Trust Design for State Income Tax Efficiency and Wealth Preservation

Focus on Incomplete Non-Grantor Trusts
We hope you enjoy the latest presentation from Northern Trust’s Line of Sight. By providing research, findings, analysis and insight on the effects and implications of our changing financial landscape, Line of Sight offers the clarity you need to make better informed decisions.
Focus on Incomplete Non-Grantor Trusts

As we plan for and manage our wealth to achieve the goals we have set, we navigate an ever-changing landscape of taxation. Identification of one’s goals is always the starting point. The process for implementation of those goals is complex and requires input from advisors.

The significance of tax considerations varies based on one’s circumstances and the tax environment. There are a number of current tax trends of note:

■ Marginal federal income tax rates on ordinary income, qualified dividends and capital gains have increased;
■ The 3.8% Medicare contribution tax on net investment income has come into effect;
■ State income tax rates have increased in many states or state tax may now apply to trusts which were exempt from state tax under prior law;
■ Combined federal and state income and Medicare contribution taxes in certain circumstances exceed 50%,¹ and can even approach 60%;²
■ The federal gift, estate and generation-skipping transfer tax rate is at a relatively low 40% rate;
■ The exclusion for the federal gift, estate and generation-skipping transfer tax has been permanently set at a historically high $5,000,000, adjusted annually for inflation; and
■ Many states no longer impose an estate or inheritance tax.

The increasing significance of income taxation in general and of state income taxes in particular, causes us to focus on opportunities to design trusts for income tax efficiency. One such opportunity is what is referred to as an incomplete non-grantor trust, commonly established under the state law of Nevada (a “NING”) or Delaware (a “DING”), both of which permit self-settled domestic asset protection trusts.
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INCOMPLETE NON-GRANTOR TRUSTS

An incomplete non-grantor trust is a trust designed to be an incomplete gift for gift tax purposes but, at the same time, treated as a taxpayer separate from the grantor for state income tax purposes resident in a state with favorable income taxation of trusts.

Incomplete gift. Because the transfer to the trust is not a completed gift it is not necessary to apply any gift tax exclusion to the trust, which is helpful for a grantor who has fully utilized her federal gift tax exclusion or wishes to preserve her exclusion for potential future transfers. The trust will be included in the grantor’s estate and the assets of the trust estate will receive a basis adjustment to their value at the grantor’s death or the federal estate tax alternate valuation date. Where long-term income tax planning is a priority, the basis adjustment at death can be a significant benefit.

Non-grantor trust separate from grantor. A trust that is a non-grantor trust is treated as a separate taxpayer for income tax purposes. As a separate taxpayer, the residence of the trust for state income tax purposes is determined under the state law with respect to trusts. Where state tax residence is determined based on factors other than the residence of the grantor, it is possible to locate the trust in a state with tax rates that are lower than those in the grantor’s home state. The tax savings opportunity in this regard pertains to state income taxation, not federal.

<table>
<thead>
<tr>
<th>The Grantor’s Goals</th>
<th>Advantages of the Incomplete Non-Grantor Trust</th>
</tr>
</thead>
<tbody>
<tr>
<td>The grantor desires to establish an irrevocable trust without giving up a basis adjustment for trust assets at death and without using his federal gift tax exclusion or paying gift tax.</td>
<td>Assets held in an incomplete non-grantor trust at death (including appreciation from current value) are included in the grantor’s gross estate and basis is adjusted to date of death or alternate valuation date value. Transfers to the trust are not completed gifts and no applicable exclusion is applied at the time of the transfer to the trust.</td>
</tr>
<tr>
<td>The grantor resides in a high income tax rate jurisdiction such as New Jersey or California and is sensitive to state and local income tax burdens.</td>
<td>A trust properly established as a separate taxpayer in Delaware or Nevada is not subject to New Jersey or California income taxes provided there is no trust nexus with the home state (such as a resident trustee) and no state source income.</td>
</tr>
<tr>
<td>The grantor has substantial assets outside the trust and desires to preserve a “nest egg” for his family and potentially himself.</td>
<td>Trust assets may be protected from the creditors of the grantor and beneficiaries as permitted under applicable state and federal law.</td>
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</tbody>
</table>

