



Year-end planning guide (2021): trust planning and administration

By Todd D. Mayo and Richard Lowry

The Year-End Planning Guide (2021) is a seven-part series of whitepapers, each of which focuses on a particular aspect of planning. In this whitepaper, we focus on trust planning and administration.

In this whitepaper, we describe the laws in effect at the time of publication. Some of these laws may be changing. Lawmakers are deliberating possible tax legislation. For a discussion of possible tax law changes, see the Advanced Planning Group's alerts and other publications.¹

MAKING YEAR-END DISTRIBUTIONS FROM NONGRANTOR TRUSTS

If you are the settlor or beneficiary of a nongrantor trust, you might ask the trustee to consider distributing the trust's income (and, depending on the terms of the trust, the trust's capital gains) to the beneficiaries who are taxed at lower rates than the trust. This may be more tax efficient, because trusts are subject to compressed income tax brackets and a lower threshold for the 3.8% net investment income tax.

Under the 65-day rule, the trustee may make a distribution within the first 65 days of 2022

¹ See, e.g., Brad Dillon and Benjamin Traves, *House Democrats Move One Step Closer to Tax Increases*,

Offering Details and Dates, September 14, 2021 (a publication of the UBS Advanced Planning Group).

and, for tax purposes, treat it as being made on December 31, 2021. This gives the trustee some extra time to evaluate whether to make a distribution. Of course, the trustee should consider the tax status, goals, and objectives of the trust and beneficiaries before making any tax-motivated distributions to any of the beneficiaries.

CONSIDERING WHETHER TO TOGGLE OFF GRANTOR TRUST STATUS

If you created a trust that is a grantor trust with respect to you, you might consider whether you should toggle off grantor trust status. A grantor trust is disregarded for federal income tax purposes. If a trust is a grantor trust with respect to you, you must report all of the trust's income on your income tax return. When you pay the taxes for the trust, you are allowing the trust property to accumulate without any diminution due to taxes. That's like making a gift to the trust without using any of your lifetime exemption.

While it's often advantageous for a trust to be a grantor trust, you potentially may find the tax bite becomes unpalatable. In some cases, the trustee may have a discretionary power to reimburse you for the income taxes that you pay. Additionally, if your spouse is a beneficiary of the trust, then the trustee might be able to make a distribution to your spouse, freeing up other resources so that you can more comfortably pay the taxes attributable to the trust. These approaches, however, aren't always viable.

Sometimes, the best option is to toggle off grantor trust status. You usually can cause a trust to become a nongrantor trust—and thus its

own taxpayer—by releasing certain powers that you have under the terms of the trust. For example, you may have the power to swap or substitute assets, or you may have the power to borrow from the trust. By releasing those powers, you might be able to toggle off grantor trust status, so that you will no longer be taxable on the trust's income. In some cases, the process for converting a trust from a grantor trust to a nongrantor trust is more involved.

Of course, it's important to think through all of the ramifications of toggling off grantor trust status. For example, converting a trust from a grantor trust to a nongrantor is an inclusion event with respect to any qualified opportunity fund, causing the immediate recognition of any deferred gains. A conversion also might trigger certain gains.

REVIEWING TRUST STRUCTURES

If you created a trust that owns an interest in a family-controlled limited partnership or limited liability company, you should consider reviewing the structure to ensure that it achieves your tax and other objectives. As discussed in the *Year-End Planning Guide (2021): Wealth Transfer Planning*, it can be important to ensure that the structure is properly designed and administered. For example, if you created the trust and are a manager of a trust-owned limited liability company, it may be best to have an independent manager who makes decisions about distributions from the limited liability company to the trust.

Todd D. Mayo is a Senior Wealth Strategist in the Advanced Planning Group, and Richard Lowry is an Associate Wealth Strategist in the Advanced Planning Group.

ADVANCED PLANNING GROUP

The Advanced Planning Group consists of former practicing estate planning and tax attorneys with extensive private practice experience and diverse areas of specialization, including estate planning strategies, income and transfer tax planning, family office structuring, business succession planning, charitable planning, and family governance.

The Advanced Planning Group provides comprehensive planning and sophisticated advice and education to UHNW clients of the firm. The Advanced Planning Group also serves as a think tank for the firm, providing thought leadership and creating a robust intellectual capital library on estate planning, tax, and related topics of interest to UHNW families.





Disclosures

This report is provided for informational and educational purposes only. Providing you with this information is not to be considered a solicitation on our part with respect to the purchase or sale of any securities, investments, strategies or products that may be mentioned. In addition, the information is current as of the date indicated and is subject to change without notice.

Neither UBS Financial Services Inc. nor its employees (including its Financial Advisors) provide property and casualty insurance, tax, or legal advice. You should consult with your legal counsel and/or your accountant or tax professional regarding the legal or tax implications of a particular suggestion, strategy or investment, including any estate planning strategies, before you invest or implement.

Best Interest Disclaimer

As a firm providing wealth management services to clients, UBS Financial Services Inc. offers investment advisory services in its capacity as an SEC-registered investment adviser and brokerage services in its capacity as an SEC-registered broker-dealer. Investment advisory services and brokerage services are separate and distinct, differ in material ways and are governed by different laws and separate arrangements. It is important that clients understand the ways in which we conduct business, that they carefully read the agreements and disclosures that we provide to them about the products or services we offer. A small number of our financial advisors are not permitted to offer advisory services to you, and can only work with you directly as UBS broker-dealer representatives. Your financial advisor will let you know if this is the case and, if you desire advisory services, will be happy to refer you to another financial advisor who can help you. Our agreements and disclosures will inform you about whether we and our financial advisors are acting in our capacity as an investment adviser or broker-dealer. For more information, please review the PDF document at ubs.com/relationshipsummary.

Original Publication Date: October 2021

Approval Code: IS2105425

Expiration Date: 10/31/2022

© UBS 2021. All rights reserved. The key symbol and UBS are among the registered and unregistered trademarks of UBS. UBS Financial Services Inc. is a subsidiary of UBS AG. Member FINRA/SIPC.