standard that is too high and that would discourage robust voluntary charitable board service.

c. **Transparency and Accountability.** If the AG thinks that the reasonableness of a decision is a close call, the AG may strongly recommend or require a court determination.

If the AG determines that a gift restriction should be modified, the AG has no authority to modify the restriction but may describe to a court the relief that the AG thinks is appropriate. The court petition should cover all relevant facts and the relief requested. If the AG agrees with the requested action, a truncated judicial process may be possible. If the AG does not agree with the requested relief, the AG will file a responsive document and might request a modified form of relief.

d. **Relationship with Charitable Sector.** A practical consideration is maintaining a good working relationship with the charitable sector and a collaborative relationship in enforcing standards and restrictions. The AG encourages having well-informed and well-counseled boards and trustees.

15. Borrowing From Endowments

Requests from charities to borrow from endowments has become more prevalent because of the financial difficulties of charities during the pandemic.

a. **Borrowing Generally Not Appropriate.** While not directly addressed by UPMIFA, an institution likely cannot borrow from an endowment fund for that institution. A loan is a contract, requiring two parties, and there would only be one party (the charity). Practically, who would sign as borrower and as lender? If the charity defaults on the loan, which directors will be the plaintiffs and which directors will be the defendants in the lawsuit to enforce the loan documents? The borrowing would likely be treated as an expenditure by the endowment fund beyond the allowed spending limits.

b. **Exceptional Circumstances When Borrowing May Be Appropriate.** In some limited circumstances, however, borrowing from an endowment might be appropriate and supported by the AG even though AGs are generally not comfortable with such borrowing. Examples (based on actual cases)–

(1) A museum must close. It has identified the perfect recipient for its collection but the receiving museum must undergo renovations to house the collection. The closing museum will provide those funds by borrowing from its endowment, selling its land after the receiving museum has undergone renovations and accepted the collection, and repaying the loan to the endowment.

(2) A private school has a downtown location that needs substantial repairs and is in an inconvenient location for students. It has identified a suitable lower-cost suburban location. The school will borrow from the endowment to purchase the new location and relocate the school, then it will sell the existing location, repay the loan from the endowment, and use the remaining sale proceeds for operations.

c. **Pledging Endowment Assets Is Generally Inappropriate.** If a direct loan from an endowment fund is not allowed, can the charity borrow from a bank and pledge the assets of the endowment fund as collateral for the loan? Although the Comments to UPMIFA suggest that pledging endowment funds as security for loans is permitted under §3(e)(3), subject to §3(e)(1), many planners believe that pledges by endowment funds have similar concerns as loans from the funds. If the lender enforces the pledge, the appearance is that the assets in the endowment fund have been used for charitable purposes beyond the restrictions in the endowment fund, and a state attorney general would likely collapse the two transactions.

Banks have figured that out and few are willing to accept endowment funds as collateral for loans to charities. The California Attorney General has been successful in some cases in saying that endowment fund assets are not available to creditors. At the least, the bank would want a legal opinion that the endowment funds are valid collateral (and some of the panelists would be unwilling to give that legal opinion).

16. Spending Limitations from Endowments

a. **Background – Change from Approach Under UMIFA.** The prior Uniform Management of Institutional Funds Act (UMIFA) provided that a gift for endowment or subject to distribution of just income meant that the donor intended to permit the charity to spend a prudent amount of appreciation. UMIFA allowed charities to spend appreciation as long as the fund was above its "historic dollar value" (i.e., the amount of contributions to the fund). If the fund was below the historic dollar value, it could continue to spend interest, dividends, rents, and royalties. This approach did not preserve the purchasing power of the fund on a long-term basis.

b. **General Spending Guidance in UPMIFA.** For endowment funds, the spending guidance in §4(a) of the Act gives funds a significant degree of flexibility. Subject to donor intent otherwise expressed in the gift instrument, the fund "may" spend or accumulate so much as the institution determines is prudent for the purposes and duration for which the fund is established. Any limitation on this general authority to spend or accumulate must be specifically stated in the gift instrument. §4(b).