Evaluating whether an incomplete non-grantor trust is a sensible planning strategy requires an assessment of the level of the anticipated tax, asset preservation and related benefits, and the expenses, complexity and uncertainties associated with the creation and ongoing administration of the trust.
Evaluating whether an incomplete non-grantor trust is a sensible planning strategy requires an assessment of the level of the anticipated tax, asset preservation and related benefits, and the expenses, complexity and uncertainties associated with the creation and ongoing administration of the trust. The timing of creating the trust and funding the trust is an important consideration. An incomplete non-grantor trust can be of material benefit for a grantor with significant appreciated assets who anticipates a future liquidity event. For example:

<table>
<thead>
<tr>
<th>Facts</th>
<th>Grantor Holds Assets</th>
<th>Trust Holds Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>$10,000,000 assets with $1,000,000 basis</td>
<td>Generally $2,142,000 federal tax upon sale</td>
<td>Generally $2,142,000 federal tax upon sale</td>
</tr>
<tr>
<td>Grantor resident of state with 10% income tax rate</td>
<td>Generally $900,000 state tax upon sale</td>
<td>Generally $0 state tax upon sale</td>
</tr>
<tr>
<td>Federal long-term capital gain and Medicare contribution tax 23.8%</td>
<td>Generally $6,958,000 after-tax assets remaining for continued investment</td>
<td>Generally $7,858,000 after-tax assets remaining for continued investment</td>
</tr>
<tr>
<td>Non-grantor trust established in state with no income tax</td>
<td></td>
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</tbody>
</table>

It is important to note that state tax authorities may challenge abusive transactions that are designed primarily to avoid the imposition of state income taxation on a particular transaction, such as the disposition of a block of highly appreciated stock. There might be more risk associated with, for example, funding a trust with assets that are certain or even highly likely to be sold shortly after the creation of the trust or with assets the grantor may require to sustain his standard of living. A trust can become even more vulnerable to challenge if a sale of its principal asset were followed by a distribution back to the grantor of all, or a substantial portion, of the proceeds. The grantor’s home state taxing authority could view such a transaction as a “sham” and might attack it on the basis of substance over form, assignment of income, or some similar theory that would effectively disregard the non-grantor trust and treat the grantor as the true seller. The grantor should understand that he has no entitlement to future distributions.

**SAMPLE TRUST DESIGN**
Consider the following incomplete non-grantor trust design based upon a recent private letter ruling issued by the Internal Revenue Service:

- The trust is for the benefit of the grantor and his issue (inclusion of the grantor’s spouse is not addressed in the ruling).
- The trust is irrevocable.
- The trustee of the trust is a trust company located in a state that allows self-settled asset protection trusts.
The trust agreement provides for a distribution committee initially comprised of the grantor and the grantor’s four adult children.

The distribution committee ceases to exist at the grantor’s death and is deemed not to exist if there are less than two qualified family members.

During the grantor’s lifetime, the trustee must distribute income and principal to the grantor and his issue as directed by the distribution committee and/or the grantor as follows:

— **Grantor’s consent power.** A majority of the distribution committee members, with the written consent of the grantor, may direct the trustee to distribute net income or principal to the grantor or the grantor’s issue.

— **Unanimous member power.** All of the distribution committee members, other than the grantor, may direct the trustee to distribute net income or principal to the grantor or the grantor’s issue.

— **Grantor’s sole power.** Grantor, individually and not as a fiduciary, may distribute to his issue principal for health, education, maintenance and support.

The Internal Revenue Service has considered a trust of this type to be an incomplete gift as to the grantor and a separate taxpayer for federal income tax purposes. The Internal Revenue Service also ruled that distributions by the distribution committee would not be considered gifts by a committee member. However, a word of caution is in order. A private letter ruling is, as its name implies, private in the sense that it may only be relied upon by the taxpayer to whom the ruling is issued (and only for federal, not state, tax purposes). It is not direct authority upon which other taxpayers can rely. So, while this private letter ruling is instructive (and we refer to it in this discussion as the sample trust), it is not definitive.

