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The Uses of Grantor Trusts in Estate Planning

The Responsibilities & Duties of an Executor

planning matters

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the uses of **grantor trusts** in estate planning

by Anne Marie Robbins, Esq. & Lauren Mulcahy, Esq.

Grantor trusts can provide substantial estate and income tax savings to those who establish them. The grantor of a "grantor trust" is treated as the owner of the trust assets for federal income tax purposes. The grantor continues to pay the income tax generated by the assets contributed to the trust and receives the benefit of all deductions and credits. Whether the grantor trust property is excluded from the estate of the grantor, and thus escapes estate tax, is dependent on the drafting of the trust. The rules regarding grantor trusts can be found in Sections 671 through 679 of the Internal Revenue Code.[1]

It is beneficial for the grantor to be treated as the income tax owner of a trust because trusts have more compressed tax brackets than do individuals. For example, in 2022, individuals were taxed at the highest marginal rate of 37% on income over $539,900, or $647,850 for married taxpayers.[2] Trusts, however, reached the top marginal rate of 37% at income above $13,450.[3]

In general, the following provisions in a trust will create a "grantor trust."

- The grantor holds power to cause trust assets to revert to the grantor.[4]
- The grantor or non-adverse party retains the power to affect the interests of the beneficiaries.[5]
- The grantor, spouse of the grantor, or a non-adverse party, has the power to deal with the trust assets for less than full and adequate consideration.[6]
- There is a specific power in a non-adverse party to lend to the grantor or grantor's spouse from the trust without adequate security or interest.[7]
- The grantor borrows from the trust without repayment before the beginning of the next tax year.[8]
- The grantor or a non-fiduciary has the power to vote closely held stock or control investments, unless consent of a fiduciary is required.[9]
- The grantor or a non-fiduciary has the power to re-acquire assets by substituting assets of equivalent value.[10]
- The trust allows the distribution of income for the benefit of the grantor or the grantor's spouse.[11]

Grantor trusts allow for income tax free growth in the trust because the grantor pays the tax without being considered to have made further gifts to the trust, thus preserving the grantor's estate and gift tax exemption to shelter other gifts. A grantor trust may allow for the exchange of low basis assets for higher basis assets, thereby providing for those assets a step-up in basis at the grantor's death.

Many different types of trusts are considered "grantor trusts." Revocable trusts are always grantor trusts. In addition, several types of irrevocable trusts can be considered grantor trusts. For example:

- **An Irrevocable Life Insurance Trust ("ILIT")** is designed to hold life insurance policies in order to keep the policy proceeds out of a grantor's taxable estate.
- **A Grantor Retained Annuity Trust ("GRAT")** allows a grantor to transfer property to a trust and retain the right to an annuity payable for a term of years. The appreciation on the assets contributed is removed from the grantor's estate for federal estate tax purposes.
- **A Spousal Lifetime Access Trust ("SLAT"),** to which assets are transferred during a grantor's life, secures the current federal estate and gift tax exemption of $12,920,000.
- **A Beneficiary Deemed Owner Trust ("BDOT")** allows the beneficiary to be treated as the owner of the trust for income tax purposes.

The advantages of grantor trusts are numerous, and we urge you to reach out to your estate planning attorney if you believe you might benefit from grantor trust planning.

1. IRC §§ 671–679.
2. Rev. Proc. 2021-45.
3. Id.
4. IRC § 673.
5. IRC § 674.
6. IRC §675(1).
7. IRC §675(2).
8. IRC §675(3).
9. IRC §675(4).
10. IRC §675(4).
11. IRC §677.

the responsibilities & duties of an executor

by James K. Estabrook, Esq. & Elizabeth Candido Petite, Esq.

After someone passes away, their estate must be administered. This is true whether the person was worth $10,000 or $10 million. The process of administering the estate is often the same regardless of its value. This article discusses the basic process of estate administration and the duties of the executor, who is the person or persons responsible for the process.

Appointment to act on behalf of the estate

The first step for an executor (or administrator, if there is no Will) is to be appointed by the local Surrogate's Court as executor. In New Jersey, this is a simple process where the Will and death certificate are presented to the court, along with the names and addresses of the next-of-kin and beneficiaries named in the Will. Assuming everything is in order, the Surrogate will admit the Will to probate and issue a Certificate of Letters Testamentary to the executor, which serves as his or her official appointment to act on behalf of the estate. The executor is then responsible for notifying all heirs and beneficiaries that probate has been completed.