The provisions seem to indicate that some minimal level of spending is required, and the fund cannot simply warehouse funds indefinitely. The fund "shall" act in good faith in considering various factors including the charitable purposes of the fund.

c. **Rebuttable Presumption of Imprudence.** About half of the states have adopted an optional §4(d) of the Uniform Act, which provides that spending in any year that exceeds 7% of the fair market value of the endowment fund, determined at least as often as quarterly over a three-year period preceding the year in which the spending occurs, "creates a rebuttable presumption of imprudence." Distributions permitted under other laws or the gift instrument are not subject to the presumption. §4(d)(1).

   On the other hand, distributions of 7% or less are not presumptively prudent. Thus, the 7% guidepost is not a safe harbor for a charity's spending, but spending exceeding 7% is presumptively imprudent, which would then require the charity, if questioned, to justify its actions. The Comments to the Act clarify that if the facts "raise the presumption of imprudence, then the institution will have to carry the burden of production (i.e., the burden of going forward with) other evidence that would tend to demonstrate that its decision was prudent. The existence of the presumption does not shift the burden of persuasion to the charity."

   An overall goal of UPMIFA, as compared to UMIFA, is to place some caps on spending to preserve the purchasing power of endowment funds over the expected life of the fund.

d. **Donor Overriding UPMIFA's Spending Rules.** The spending rule in UPMIFA is a rule of construction regarding what a donor intended by using terms such as "endowment" or "pay only the income." Section 4(a) begins by saying that the spending guidance in §4 is "subject to the intent of a donor expressed in the gift instrument." How would a donor overcome the spending rules? The Comment to §4 provides that an instruction to "pay only the income" will not be specific enough, but an instruction to "pay only interest and dividend income" earned by the fund would be. If a donor does not want the spending rule in UPMIFA to apply, the donor should be as specific as possible.

e. **Fund Overcoming Rebuttable Presumption of Imprudence.** If a fund has distributions below 7% for a few years and then exceeds 7%, but does not bring the average over 7% for the four-year period, the presumption does not apply. The Comments to §4(d) discuss situations that might overcome the presumption. For example, limiting distributions for an extended period of time to save for a capital project and then taking a distribution that exceeds 7% of the four-year lookback may be prudent. "For some endowment funds fluctuating spending rates may be appropriate." Examples in the Comments address capital projects, but the rationale should extend to other activities that require an unequal large distribution in one year preceded or followed by years of minimal distributions. Comments suggest that the big distribution could come at the beginning or the end of the period of reduced spending.

   Other situations, beyond those mentioned in the Comments, might include having consistent higher returns to support distributions above 7%, or one-time exigent circumstances that demonstrate that the permanence of the fund will not be jeopardized.

f. **Are Private Foundations Subject to the Spending Rules of UPMIFA?** As a practical matter, most private foundations will not be affected by UPMIFA's spending rules. A gift with no donor restrictions or in response to solicitation materials that have no special purposes expressed does not create an endowment fund subject to the spending rules. The governing documents of corporate foundations typically do not have restrictions, and if they do, the governing documents can be amended to remove the restrictions. For that reason, if a donor who is creating a foundation wants to create restrictions, a trust format is typically used. Keep in mind, though, that UPMIFA does not apply to trusts unless the institution is also serving as the trustee.

   Observe that the 5% distribution requirement for private foundations in §4942 of the Internal Revenue Code is to ensure that foundations spend enough, but UPMIFA is designed to ensure that an endowment fund does not spend too much. The purposes of the two separate provisions are in tension with each other.

17. Releasing or Modifying Restrictions on Charitable Gifts

Brief Summary of UPMIFA Modification Provisions. UPMIFA allows a charity to release or modify a restriction in certain circumstances.

a. **Donor Consent.** The charity may release or modify a restriction regarding the *management, investment, or purpose* of a fund if the donor consents in writing. [UPMIFA §4(a)]. The actual donor's consent is required, and not someone acting for the donor (such as a spouse). However, the representative of the donor's estate or heirs should be able to provide consent.