**INCOMPLETE GIFT PLANNING FOR GIFT TAX**

How does one design a trust that will not be treated as a completed gift for gift tax purposes but will be considered a taxpayer separate from the grantor for income tax purposes? The challenge is to structure the trust so that the grantor has sufficient control to keep her contributions to the trust from being treated as completed gifts, but insufficient control to require that she be treated as the owner of the trust’s income. The strategy is dependent upon a degree of mismatching, so to speak, in the federal gift tax provisions and federal income tax provisions. The gift tax issues are discussed in this section, and the income tax issues in the next section.

A gift is complete if the grantor has given up dominion and control and has not reserved sufficient power to change the disposition of the property. In each case, the terms of the power must be examined and the scope of the power must be determined. For example, if the grantor reserves a power to direct disposition of the trust’s remainder among her descendants, then her contributions to the trust generally are not completed gifts.
A grantor would be considered to possess such a reserved power (and the gift would still be considered incomplete) even if the power can only be exercised in conjunction with another person, as long as that other person does not have a “substantial adverse interest in the disposition of the transferred property or the income therefrom.” This terminology is not clearly defined. However, if a power does not survive the death of the grantor and cannot be exercised in favor of the possessor’s estate, creditors or the creditors of his estate, the person is considered a mere co-holder of the power, not as having a substantial adverse interest.\(^8\)

**Example:** In the sample trust, the grantor retained the consent power. Under this power, the trustee is required to distribute income and principal as directed by a majority of the distribution committee with the written consent of the grantor. Because the distribution committee ceases upon the death of the grantor, the members are not considered to have substantial adverse interests. Accordingly, even though the grantor’s power could be exercised only in conjunction with the distribution committee, because the distribution committee does not have substantial adverse interests for gift tax purposes the grantor is considered to have that power such that gifts to the trust are not completed gifts.

A gift is incomplete if the grantor is given the power to name new beneficiaries or change the interests among the beneficiaries (unless the power is held by the grantor as a fiduciary and is limited by a fixed or ascertainable standard).\(^9\)

**Example:** In the sample trust, the grantor retained the sole power. Under this power the grantor, individually and not in a fiduciary capacity, had the discretionary power to distribute income and principal among his issue for their health, maintenance, support and education. Because the grantor individually has the power to change the interests of beneficiaries, gifts to the trust are wholly incomplete. Although the power is subject to a standard, the grantor holds the power in a non-fiduciary capacity.

When will an initially incomplete transfer to a trust be considered complete and the gift tax apply? There are a number of circumstances when this will occur. One is when a distribution is made from the trust to a person other than the grantor. Another is when the grantor gives up the power or the power is terminated during the lifetime of the grantor.\(^10\)

**Example:** In the sample trust, a completed gift by the grantor will occur each time a distribution is made to a beneficiary other than the grantor during the grantor’s lifetime. Distributions to the grantor will not be gifts by the grantor or a member of the distribution committee.

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The challenge is to structure the trust so that the grantor has sufficient control to keep her contributions to the trust from being treated as completed gifts, but insufficient control to require that she be treated as the owner of the trust’s income.
When might members of a distribution committee or similar committee be considered to hold powers which could result in gift tax consequences or estate tax inclusion for them? This can occur when they are considered to hold general powers of appointment.

A person is not considered as holding a general power of appointment if she holds the power with the creator of the power. In addition, a person is not considered as having a general power of appointment if the power is held in conjunction with a person with a substantial interest in the property adverse to the exercise of the power in favor of the possessor of the power. Satisfying this condition requires careful planning in light of the identity and interests of the beneficiaries of the trust and the identity of the members of any distribution or similar committee. It can be a very difficult issue to resolve in the trust design process. However, it is highly important in light of the potential tax consequences to committee members.

