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Steve Leimberg's Estate Planning Email Newsletter Archive Message #2500

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Subject: Alan Gassman, Christopher Denicolo, Kenneth Crotty & Brandon Ketron: The Reversible Exempt Asset Protection ("REAP") Trust for 2017 Planning

"When we look back in a year on the unexpected results of the 2016 Presidential Election, and the tendency for clients and advisors to "wait and see" what happens with estate and gift taxes, we may find that the majority of planners and decision makers erred on the side of doing nothing, costing families significant portions of their assets upon the death of loved ones in the future.

Alternatively, when we look back in five years we may find that the estate tax 'went away' but came back in harsher form, after a period of time during which those who planned ahead came out much better than those who did not. While some commentators believe that repeal of the estate tax is a strong possibility, others have pointed out the several likely alternatives that must be considered to stay two or more move moves ahead on the chess board of family wealth planning in this dynamic environment.

By our view it is crucial to give clients options that include flexible methods of taking advantage of present opportunities, while being able to change or reverse what is done, or assure that it would be wanted in a no estate tax world, while also being ahead in the non basis step up environment that may be coming.

The 'Reversible Exempt Asset Protection Trust,' also known as the Reversible Mirror Trust, allows clients to take advantage of presently available and effective estate tax planning opportunities, while providing the flexibility needed to address to the possible uncertainties that might exist the horizon, while also providing asset protection that may greatly exceed what is now otherwise in place."

Now, **Alan Gassman**, **Ken Crotty**, **Chris Denicolo** and **Brandon Ketron** provide members with their commentary on what they refer to as "The Reversible Exempt Asset Protection ("REAP") Trust."

Alan S. Gassman, **J.D., LL.M.**, is a partner in the law firm of **Gassman, Crotty & Denicolo, P.A.**, and practices in Clearwater, Florida. He is a frequent contributor to **LISI**, and has published numerous articles and books in publications such as BNA Tax & Accounting, Estate Planning, Trusts and Estates, Interactive Legal and Haddon Hall Publishing. The Alan Gassman Channel at Interactive Legal has recently opened, and features many books and resources, including many Florida and Federal based materials, forms and resources. He is also the Moderator for Bloomberg BNA's 2017 Estate Planning Webinar Series. Alan and Srikumar Rao, Ph.D. will be giving a seven hour program entitled Professional Acceleration Workshop that is free for law students, and only $125 for other attendees on Saturday, February 11th at Stetson Law School beginning at 9:00 a.m. You can contact Alan at agassman@gassmanpa.com for more information with respect to this Stetson Law School Benefit Event sponsored by InterActive Legal.

Christopher Denicolo, **J.D., LL.M.**, is a partner at the Clearwater, Florida law firm of **Gassman, Crotty & Denicolo P.A.**, where he practices in the areas of estate tax and trust planning, taxation, physician representation, and corporate and business law. He has co-authored several handbooks that have been featured in Bloomberg BNA Tax & Accounting, Steve Leimberg's Estate Planning and Asset Protection Planning Newsletters and the Florida Bar Journal. is also the author of the Federal Income Taxation of the Business Entity Chapter of the Florida Bar's Florida Small Business Practice, Seventh Edition Mr. Denicolo received his B.A. and B.S. degrees from Florida State University, his J.D. from Stetson University College of Law and his LL.M. (Estate Planning) from the University of Miami. His email address is christopher@gassmanpa.com.

Kenneth J. Crotty, J.D., LL.M., is a partner at the Clearwater, Florida law firm of **Gassman, Crotty & Denicolo, P.A.**, where he practices in the areas of estate tax and trust planning, taxation, physician representation, and corporate and business law. Mr. Crotty has co-authored several handbooks that have been published in BNA Tax & Accounting, Estate Planning, Steve Leimberg's Estate Planning and Asset Protection Planning Newsletters and Estate Planning magazine. Mr. Crotty is a co-author of the

BNA book Estate Tax Planning in 2011 & 2012. His email address is ken@gassmanpa.com.

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Here is their commentary:

EXECUTIVE SUMMARY:

When we look back in a year on the unexpected results of the 2016 Presidential Election, and the tendency for clients and advisors to "wait and see" what happens with estate and gift taxes, we may find that the majority of planners and decision makers erred on the side of doing nothing, costing families significant portions of their assets upon the death of loved ones in the future.

Alternatively, when we look back in five years we may find that the estate tax "went away" but came back in harsher form, after a period of time during which those who planned ahead came out much better than those who did not.

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In other words, while some believe that the estate tax is facing the ghoulish prospect of the grim REAPer, we think that knowledgeable advisors should be embracing the REAP Trust.