b. **Cy Pres and Deviation Modifications.** If a *purpose or use* restriction becomes unlawful, impracticable, impossible to achieve, or wasteful, the court may modify the restriction in a manner consistent with the donor's intent (which is similar to the cy pres doctrine, RESTATEMENT (THIRD) OF TRUSTS §67; UNIF. TRUST CODE §413.). Similarly, the court can modify a *management or investment* restriction if it has become impracticable or wasteful, impairs the management or investment of the fund, or (if due to unforeseen circumstances) the release would further the purposes of the fund. (This is similar to the deviation doctrine, RESTATEMENT (THIRD) OF TRUSTS §66; UNIF. TRUST CODE §412.) In either case, the attorney general must be notified. [UPMIFA §4(b)-(c)]

c. **Small Funds.** If a fund is less than $[25,000] in value and over [20] years old, and the charity determines that a restriction on the *management, investment, or use* of the fund is unlawful, impracticable, impossible to achieve, or wasteful, the charity can (after notice to the attorney general) release or modify the restriction. It must thereafter use the funds in a manner consistent with the donor's charitable purposes. [UPMIFA §4(d); some enacting states have increased the amount considered small.] Less than half the states have adopted this provision.

None of those provisions directly address "spending." Does spending fall within purpose and/or use?

d. **Multiple Donors.** If multiple donors contribute to a fund, the consent of all of the donors will generally be required to release or modify restrictions. For example, if spouses contribute to a fund, after the death of one of the spouses, the surviving spouse could consent to release or modify a restriction regarding the half contributed by him or her. State property rights giving spouses management authority over marital or community property might be a basis for a surviving spouse to consent to a release or modification regarding the entire donation.

18. Enforcing Donor Intent

a. **Desires of Charity to Change Use of Fund or Restrictions.** Conditions may change, making gift restrictions inappropriate. For example, a charity may wish to change the name of a building because the existing name has become an embarrassment or in order to solicit a new donor for extensive renovations. During the pandemic, charities have wished to make changes to allow using funds to meet pressing needs that have arisen because of the pandemic.

b. **Donor Standing.** If the charity simply changes the use of the funds without obtaining authorization to do so, can the donor enforce the existing standard? Or can the donor participate in a judicial action to modify the restriction?

(1) **Traditional View.** These cases have traditionally been viewed as property cases, and once the donor has parted with the property the donor has no further interest in the property and the attorney general must enforce rights for the benefit of the public.

(2) **Shift Toward Some Recognition of Donor Standing.** The traditional view is changing. UPMIFA does not address donor standing to enforce restrictions (an amendment to provide donor standing was considered but was not included in the final version of the Act). Its silence regarding donor standing was not intended as a statement against donor standing. The Uniform Trust Code includes donor standing for donors to charitable trusts. *See* UNIF. TRUST CODE §4.05 ("The settlor of a charitable trust, among others, may maintain a proceeding to enforce the trust"); UPMIFA §4(a) (does not recognize donor standing to enforce restrictions but gives the donor the power to consent if a charity wishes to release or modify a restriction without court

approval). A Pennsylvania statute clearly affords the donor standing to enforce charitable restrictions.

(3) **Breach of Contract Theory.** The donor makes a gift to charity for a restricted purpose. Is that a contract that the donor can enforce under a breach of contract theory if the restrictions are not followed? Possibly not, but commercial litigators do not know that and make the contractual law argument anyway regarding charitable restrictions. A growing trend is to make the breach of contract argument, partly just in hopes of getting the issue before a sympathetic jury. Some recent cases have adopted the contract approach. The agreement to accept a charitable donation may be drafted to sound like a contract (or might explicitly be structured as a contract), and the agreement might specifically provide an enforcement mechanism and may grant the donor standing to enforce the agreement and might further provide that the charity is estopped from raising standing in an enforcement action. Would such an agreement foreclose the attorney general from raising the standing issue? (Some charities absolutely refuse in donor agreements to grant donors the right to sue the charity to enforce charitable agreements.)

(4) **Successor to Donor with Standing.** If the donor is able to negotiate with the charity to have standing to enforce the agreement, will the donor's estate or family have standing to enforce restrictions after the donor's death?