**Example:** In the sample trust the distribution committee ceases to exist upon the death of the grantor and is deemed to cease to exist when there are fewer than two qualified family members of the committee. In addition, vacancies in the committee are not automatically filled. Under the specific facts the members were considered to have substantial adverse interests in the property subject to their powers. Distributions to beneficiaries other than the grantor upon exercise of the consent power and the unanimous member power are gifts by the grantor, not a committee member, and there is no estate tax inclusion for committee members.

**INCOMPLETE NON-GRAantor TRUST TREATED AS A SEPARATE TAXPAYER FOR INCOME TAXATION**

Having charted the incomplete gift path, we turn to the income tax issue. Recall that the objective is for the trust to be treated as a taxpayer separate from the grantor. Note that the federal treatment of a trust is ordinarily followed by the states, but this result should be confirmed in each particular circumstance. Please see the separate discussion of New York's treatment of Incomplete Non-Grantor Trusts on page 9.

For federal income tax purposes a trust either is treated as a separate taxpayer or as if the grantor or another person (commonly a beneficiary) is the owner of the trust such that the income of the trust is taxable to the person treated as the owner. To demonstrate the potential impact of a trust's income tax classification, consider the following example:

**Example:** Presume that the grantor is a resident of State X, subject to State X's income-taxing jurisdiction, and that the trust, if a separate taxpayer, would not be subject to State X's income-taxing jurisdiction, but rather would be a Nevada resident trust not subject to state income taxation. If the trust is treated as a separate taxpayer, then as a resident trust of Nevada, its income may potentially not be subject to any state taxation. However, if the trust is treated as a grantor trust owned by the State X resident grantor, then its income will flow through to the grantor and be subject to State X income taxation.
There are numerous circumstances under which a grantor is treated as the owner of a trust.13 These must be avoided in order to achieve separate trust treatment desired for the incomplete non-grantor trust. Consider a trust the establishment of which is an incomplete gift because income may be paid to or accumulated for the benefit of the grantor and the grantor retains the power exercisable by will to designate the remainder beneficiaries among his descendants. Will these powers cause the trust to be treated as owned by the grantor for income tax purposes? If so, how can they be modified to achieve our dual mandate?

**Grantor Control of Beneficial Enjoyment**

A trust is treated as owned by the grantor for income tax purposes if the grantor, another person, or the grantor and another person, has a power of disposition over the income or corpus of the trust, but only if the power can be exercised without the approval or the consent of a person who is considered an “adverse party.” For federal income tax purposes, an adverse party is defined as any person who has a substantial beneficial interest in a trust which would be adversely affected by the exercise or non-exercise of the power he possesses respecting the trust.14 Therefore, for income tax purposes, grantor-type trust treatment can be avoided by requiring that the grantor’s powers be exercised only with approval or consent of an adverse party. The challenge is to accomplish that requirement without causing the gift to be complete and without causing negative tax consequences to the adverse party.

**Example:** In the sample trust, many of the grantor’s powers are exercisable only with the consent or approval of some or all of the distribution committee, and because the distribution committee members (the grantor’s children) were all beneficiaries of the trust, they were considered adverse parties for income tax purposes such that the grantor was not treated as the owner of the trust. Note that the meaning of an adverse interest for gift tax purposes and an adverse party for income tax purposes are not presently understood to be synonymous.

There are also limited types of powers of disposition that won’t defeat separate taxpayer treatment. For example, a power to distribute the corpus of a trust to a beneficiary that is limited to a reasonably definite standard set forth in the trust instrument is permissible.15 In addition, a power in the grantor exercisable solely by will generally is permissible.16

**Example:** In the sample trust, the grantor’s only power which was not subject to the approval or consent of the distribution committee was the grantor’s sole power during his lifetime to distribute trust principal for the health, maintenance, support and education of his issue, and because that power is limited by an ascertainable standard it does not defeat separate taxpayer status.
**Income for the Benefit of Grantor (or Grantor’s Spouse)**

A grantor also will be treated as the owner of the portion of a trust whose income may be distributed to the grantor or the grantor’s spouse, held or accumulated for future distribution to the grantor or the grantor’s spouse, or applied to the payment of premiums on the life of the grantor or the grantor’s spouse, unless the distribution may only be made with the approval of an adverse party.\(^\text{17}\) In the sample trust, the grantor’s spouse was not included in the class of permissible beneficiaries of income or principal.