FACTS:

When Mr. Trump was elected on November 9, the possibility of a repeal or at least a substantially modified estate tax system, became closer to a reality. Mr. Trump has not formally announced a detailed proposal on the estate tax, but his campaign website offered the following:

The Trump Plan will repeal the death tax, but capital gains held until death and valued over $10 million will be subject to tax to exempt small businesses and family farms. To prevent abuse, contributions of appreciated assets into a private charity established by the decedent or the decedent’s relatives will be disallowed.1

It remains to be seen how (or if) this proposal or something similar thereto will be developed into law, and how it will apply from a practical standpoint. During his campaign and since he has been elected, Mr. Trump has discussed many objectives other than estate tax repeal that have received a lot more attention and have generated and likely will continue to generate much debate. Accomplishing these objectives, and being postured for re-election in 2020 will require the expenditure of much political capital, which could limit, delay, or hinder the possibility of significant estate tax law changes, and increase the likelihood that any estate tax law changes will occur only as part of changes to the budget. Further, under the Byrd Rule, any legislation which affects the budget can only be effective for ten (10) years unless a three-fifths (3/5) majority in the Senate (i.e., sixty (60) senators) vote for such legislation.

With the Republicans currently having a slim majority of fifty-two (52) in the Senate, it is unlikely that the sixty (60) senators threshold would be overcome in order to avoid the Byrd Rule from restricting estate tax legislation from sun setting in ten (10) years. Given the amount of political capital that is likely to be expended by Mr. Trump on other issues which were on the forefront in the campaign process, and the present controversy with respect to Russia's alleged involvement in the election, it is unlikely that there will be a standalone estate tax elimination bill that is not tied to the budget.

In short, we cannot be sure if anything is going to happen to the estate tax, or if any such changes to the estate tax will sunset within the next decade or so to cause to the estate tax to come back with a vengeance to apply to a greater fraction of the population than the current law. Accordingly, a sound estate planning structure needs to be fluid and malleable to account for whatever lies beyond the horizon.

COMMENT:

The Reversible Exempt Asset Protection Trust operates in a conventional way- it is an irrevocable trust established by an individual for the benefit of his or her spouse and/or descendants. It allows for assets to be held thereunder for the benefit of the grantor's desired beneficiaries in a protective manner where the assets can be protected from the beneficiaries' creditors, and can be exempt from federal estate tax at their levels under current law (and, more than likely, under any new estate tax regime espoused by Mr. Trump's administration). Also, presumably, the assets can be shielded from a possible capital gains income tax on the death of the grantor or other family members if the Canadian style tax on appreciated property upon death is enacted.

However, a key difference from the conventional dynasty trust is that the Reversible Exempt Asset Protection Trust will be established in an asset protection jurisdiction, and the Trust will name a committee of independent trust protectors who have the power to amend the Trust under certain circumstances. Specifically, the trust protectors' authority will include the power to cause the transfer of the Trust the assets back to the grantor under limited conditions as determined in their discretion, such as if the grantor's net worth ever drops below a certain level, or if the federal estate law is ever repealed or is no longer considered to be a concern to the family.

It is important that the Trust be drafted as a domestic or offshore asset protection trust, and that it be sitused in a jurisdiction that provides for the protection of the Trust assets from the creditor of the grantor despite the possibility of the grantor becoming a beneficiary of the Trust. Under PLR200944002, assets held under a self-settled trust under which the grantor was a discretionary beneficiary was protected from the creditors of the grantor based upon Alaska law and found to not be includable in the estate of the grantor for federal estate tax purposes. The jurisdiction in question in this PLR was Alaska, and the grantor was a resident of Alaska when the trust was established and when the ruling was given. Some commentators have expressed concern that having the resident of non APT jurisdiction use a domestic asset protection jurisdiction will not be sufficient because the Full Faith and Credit Clause of the United States Constitution or conflict of law rules may allow a creditor holding a judgment against the grantor in another state to access the assets of the trust. Commentary to the Uniform Voidable Transfers Act supports this hopefully incorrect position, although the Huber2 case gives planners some pause as to setting up a domestic asset protection trust in a state in which the grantor does not reside.

In the Huber case, an Alaska asset protection trust was set up by a Washington resident for the obvious purpose of avoiding creditor claims involving real estate outside of Alaska that was held indirectly via LLC's by the trustee. The grantor's creditors were able to reach the assets under the trust due to the Bankruptcy Court finding that Washington state law applied to the trust, rather than Alaska law, due to Washington having the most significant relationship to the trust and the trust having minimal contacts with Alaska. This is why the ability of the Trustee to benefit the grantor of the trust is best non-existent unless or until an issue of independent significance exists.

Most planners agree that it is safest to establish the trust in an offshore asset protection jurisdiction, such as Nevis, the Cook Islands, or Belize, which each has well-developed trust law, if the client resides in a non-asset protection trust state and wishes to be a discretionary beneficiary from the beginning.