(5) **Entity with Standing to Enforce Restrictions.** If a "permanent donor" (i.e., an entity, such as the donor's single member LLC) makes the gift, the entity could provide for standing to enforce the gift in the donation agreement. Membership interests could pass from the donor's estate to family members, and the LLC could still enforce the restriction decades later.

c. **Enforcement Through Other Charities.** Consider providing that if the use restriction is not satisfied, the charitable gift passes to another charitable organization. That gives the other charity an incentive to pursue a failure to abide by the restriction. Larry Katzenstein offers the following example:

> I give and bequeath $10 million to Yale University to be used to endow a fulltime professorship and major in alchemy. If Yale University has failed to establish such professorship and major by the second anniversary of my death, such gift shall become the property of Harvard University for its general charitable and educational purposes. If Harvard University shall fail within a reasonable time to enforce its rights following failure by Yale University to carry out my wishes, such gift shall become the property of Brown University for its general charitable and educational purposes. I direct my personal representative to notify Harvard University and Brown University of this gift and further direct as a condition of this gift that Yale University provide annual reports to Harvard University and Brown of its progress in establishing this gift.

d. **Constructive Trust.** The constructive trust theory is a remedy used by some courts to get around the standing issue. The donation to the charity could be viewed as a trust arrangement, and the UTC does give the donor standing to enforce the trust.

e. **Streaming Gifts.** The donation might be structured as a series of donations, assuming the use restrictions are being met at the time of each donation, rather than as a single large donation. Larry Katzenstein provides this example:

> I have previously contributed $10 million to a donor advised fund (the "Fund") at the Metropolis Community Foundation. It is my wish to support X University's major in socialism studies and in furtherance of that goal, I have requested that the Fund distribute $100,000 to the University in each year, in perpetuity, in which it receives written confirmation from the University confirming that a major in socialism studies is still being offered.

f. **Carrots Instead of Sticks.** A donor might give an initial $10 million gift with a promise of an additional $10 million if the first $10 million is used as the donor wishes. From Larry Katzenstein:

> I have this day given to Yale University a $10 million endowment gift. I've also this day caused my private foundation to make a charitable pledge to the university of an additional $10 million payable on the tenth anniversary of this gift provided that in each of the university's academic years between now and that date the university shall confer at least one doctor of philosophy degree, which degree shall not be an honorary degree, on a candidate in Finnish language and literature.

Items 19-24 are observations from the seminar at the Summer Meeting: Estate Planning in a Pandemic – and Beyond by Ronald D. Aucutt (moderator), Lauren Y. Detzel, and Charles D. Fox, IV

19. Transfer Tax Legislative Landscape

a. **Biden Proposals.** Former Vice President and the Democratic Presidential nominee Joe Biden proposes ending the step-up in basis at death on capital gains exceeding $100,000. His position on transfer taxes is not clear (but the Obama administration had favored the $3.5 million exemption/45% rate approach). He proposes many other income tax changes, including rolling back for high-income taxpayers many of the individual income tax changes made in the 2017 Tax Act. For a more detailed summary of the Biden proposals, see Item 2.c. of Hot Topics Current Developments (September 2020) found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights**.

b. **Sanders "For the 99.8 Percent Act."** Senator Sanders on January 31, 2019 introduced S. 309 titled "For the 99.8 Percent Act," which would reduce the basic exclusion amount to $3.5 million (not indexed) for estate tax purposes and to $1.0 million (not indexed) for gift tax purposes and increase the rates: 45% on estates between $3.5 and $10 million, 50% on $10 million - $50 million, 55% on $50 million - $1 billion, and 77% over $1 billion. (The GST rate is not specifically addressed, so presumably it would be the highest marginal estate tax rate of 77% under §2641(a)(1), with a $3.5 million GST exemption.)

   Rep. Jimmy Gomez (D. California) introduced a similar bill in the House (H.R. 4857, with 37 other sponsors) on October 25, 2019.

   In addition, the bill would make ***major*** dramatic changes to the transfer tax system including, among other things, provisions addressing GRATs, grantor trusts, valuation discounts, limiting the period in which trusts are GST exempt, and "simplification" provisions for the gift tax annual exclusion. These changes are summarized in Item 2.e. of Hot Topics Current Developments (September 2020) found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights**.

   The Sanders bill will be the leading candidate for transfer tax legislation from Democrats because it has been around for some years. Even if Republicans continue to control the Senate, some of the provisions in the Sanders bill could be "pulled off the shelf" as pay-fors for other congressional measures (the basis consistency provision was originally in the Sanders bill and was included in legislation several years ago to help in paying for the extension of a transportation bill).

c. **Estate Tax Repeal Bills.** Republican estate tax repeal bills are filed every year, but they retain the gift tax. (One panelist speculates that some staff members want to retain the gift tax so that "when the estate tax returns there will some estates left to tax.")