If under state law the income of the trust may be subject to the claims of the grantor’s or the grantor’s spouse’s creditors, the trust may be treated as coming within this income-for-the-benefit of grantor trust rule. In addition, if the grantor’s or grantor’s spouse’s creditors can reach the trust assets, the grantor is considered to have retained the right to indirectly control beneficial enjoyment of the trust assets. It is for these reasons that incomplete non-grantor trusts are commonly established under the laws of states that recognize self-settled domestic asset protection trusts. Some practitioners recommend establishing the trust in a state where there is no carve out for excepted classes of creditors under the state’s asset protection statute. This should avoid any potential argument that income could be used to benefit the grantor due to potential claims by excepted classes of creditors, alimony or child support being the most often cited examples.\(^\text{18}\)

**Example:** In the sample trust the distribution committee’s role in decisions with respect to distributions to the grantor (the consent power and the unanimous member power) is designed to avoid grantor trust treatment under the income-for-the-benefit of grantor trust rule.

**Beneficiary Treated as Owner**

There are circumstances where a beneficiary of a trust may be treated as the owner of the trust for purposes of the grantor trust income tax rules. This possibility arises when a beneficiary is given powers that the Internal Revenue Service considers the equivalent of direct ownership of trust property. A common example is a power to withdraw the assets of the trust. In order to cause a beneficiary to be treated as the owner of a trust, the power generally must be exercisable by the beneficiary alone and for her benefit.\(^\text{19}\) When designing an incomplete non-grantor trust, attention should be paid to the extent of beneficiary powers, including powers the beneficiary might have as the member of a distribution or other committee, so as not to cause unintended grantor trust income tax treatment as to a beneficiary.

**New York Defective Grantor Trust Tax Status for Incomplete Non Grantor Trusts**

New York has enacted legislation that treats an incomplete non-grantor trust as a defective grantor trust for purposes of New York taxation (including for New York City income tax). New York law defines an incomplete non-grantor trust as a trust created by a New York resident, the funding of which is considered an incomplete gift under Internal Revenue Code Sec. 2511, but which is not taxable to the grantor under Internal Revenue Code Sec. 671-679. New York defective grantor trust status applies as of January 1, 2014 to all incomplete non-grantor trusts still in existence as of June 1, 2014. Consequently, there is no longer any state income tax benefit for New York residents contemplating an incomplete non-grantor trust structure.
States ordinarily tax the worldwide income of resident individuals and resident trusts, but only the state-source income of non-residents. Therefore, once a trust is established as a taxpayer separate from the grantor, the next question is how to design the trust so as to be considered a resident of a state with favorable income tax treatment of trusts and to avoid being treated as a resident of a state with unfavorable income tax treatment of trusts.20 Note that this design and analysis has no bearing on the taxation of state-source income, which will be subject to state income taxation in all cases where a state imposes an income tax.

The state laws with respect to the determination of the residence of a trust are not uniform. Depending upon the state or states in question, state tax residence of a trust may be based upon one or more of:

- The residence or domicile of the grantor when the trust became irrevocable (either during life or at death);
- The residence or domicile of the trustee or trustees of the trust;
- The residence or domicile of the fiduciaries of the trust in addition to the trustees, such as advisors;
- The residence or domicile of the beneficiaries of the trust;
- The place of administration of the trust; and/or
- The presence of tangible assets or commercial activity in the state.
- State tax law that treats non-grantor trusts for federal income tax purposes as defective grantor trusts for state income tax purposes.

