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Taking Advantage of Favorable Estate Tax Laws: Spousal Lifetime Access Trusts

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If you've been keeping an eye on the estate tax exemption level, you already know that it has varied dramatically over the past two decades. In 2007, the estate tax exemption was $2 million. In 2020, the level rose to $11.58 million, with inflation adjustments scheduled for the years 2021 through 2025. Now, we are once again in a cycle where the exemption amount could either "sunset" back down to approximately $6 million on January 1, 2026 or be changed in the near term by legislation to a more permanent and/or lower amount. Given this uncertainty around where the estate tax exemption level will be set in the coming years, our approach is to hope for the best and plan for all scenarios. We do this by looking for opportunities to do smart estate planning—in other words, planning that provides for your goals while also offering the potential for tax savings.

"A man who does not plan long ahead will find trouble at his door."
– Confucius

The Basics of a Spousal Lifetime Access Trust

One opportunity you may consider is a spousal lifetime access trust, or SLAT. Unlike other types of marital trusts that are only established upon death, a SLAT is an irrevocable trust that you set up during your lifetime for the primary benefit of your spouse. You create the trust and name your spouse as the primary beneficiary and sometimes the trustee, either alone or with a co-trustee. The SLAT is usually designed so that any assets gifted to it, along with any growth on those assets, are not included in either your taxable estate or your spouse's taxable estate. However, your spouse has access to these funds during his or her life; because of that you also benefit indirectly from that access.

The assets transferred to a SLAT can only be accessed by your spouse and, depending on how you establish the trust, maybe your children and grandchildren. SLATs are quite flexible, so you can also draft the trust such that the assets can be used only for certain purposes. Some clients include provisions in their SLAT so that in the event of a divorce, the spouse is no longer a beneficiary. Other clients look to ensure they have life insurance in place so that if the spouse who is beneficiary of the SLAT passes first, there is a death benefit to help support the surviving spouse. Still other clients take the opportunity to have the spouse who is beneficiary of the first SLAT create a SLAT for their spouse as well with their own assets. If this is something you are considering, it is important to keep in mind that if you and your spouse both create SLATs at the same time with the same exact provisions for the benefit of each other, you may run afoul of gift tax regulations or the reciprocal trust doctrine.

Advantages of Creating a SLAT

There are a number of potential benefits that come with creating a SLAT:

- **Optimization of the estate tax exemption during your lifetime.**
  When you transfer assets to the SLAT, you utilize some of your lifetime estate and gift exemption. This may help you optimize what you can pass on free of estate tax in the event the exemption amount is reduced in the future.
- **Asset protection.**
  When you create a SLAT, you are putting assets into an irrevocable trust for another person's benefit and giving up all use and control of those assets. As a result, those assets are usually not considered yours for attachment in case of litigation or bankruptcy.
- **Creditor protection.**
  If you appoint an independent trustee who decides how and when distributions are made to your spouse, you may be able to provide creditor protection for your spouse as well.

Key Takeaway

A SLAT is an estate planning tool that is straightforward in its implementation and ongoing administration. Consider talking to your financial advisor about layering a SLAT into your own planning to take advantage of the current exemption level.

About the Author

Michael Aronson is a Financial Advisor, Family Wealth Advisor and Head of the Flagler Group at Morgan Stanley. The Flagler Group helps accomplished families and individuals navigate the challenges and complexities of wealth. Mike leads the team in expanding our understanding of each of our clients, looking for risks and opportunities, even beyond their investment portfolios. Our mission is to help our clients achieve a feeling of comfort and preparedness, knowing they can address the important financial decisions that will impact them and their family. Mike can be reached by email at Michael.D.Aronson@MorganStanley.com, or by phone at 561.820.2347. His office is located at 777 S. Flagler Drive, Suite 700E, West Palm Beach, Florida, 33401.

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