20. Anti-Clawback Regulation

a. **Window of Opportunity.** The anti-clawback final regulation provides a special rule that allows the estate to compute its estate tax credit using the higher of the BEA [basic exclusion amount] applicable to gifts made during life or the BEA applicable on the date of death. Reg. §20.2010-1(c)(1). The final regulation confirms that a window of opportunity exists for transfer planning before the BEA reverts to $5 million indexed. "[T]he increased BEA is a 'use or lose' benefit that is available to a decedent who survives the increased BEA period only to the extent the decedent "used it" by making gifts during the increased BEA period." Preamble to Final Regulation at 4.

b. **No "Off-the-Top" Use of Increased BEA.** The two different places in the preamble to the final regulation confirm that the IRS does not adopt a rule allowing "donors to utilize the increase in the BEA without being deemed to have utilized the base BEA, so that the base BEA would remain available for transfers made after 2025." Preamble to Final Regulation at 8. Consider not making the split gift election, so that all gifts come from one spouse, utilizing that spouse's excess exclusion amount that is available until 2026. For this purpose, it is better for one spouse to make an $11 million gift than for both spouses to make $5.5 million gifts.

c. **Portability; Impact of Decrease in BEA on DSUE Amount.** The final regulation clarifies that "a DSUE amount elected during the increased BEA period will not be reduced as a result of the sunset of the increased BEA." Preamble to Final Regulation at 5. Examples 3 and 4 of the final regulation confirm this result. Reg. §20.2010-1(c)(2)(iii)Exs.3-4.

d. **Anti-Abuse Rule.** The preamble notes that a commenter recommended that the IRS revise the anti-clawback rule so that it would not apply to gifts that are included in the gross estate. Examples include gifts with retained life estates or with retained powers or interests or certain gifts "within the purview of chapter 14" (not identified in the preamble as gifts valued at a higher amount under §§2701 or 2702). The preamble concludes that although "such a provision is within the scope of the regulatory authority granted in section 2001(g)(2), such an anti-abuse provision would benefit from prior notice and comment. Accordingly this issue will be reserved to allow further consideration of this comment."

Clients are "whiney" about gifts—that is, WIINI: "**W**hat **I**f **I N**eed **I**t. Clients may feel more comfortable making a gift to a trust and retaining the income of the trust. The gift will be a completed gift of the full value of the transferred asset if §2702 is not satisfied and if the donor's creditors cannot reach the assets. The asset will be included at its date of death value in the gross estate under §2036(a)(1), but the date of gift value will not also be included in the estate tax calculation as an adjusted taxable gift. §2001(b) (last sentence). The effect is that the asset has been given to someone else, the date of death asset value is included in the gross estate, but at least the date of gift value is offset by the estate tax unified credit, which is increased by the amount of exclusion applied against lifetime gifts if that amount exceeds the exclusion amount available at death (for example, due to a decrease in the basic exclusion amount in 2026). The anti-abuse rule might provide that the estate exclusion amount at death might be limited to the BEA at death (not the larger exclusion amounts that had been applied to gifts when a larger exclusion amount existed) for gifts included in the gross estate. Such an anti-abuse rule could be retroactive, in the sense that the anti-abuse rule is merely an estate tax rule that could apply to all decedents dying after the publication of the anti-abuse exception to the regulation, even with respect to a gift made before the publication of that exception.

21. Transfer Planning Issues, Including Strategies for Using Current Large Exclusion

a. **Annual Exclusion Gifts.** Annual exclusion gifts are particularly important during pandemic situations in which family members may need support. Clients are asking how they can provide support assistance for their children and grandchildren.

b. **Tuition or Medical Expense Payments.** Payments of tuition for education or of medical expenses are exclusions from being treated as taxable gifts. §2503(e). The medical expense definition is extraordinarily broad (but does not cover voluntary plastic surgery).