For grantors resident in states that look (without exceptions) to the residence or domicile of the grantor to determine the residence of a trust or residents of New York, the incomplete non-grantor trust presents no state income tax efficiency benefits.21 In addition, if the grantor resides in a state that taxes certain accumulations in out-of-state trusts upon distribution to in-state beneficiaries, as in the States of California or New York, overall state income tax will depend in part upon the state of the grantor’s or other beneficiary’s residence at the time of any distribution from the trust. Because the trust state tax resident rules are not uniform, it is possible for a trust to be considered resident in more than one state. Conversely, a trust may not be considered resident in any state.

Delaware and Nevada are two “tax favored” states for trusts. Delaware considers a trust resident in the state if the trust has a Delaware trustee or the trust was created by a Delaware domiciliary. However, a Delaware resident trust is not required to file a Delaware income tax return if it has no Delaware resident beneficiaries and no Delaware source income. Delaware allows a deduction for income accumulated for non-resident beneficiaries.22 Nevada has no income tax and a constitutional prohibition against a personal income tax.23
If the grantor is not a resident of a state that determines the residence of a trust based on the domicile of the grantor or a resident of New York, the trust may be designed to be governed by the law of a state that determines the residence of the trust based on the residence of the trustee or the place of the administration of the trust. The grantor may name a trustee resident in the state of choice and the trust may be administered in the state of choice, thus being treated for state income tax purposes as a resident of that state.

**Example:** Grantor, a non-resident of New York and who is resident in a state that does not determine trust residence based on the grantor’s domicile, creates an incomplete non-grantor trust governed by the law of the state of Nevada, designates The Northern Trust Company of Nevada as trustee, and The Northern Trust Company of Nevada administers the trust in Nevada with the trust assets located in Nevada. With proper trust design, the trust will be a resident of Nevada not subject to state income taxation in Nevada or any other state unless perhaps if income is sourced to another state. Any state source income from other states may be subject to taxation in those states.

**Example:** Grantor, a non-resident of New York and who is resident in a state that does not determine trust residence based on the grantor’s domicile, creates an incomplete non-grantor trust governed by the law of the State of Delaware, designates The Northern Trust Company of Delaware as trustee, and The Northern Trust Company of Delaware administers the trust in Delaware. If there are no Delaware beneficiaries and no Delaware source income, there will be no Delaware state income tax or any other state income tax unless income is sourced to another state. Any state source income from other states may be subject to taxation in those states. It is necessary that the Delaware trustee materially participates in the administration of the trust, which activities should include, but are not necessarily limited to, custody of part or all of the assets, maintenance of records in Delaware, or preparation or arrangement for preparation of fiduciary income tax returns for the trust in Delaware.
TRUST DESIGN AND IMPLEMENTATION

As the preceding discussion demonstrates, trust design for tax efficiency is unique to each grantor and trust circumstance. Considerations to be addressed include:

- The current and future residence of the grantor;
- The family and financial circumstances of the grantor;
- The applicable federal and state tax laws;
- The potential that state taxing authorities may challenge the validity of the trust and the willingness to assume that risk;
- The type of assets to be held in the trust;
- The selection of the trustee and the scope of the trustee’s powers;
- The selection of committee members and the scope of committee members’ powers;
- The identity of the beneficiaries of the trust and their residence;
- The identity and residence of advisers and trust protectors; and
- The ability to grant advisers and committee members powers of direction under state law.

There are process questions to address as well. Will the taxpayer seek a formal private letter ruling regarding the federal gift and income tax treatment of the grantor, the trust, and/or the committee members? Will the grantor seek private rulings or formal legal opinions regarding state tax matters such as the residence of the trust, the state income taxation of the trust, and/or the state income taxation of the beneficiaries of the trust? These are important considerations to evaluate with one’s team of professional advisors and fiduciaries. Whether an incomplete non-grantor trust is a sensible planning alternative for a particular individual requires consideration of the opportunity and associated risks for tax savings, wealth preservation and achieving related goals, as well as the associated investment in the work of planning and the costs of a private letter ruling, legal opinions, establishment of the trust and ongoing administration. In all events, the reality is that circumstances and tax law changes should be taken into account because we live in a mobile society with fluid tax laws.
OUR SERVICES
The Northern Trust Company of Nevada and The Northern Trust Company of Delaware offer trust services for incomplete non-grantor trusts. The Northern Trust Company of Nevada is a Nevada state chartered retail trust company. The Northern Trust Company of Delaware is a Delaware limited purpose trust company, opened in Wilmington Delaware in 2004, which in 2015 has assets under administration of more than $15 billion. At Northern Trust we work with our clients and their advisors to help design trusts aligned with their goals, including tax efficiency and wealth preservation. We offer consulting services, fiduciary services and directed trust services.