Marshalling assets

The executor or administrator (once appointed, the responsibilities are the same) must then collect, or marshal, all of the decedent's assets. Typical assets include bank and brokerage accounts, real estate, business interests, tangible personal property (such as cars), life insurance policies and retirement assets. The latter two often have "designated beneficiaries" listed on the accounts, in which case those assets pass directly to those beneficiaries and the executor does not need to collect them as part of the estate. Likewise, assets that are owned jointly often pass directly to the surviving owner without having to pass through the estate.

Finding and collecting all of these assets can range from being very simple to incredibly complex, depending on how organized the decedent's finances were (and how involved the executor was prior to death). Often the executor must monitor the decedent's mail for bank statements, review prior years' tax returns, and write to various financial institutions asking if the decedent had any accounts there.

The executor will need to open an estate bank account and transfer the decedent's individual bank and brokerage accounts into the estate account in order for the executor to access those funds. The estate account is also where any refund checks payable to the decedent or estate (for example, an income tax refund), or the proceeds from the sale of assets, such as real estate, can be deposited.

Paying debts & administration expenses

The executor and estate beneficiaries are not personally liable for any debts of the decedent, but they must be paid from estate assets, to the extent that the estate has sufficient assets, before any amounts can be distributed to the beneficiaries. Thus, the executor must identify all debts and creditors of the estate and pay those debts, or negotiate payment, within a reasonable time after death. Debts include medical expenses from the decedent's last illness, credit card payments, taxes, and any expense relating to their personal residence.

Estate expenses include items such as the funeral and burial expenses, professional fees to administer the estate (e.g., attorney's fees, accountant's fees, appraisal fees), and death taxes.

The executor is responsible for filing the decedent's final income tax return. We recommend that a final income tax return always be filed even when no tax is due to put the taxing authorities on notice of the decedent's death. The estate may also be liable for income taxes if the estate assets have generated income after the decedent's death, for example, interest or dividends earned or realized gains from the sale of securities.

The executor may also be responsible for filing estate and inheritance tax returns and paying any tax that is due. Estate tax returns are due if the estate exceeds the exemption amount at the time of the decedent's death, which currently is $12.92 million for federal estate taxes. In addition, estates that are under the threshold may decide to file a return to elect "portability" if there is a surviving spouse. New Jersey abolished its estate tax in 2018, but other states have state estate tax, which applies to residents of those states and may also apply to nonresidents who own property in those states. New Jersey still has an inheritance tax, which is imposed on bequests to anyone other than a surviving spouse, direct ancestor or descendant of the decedent, or a charity.

The executor should work with an attorney to determine the tax liabilities of the estate to ensure that they are properly met, as an executor may be personally liable for unpaid taxes.

Any debts and expenses that have been paid by someone personally—which is usually the case with the funeral and burial expenses—can be reimbursed from estate assets once the executor has collected the assets.

Distributions to beneficiaries

Once all of the estate assets have been collected, and debts and expenses have been satisfied, the executor is ready to distribute the estate to the beneficiaries in accordance with the terms of the Will. However, first the executor should provide an accounting to the beneficiaries to inform them of what occurred during the estate administration. In its simplest form, this could be bank account statements, or it can be a formal accounting presented to the Surrogate for approval. Because the executor must account, it is imperative that he or she keep detailed records during the estate administration. Once the accounting has been approved by the beneficiaries, and they have signed a refunding bond, the executor can distribute the remaining assets and close the estate.

Conclusion

The entire estate administration process often takes at least 12–18 months to complete, depending on the complexity of the assets and whether any estate or inheritance tax returns are due (and if they are audited). An executor may make interim distributions to beneficiaries during the process, if the executor determines that doing so is prudent.

Because administering an estate can be a complex process, executors should consider engaging an attorney to assist them. Executors, like all fiduciaries, are held to strict standards because they are responsible for assets that belong to others. Working with professionals will ensure that executors are not in breach of these duties.

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