Technical Advice Memorandum 199941013 and Letter Ruling 200602002 allowed prefunding private school tuition for grandchildren for future years. The payments could not be refunded, and payments would be forfeited if the grandchild ceased to attend the school.

c. **Long-Term Dynasty Trusts.** To maximize use of the GST exemption, make gifts to long-term trusts that last for multiple generations. Clients may want to take advantage of the increased GST exemption before it is reduced in 2026 (or in earlier legislation).

d. **Grantor Trusts.** Transfer planning often involves gifts or sales to grantor trusts. Clients pay the income tax attributable to the trust income, allowing the trust to accumulate more rapidly.

e. **SLATs.** Because of the "WIINI" phenomenon (see Item 20.d above), some clients have considered making gifts to a trust in which the grantor's spouse is a discretionary beneficiary. The grantormay wish to make gifts in a way that the grantor's spouse (or the grantor) could retain some use of the assets in case needed as a "rainy day" fund. The trust could be designed to give as much control and flexibility as possible to the grantor's spouse without creating tax or creditor concerns. The trust could still be used for the "marital unit" if the client has concerns that large gifts may unduly impoverish the grantor and his or her spouse, but the assets would not be included in the gross

estates of the grantor or the grantor's spouse. Such a trust would likely be a grantor trust as to the grantor under §677 (unless the consent of an adverse party were required for distributions to the spouse).

For a detailed discussion of SLATs and "non-reciprocal" SLATs, including a discussion of the §§2036 and 2038 issues and creditor issues, see Items 78 and 80 of the ACTEC 2020 Annual Meeting Musings (March 2020) found **here**, Item 10.i. of Estate Planning Current Developments and Hot Topics (December 2019) found **here**, and Items 15-16 of the Current Developments and Hot Topics Summary (December 2013) found **here**, all available at **www.bessemertrust.com/for-professional-partners/advisor-insights**.

f. **Trust with Grantor as Discretionary Beneficiary.** A grantor might create a trust naming the grantor directly as a discretionary beneficiary, with the possibility of it serving as a "WIINI fund" in the unlikely event that financial calamities occur, without triggering §2036(a)(1) (a transfer with an implied agreement of retained enjoyment). This only works, though, if local law does not allow the grantor 's creditors to reach the trust because of the grantor 's status as a beneficiary (or else the gift would not be a completed gift and the assets would be included in the grantor 's gross estate for estate tax purposes). Self-settled trusts (sometimes-referred to as domestic asset protection trusts, or DAPTs) may be considered in jurisdictions that allow distributions to the grantor in the discretion of an independent trustee without subjecting the trust to claims of the grantor's creditors. For a discussion of planning considerations for trusts that include the grantor as a discretionary beneficiary (or as a discretionary beneficiary at a later time), see Item 79 of the ACTEC 2020 Annual Meeting Musings (March 2020) found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights**.

Another way that a grantor might be able to "benefit" from assets in an irrevocable trust, even if the grantor is not a beneficiary, is for the grantor to borrow needed funds from the trust (with no pre-arrangement).

22. Multiple "Non-Reciprocal" SLATs

a. **Both Spouses as Beneficiaries of Trust Created by Other Spouse; Reciprocal Trust Concern.** Some clients may want to go further and have each of the spouses create SLATs for the other spouse; the issue would be whether such trusts could be structured to avoid the reciprocal trust doctrine and therefore avoid estate inclusion in both spouses' estates.

If A creates a trust for B and B creates a trust for A, and if the trusts have substantially identical terms and are "interrelated," the trusts will be "uncrossed," and each person will be treated as the grantor of the trust for his or her own benefit. *United States v. Grace*, 395 U.S. 316 (1969). In *Grace*, the trust terms were identical, the trusts were created 15 days apart, and the trusts were of equal value. The Court reasoned:

> Nor do we think it necessary to prove the existence of a tax-avoidance motive. As we have said above, standards of this sort, which rely on subjective factors, are rarely workable under the federal estate tax laws. Rather, we hold that application of the reciprocal trust doctrine requires only that the *trusts be interrelated,* and that the arrangement, to the extent of mutual value, leaves the settlors in approximately the *same economic position* as they would have been in had they created trusts naming themselves as life beneficiaries. (Emphasis added)

If the terms of the two trusts are not substantially identical, the reciprocal trust doctrine does not apply. *See Estate of Levy v. Commissioner,* 46 T.C.M. 910 (1983); PLR 200426008; *but see Estate of Green v. United States,* 68 F.3d 151 (6th Cir. 1995) (Jones, J. dissenting).

b. **Possible Distinctions to Avoid Reciprocal Trust Doctrine.** Possible distinctions that the trusts could have include the following.