ABOUT THE CONTRIBUTORS
Laura Mandel serves as president of The Northern Trust Company of Delaware, a Delaware limited purpose trust company in Wilmington, Delaware. In this role, she is responsible for managing Northern Trust’s Delaware office, which was opened in 2004 and in 2014 has more than $16 billion of assets under administration.

Prior to managing Northern Trust’s Delaware office, Laura was a senior vice president and fiduciary relationship manager in Chicago where she managed one of Northern Trust’s largest and most complex portfolios of trust and investment management accounts in the wealth management business unit. She also dedicated more than seven years of service in Northern Trust’s legal department as a senior attorney advising trust administrators, investment managers and fiduciary officers on a variety of trust and investment legal issues. Prior to joining Northern Trust, Laura worked at Harris Trust and Savings Bank where she served in both the legal department and as a senior trust administrator and managed one of Harris Bank’s suburban trust departments. Early in her career, Laura practiced law with two Chicago firms where she specialized in estate planning and trust law.

Laura received her bachelor’s degree with honors from Loyola University of Chicago and attended both Georgetown Law Center, where she was on the Dean’s List, and Loyola School of Law where she received her J.D. Laura was on the trust administration faculty of the American Bankers Association’s National Trust School and also served on its board of directors. She was also a faculty member for the American Bankers Association’s National Graduate Trust School. Laura has earned her Chartered Private Wealth Advisor designation and speaks and writes frequently on various trust and fiduciary topics. She is admitted to the bar of the State of Illinois and to the bar of the United States Supreme Court. She is a member of the Estate Planning Council of Delaware and an associate member of the Delaware State Bar Association Estates and Trusts Section. Laura also serves on the Professional Advisory Committee for the Delaware Community Foundation.
Suzanne L. Shier is the wealth planning practice executive and chief tax strategist/tax counsel for the Wealth Management business unit at Northern Trust and serves on the Wealth Management operating group. She is responsible for leading Wealth Planning Advisory Services and for providing thought leadership on wealth planning and tax issues of interest to clients and their advisors, with a special emphasis on wealth planning and tax policy, legislation, strategies, trends and developments.

Prior to joining Northern Trust, Suzanne spent 26 years as a partner at Chapman and Cutler LLP in Chicago, ultimately leading the firm’s trusts and estates practice, representing individuals, charitable organizations and corporate fiduciaries in a full range of wealth planning and fiduciary matters, including philanthropy, domestic and international wealth planning, and fiduciary administration.

Suzanne is an adjunct professor in the Master of Laws in Taxation Program at Northwestern University Law School and also a frequent speaker and author. She has been quoted in publications such as *The Wall Street Journal* and Bloomberg and has received numerous professional honors and recognitions, including selection for inclusion in *Best Lawyers in America in Trusts and Estates*.

Suzanne earned her bachelor’s degree with distinction in economics and sociology from the University of Michigan in 1982. She received her law degree, cum laude, from the Loyola University Chicago School of Law in 1985 and a master of laws in taxation from the DePaul University College of Law in 1997.

In the civic community, Suzanne supports diversity and education initiatives. She has been involved with the executive committees and boards of directors of Gads Hill Center and the Chicago Coalition of Women’s Initiatives in Law. Suzanne is chairperson of the board of directors of Chicago Scholars, a college access program for high potential urban students, and a trustee of Hope College.