The Trust also will normally include a committee of independent trust protectors whose powers must be carefully drafted in order to prevent estate tax inclusion of the Trust assets in the estate of the grantor upon creation of the Trust. For example, the grantor should not have any power to remove and replace any of the trust protectors, nor should the grantor have any power or authority to exercise the trust protectors' powers. Further, the trust protectors' exercise of power should not be conditioned upon the approval of the grantor or any individual who is related or subordinate to him (such as his or her spouse, children, parents, or siblings), and may be conditioned upon events that are beyond the control of the grantor and the trust protectors.

The trust protectors' powers should be exercisable only in their sole and absolute discretion, and may include the power to add the grantor as a beneficiary of the trust if his or her net worth drops below a certain level that is unforeseen and independently significant.

Additionally, because the trust protectors will have a wide latitude under the Trust documents, it is important to assure that the parties appointed are trusted individuals or financial institutions with appropriate checks and balances in place between them. The authors typically recommend that the committee consist of at least three trust protectors, and that there is a clearly articulated mechanism for the succession and possible replacement thereof by other trust protectors or by another independent party. **Alexander Bove**'s wonderful writings on Trust Protectors should be reviewed carefully by anyone drafting trusts of this nature.

In situations where the client has considered or has undertaken the process of making transfers to an irrevocable trust for the benefit of his or her spouse and/or descendants, drafting the trust as a Reversible Exempt Asset Protection Trust with trust protectors does not require significant restructuring. The Reversible Exempt Asset Protection Trust can have the same dispositive and trusteeship provisions as a pre-existing irrevocable dynasty trust that the client has established, and may be merged into existing trusts if and when it becomes apparent that this is in the best interests of the family.

Further, a client who has considered entering into an installment sale or private annuity sale to a pre-existing irrevocable dynasty trust that has an independent net worth of sufficient assets as ballast capital may instead sell assets to the new Reversible Exempt Asset Protection Trust in exchange for the installment note or private annuity. The Reversible Exempt Asset Protection Trust can provide for the same beneficiaries as the pre-existing trust, and the pre-existing trust can guarantee the installment or private annuity obligation of the new Reversible Exempt Asset Protection Trust which is owed to the client.

The Reversible Exempt Asset Protection Trust can be drafted as a grantor trust for federal income tax purposes so the client will be responsible for paying any taxes associated with the trust's income, and the client can engage in an installment sale transaction with the Trust without causing any adverse income tax consequences. This can allow the Trust's assets to grow on a tax-free basis, while allowing the grantor to engage in future transactions with the trust (such as installment sale or private annuity transactions) with any income taxes resulting from any such transactions.

A similar approach was articulated by **Marty Shenkman** and **Jonathan Blattmachr** in a recent presentation on planning for the possible new estate tax regime. They have discussed the advantages of using a "Hybrid Asset Protection GRAT" as a very desirable planning strategy in light of the uncertainty that is on the horizon. This technique involves a grantor establishing a grantor retained annuity trust (GRAT) in an asset protection jurisdiction where trust protectors would also have the right to directly or indirectly allow assets to pass to or for the benefit of the grantor. By using a zeroed-out GRAT that is drafted to provide that the annuity payments owed back to the grantor are based on a percentage of the initial contribution, and that the trust protectors under the GRAT have the discretion to distribute additional assets to the grantor, flexibility is attained if circumstances change or the estate law materially changes. The Hybrid Asset Protection GRAT is one variety of Reversible Exempt Asset Protection Trust that can help families with significant wealth navigate the present not so calm waters very successfully.

If the estate tax is permanently eliminated, the Reversible Exempt Asset Protection Trust could be merged into the pre-existing dynasty trust, or the assets thereof could be distributed back to the grantor by the trust protectors. If the estate tax remains in its current form, or continues to be a concern for the client, then the assets can remain under the Reversible Exempt Asset Protection Trust and escape the impositions of federal estate tax on the death of the grantor, and perhaps at the levels of his or her descendants.

Conclusion

A great many planners have clients who have spent a lot of time and money working on their estate plans that are currently in process, or have sales, liquidity, repaid growth in value, high earnings or near death situations that call for conventional planning. Planners are unsure what to tell their clients in light of this uncertainty. It is incumbent upon planners to inform and educate their clients of all options and alternatives, to make them aware of possible risks and downside that could occur if laws do not change, or if the tax law system is different from what is expected. The REAP Trust provides planners with a tool can be used effectively in differing estate tax climates to achieve the clients' planning objectives, tax and otherwise, while also providing significant asset protection opportunities that should not be ignored.

YOU CAN'T SOW WHAT YOU DON'T REAP!

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Alan Gassman

Chris Denicolo

Ken Crotty

Brandon Ketron

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CITATIONS:

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[1] *See*, https://www.bna.com/trump-plan-repeals-n57982077269/.

[2] *Waldron v. Huber (In re Huber)*, 2013 WL 2154218 (Bk. W.D. Wa., Slip Copy, May 17, 2013).