- Create the trusts at different times (separated by months, not 15 days as in *Grace;* 6 months is preferable, but that would not be possible at this point for clients who want to create both trusts during this calendar year).

- Fund the trusts with different assets and different values (observe that *Grace* holds that just having different assets is not sufficient to avoid the doctrine, but it applies only to the extent of mutual value, *Estate of Cole v. Commissioner,* 140 F.2d 636 (8th Cir. 1944)).
- One trust allows distributions without any standard but the other trust imposes a HEMS standard.
- One trust might require considering the beneficiary-spouse's outside resources and the other would not.
- One of the spouses would become a discretionary beneficiary only after the lapse of some specified time (say, 5 years) or on the occurrence of some event (say, the settlor-spouse's death). For example, Letter Ruling 200426008 addresses trusts under which (i) husband would not become a beneficiary of wife's trust until three years after wife's death and then only if the husband's net worth did not exceed a specified amount and his income from personal services was less than a specified amount, and (ii) wife had a "5 or 5" power of withdrawal from husband's trust after their son's death.
- One trust includes the settlor's spouse as a discretionary beneficiary but the other trust would merely give an independent party, perhaps after the passage of some specified time, the authority (not exercisable as a fiduciary) to add that settlor's spouse as a discretionary beneficiary.
- One trust allows conversion to a 5% unitrust but the other trust prohibits that.
- Provide different termination dates and termination events.
- Provide for different remainder beneficiaries upon termination of the trusts.
- Include an inter vivos power of appointment in one trust and not the other (like in *Levy*).
- Utilize different testamentary powers of appointment (maybe one trust has one and the other does not or perhaps there are different classes of permitted appointees or perhaps in one trust the power is exercisable only with the consent of a non-adverse party).
- Use different trustees.
- Structure different removal powers (one allows the grantor to remove and comply with Rev. Rul. 95-58 but the other puts removal powers in the hands of some third party).
- Do not designate each spouse as trustee of the trust created by the other spouse. Reciprocal dispositive powers may be sufficient to invoke the reciprocal trust doctrine if the trusts are sufficiently interrelated; reciprocal economic interests may not be required. *See Bischoff v. Commissioner,* 69 T.C. 32 (1977); *Exchange Bank & Trust v. United States*, 694 F.2d 1261 (Fed. Cir. 1982).

For a more complete discussion of the reciprocal trust doctrine, authorities holding that the reciprocal trust doctrine does not apply if there are substantial differences between trusts, authorities for applying the doctrine to reciprocal powers, and related creditors' rights issues, see Item 80 of the ACTEC 2020 Annual Meeting Musings (March 2020) found **here**, Item 10.i. of Estate Planning Current Developments and Hot Topics (December 2019) found **here**, and Item 5.l of the December 2012 "Estate Planning Current Developments and Hot Topics" found **here** and available at **www.bessemertrust.com/for-professional-partners/advisor-insights.**

23. Efficient Planning Opportunities in a Pandemic Environment (Low and Volatile Values, Low Interest Rates)

a. **Loans.** Simple cash loans at historically low applicable federal rates (AFRs) can result in significant wealth transfer. For example, a loan from parent to child for nine years at the 0.38% mid-term AFR (for October 2020) could result in a significant wealth arbitrage transfer if the child could reinvest the loan proceeds to earn, for example, 5% per year. Loans similarly could be used to provide support for parents without gift consequences. Similarly, a loan from a trust to the settlor at low rates could

assist the settlor if the settlor later needed financial assistance (assisting with the WIINI concern), assuming the trustee can justify the loan from a fiduciary standpoint and assuming no pre-arrangement that such loans would be made.

b. **Refinancing Loans.** Refinancing prior loans at the much lower current AFR rates can result in significant savings to the borrower. Could the IRS assert that the refinancing results in a gift if no other consideration is given for the refinancing (such a pay-down of some of the loan, providing additional collateral, etc.)? A possible rationale for the refinancing is that the borrower could pay off the loan (assuming no prepayment penalty exists) and the lender could choose to make a new loan at the lower current rates.

c. **GRATs and CLATs.** GRATs (grantor retained annuity trusts) and CLATs (charitable lead annuity trusts) using the low interest §7520 rate (generally 120% of the mid-term AFR) can result in significant wealth transfer. The §7520 rate would clearly be used to determine the gift value of the remainder interest transfers for GRATs or CLATs.