Suzanne is a fellow of the American College of Trust and Estate Counsel and a member of the Chicago Bar Association, Chicago Estate Planning Council, American Bar Association, International Bar Association and the International Society of Trust and Estate Practitioners.

ABOUT NORTHERN TRUST
Northern Trust Corporation (NASDAQ:NTRS) is a leading provider of investment management, asset and fund administration, fiduciary and banking solutions for corporations, institutions and affluent individuals worldwide. A financial holding company headquartered in Chicago, Northern Trust serves clients in more than 40 countries from offices in 18 U.S. states and 20 international locations in North America, Europe, the Middle East and the Asia-Pacific region.

As of September 30, 2015, Northern Trust had assets under custody of $6.0 trillion, assets under management of $887 billion and banking assets of $120 billion. Northern Trust, founded in 1889, has earned distinction as an industry leader, combining exceptional service and expertise with innovative capabilities and technology. For more information, visit northerntrust.com.
ENDNOTES

1 The combined income tax rate will exceed 50% in the case of individuals and trusts subject to the 39.6% marginal federal ordinary income tax rate, the 3.8% Medicare contribution tax rate and a state income tax rate in excess of 6.6%. In 2016 state marginal ordinary income tax rates exceed 6.6% in California, Connecticut, Hawaii, New Jersey, New York, North Carolina and the District of Columbia.

2 For a high income individual or trust subject to California state income tax, the 39.6% marginal federal ordinary income tax rate, 3.8% Medicare contribution tax rate and the 13.3% marginal California ordinary income tax rate totals 56.7% in 2016.

3 PLR 201310002 (March 8, 2013). This discussion is only a summary. For the details of the letter ruling the reader is referred to the text of the PLR. PLR 201410009 (March 7, 2014). The design of the trust is substantially similar to that approved by the Internal Revenue Service in PLR 201310002 except that the Distribution Committee members included guardians of the grantor’s five minor children who were beneficiaries of the trust. See also PLR 200731019, PLR 200729025, PLR 200715005, PLR 200647001, PLR 200637025, PLR 200612002, PLR 200502014, PLR 200247013, PLR 200148028. Private letter rulings may only be relied upon by the taxpayer to whom they are issued and are not legal precedent for other taxpayers.

4 Treas. Reg. Sec. 25.2511-2(b).

5 Id.

6 Id.

7 Treas. Reg. Sec. 25.2511-2(e). A donor is considered as himself having a power in conjunction with any person not having a substantial adverse interest in the disposition of the transferred property or the income from the transferred property.

8 Treas. Reg. Sec. 25.2514-3(b)(2).

9 Treas. Reg. Sec. 25.2511-2(c).


11 Code Sec. 2514(c)(3)(A).

12 Code Sec. 2514(c)(3)(B); Treas. Reg. Sec.25.2514-3(b)(2).

13 Code Secs. 671-677 set forth the circumstances under which a grantor will be treated as the owner of a trust. See also S 612(b)(41) of NY Tax Law treating incomplete non grantor trusts as defective grantor trusts.

14 Code Sec. 672(a).

15 Code Sec. 674(b)(5)(A).

16 Code Sec. 674(b)(3).

17 Code Sec. 677(a).

18 Consideration should also be given to the location of assets and any opportunity for creditors to reach trust assets based on their location.

19 Code Sec. 678.

20 State tax residence may be based upon “residence” and/or “domicile.” For purposes of this discussion the terms are used interchangeably, although the technical definitions vary. Careful review of the applicable laws of the states in question in a particular circumstance is recommended.

21 Connecticut, the District of Columbia, Illinois, Michigan, Minnesota, Ohio, Pennsylvania, Virginia and Wisconsin are examples of grantor’s domicile or so called “residence by birth” states. New York treats incomplete non-grantor trusts as defective grantor trusts.

22 30 Del. C. Secs. 1635(a); 1636(a).

23 Constitution of the State of Nevada, Article 10, Section 1, Subsection 9.

24 12 Del.C. Sec. 3570(b).

25 18 Code Sec. 3570(b).
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