d. **Sales.** Similarly, sales using notes at current low interest rates can result in substantial wealth transfer if the sale proceeds are invested in a way that results in growth rates significantly higher than the interest rate on the note. Most planners use the AFR, under the auspices of §7872, as the interest rate on notes for intrafamily installment sales. Section 7872 addresses the gift tax effects of "below-market" loans, and §7872(f)(1) defines "present value" with reference to the "applicable Federal rate." Using §7872 rates would seem to be supported by the position of the IRS in several Tax Court cases and in several private rulings. *True v. Commissioner*, T.C. Memo. 2001-167 ("We concluded in Frazee v. Commissioner, supra at 588-589, that section 7872 does not apply solely to loans of money; it also applies to seller-provided financing for the sale of property. In our view, the fact that the deferred payment arrangement in the case at hand was contained in the buy-sell agreements, rather than in a separate note as in Frazee, does not require a different result."), *aff'd on other grounds*, 390 F.3d 1210 (10th Cir. 2004); *Frazee v. Commissioner*, 98 T.C. 554, 588, 590 (1992) ("Nowhere does the text of section 7872 specify that section 7872 is limited to loans of money. If it was implicit that it was so limited, it would be unnecessary to specify that section 7872 does not apply to any loan to which sections 483 or 1274 apply. The presence of section 7872(f)(8) signaled Congress' belief that section 7872 could properly be applicable to some seller financing. We are not here to judge the wisdom of section 7872, but rather, to apply the provision as drafted… We find it anomalous that respondent urges as her primary position the application of section 7872, which is more favorable to the taxpayer than the traditional fair market value approach, but we heartily welcome the concept."); Letter Rulings 9535026 & 9408018 ("… the court [in *Frazee v. Commissioner*] noted that § 7872 was enacted specifically to address the gift tax treatment of below-market loans. Thus, the court concluded that the application of § 7872 is not limited to loans of cash. Rather, the term "loan" under § 7872 is broadly interpreted to include any extension of credit.") *Cf. Nelson v. Commissioner*, T.C. Memo. 2020-81 (no issue raised in case that using the mid-term AFR on a $20 million note for a sale transaction resulted in a gift).

Despite this authority, some planners have reported anecdotally that the IRS has contested (and is currently litigating) the use of the AFR for sale transactions in some situations.

24. Increased Importance and Awareness of Ancillary Documents

a. **Management of Financial Affairs; Powers of Attorney.** Planners traditionally provide for management during periods of incapacity by using powers of attorney or funded revocable trusts. Powers of attorney either can be effective immediately or can be "springing" powers that become effective upon the principal's incapacity (which leaves the practical problem of how to establish that incapacity has triggered the springing power). Florida has repealed its springing power of attorney law, effective Oct. 1, 2011; powers executed after that date are invalid if conditioned on a future date or occurrence of a future event.

Powers of attorney and revocable trusts must be coordinated (standards to determine incapacity, liability for mismanagement, etc.). The agent under the power of attorney (which might authorize transferring assets to the revocable trust) would manage assets that had not been transferred to the revocable trust prior to incapacity.

Some states require that durable powers of attorney be notarized. Be sure to satisfy execution requirements.

b. **Medical Directives and Legal Wills.** Some states combine all health care decisions into one document and other states have separate documents for general health care decisions and for the "pull the plug" decision. If separate documents are used, make sure no inconsistency exists as to who has particular powers. Planners should be sure of execution, amendment and termination procedures, which can be different for each document. Make sure to stipulate clearly any limit on an agent's authority.

Having medical directives for unmarried cohabitants is especially important. Otherwise, the companion will have no authority to provide medical consent.

c. **Storage and Access to Documents.** If the attorney retains documents, provide a mechanism for access to the documents. For example, the client may sign an escrow arrangement describing details about when the attorney could release a power of attorney to the agent (and releasing the law firm from liability if the firm acts reasonably). Some law firms include that authorization in the engagement letter. Example engagement letter forms in ACTEC Engagement Letters: A Guide for Practitioners (3rd ed. 2017), found **here**, deal with the custody of documents (in paragraphs titled "Our Policies Concerning Client Files and Original Documents").