50th Annual Philip E. Heckerling
Institute on Estate Planning
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Heckerling 2018 - Report No. 4
(Wednesday 1/24/18)

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As we have done in January for the last twenty one years, and again with the permission of the University of Miami School of Law Center for Continuing Legal Education, we will be posting daily Reports to this list containing highlights of the proceedings of the 52nd Annual Philip E. Heckerling Institute on Estate Planning that is being held on January 22-26, 2018 at the Orlando World Center Marriott Resort and Convention Center in Florida. A complete listing of the proceedings and the Institute's 2018 brochure are available at www.law.miami.edu/heckering. Introduction Part 1 issued on 1/11/18 covered the Institute Opening Reception, its Scope, the Faculty, the Advisory Committee, the Sponsors and the Vendors, plus general information at the end about the Institute. Introduction Part 2 issued on 1/12/18 contained a complete listing of all of the proceedings of this Institute. This Report continues our coverage of the proceedings.

We also will be posting the full text of each of these Reports on the ABA RPTE Section's Heckerling Reports Website, as we have since the 2000 Institute. The Reports from 2000 to 2017 can now be found at URL http://www.americanbar.org/groups/real_property_trust_estate/events_cle/heckerling.htm. In addition, each Report from 2006 to date can also be accessed at any time from the ABA-PTL Discussion List's Web-based Archive that now only goes as far back as January of 2006 and is located at URL http://mail.americanbar.org/archives/aba-ptl.html.

Announcement: If you have not subscribed to it yet, you ought to take a look at the Wills, Trusts & Estates Prof. Blog that is hosted by FeedBitz and edited by Prof. Gerry W. Beyer of the Texas Tech University School of Law. There is a daily post each day with (typically) 4 to 5 highlighted items of current interest which can be opened up and read in more detail if of interest. This is a free service. For more information and to subscribe, go to https://app.feedblitz.com/f/fbz?Sub=8995.

Summary: This Report #4 contains our coverage of the two general sessions that were held on Wednesday morning, those being on long term care and US taxation of US grantors and beneficiaries of foreign trusts.

The next Report #5 will cover the traditional Q&A session that was held on Wednesday morning and the Fundamentals #2 session on Subchapter J issues that was held Wednesday afternoon concurrent with special sessions #'s 1 and 2.

Wednesday, January 24, 2018

9:00-9:50
Will You Still Need Me, Will You Still Feed Me, When I’m Sixty-Four? [ELD]
Presenter: Bernard A. Krooks
Reporter: Bruce Tannahill

Not sure that the Beatles were thinking about financing long-term care, but you and your clients should be! Seventy percent of Americans age 65 and older will need some form of long-term care during their lifetime. Unfortunately, the U.S. has no health insurance system for long-term care. To many, this comes as a rude awakening as their health declines and the need for care arises. This presentation addressed the myriad of options available to people in need of long-term care, how to finance such care, and other issues that should be addressed during this process. Here are some of the more significant details.

Introducing Mr. Krooks, Stacy Eastland noted that the Joint Committee on Taxation said that only 1800 of the 26 million people who die annually will be subject to estate tax. He pointed out that 100% of people have the possibility of growing old, developing dementia, or needing long-term care (LTC) assistance.

After playing a portion of the Beatles “When I’m 64,” Mr. Krooks said that 84 is the new 64 and reviewed statistics on the aging of the United States populace. Forty million (13% of the population) are now over 65 with 25% expected to live past 90 and 10% past 95. By 2050, 20% of the population (88.5 million) will be over 65.

Over five million people currently have Alzheimer’s disease with the number expected to triple by 2050. It doesn’t just affect persons over 65 – 200,000 people under 65 have it. It is the most expensive disease in the nation, with an annual cost of $259 billion, with the government paying about 68% of the cost. The cost is projected to rise to $1.1 trillion by 2050. In comparison, cancer costs $66 billion annually.

Elder Law Myths and Reality

Mr. Krooks addressed some elder law myths and the realities.

Myth: It won’t happen to me, I’ll never go to a nursing home.

Reality: 70% of people turning 65 will need LTC and 50% will need nursing home care.

Myth: Even if I have to go into a nursing home, Medicare will take care of me.

Reality: Medicare doesn’t pay for LTC. It provides some coverage for skilled nursing home care if certain requirements are met, custodial care and LTC costs for chronic illnesses are not covered.

Myth: LTC isn’t that expensive.
Reality: The average annual LTC cost in U.S. is $100,000 and can exceed $200,000 in major metropolitan areas.

Myth: I’m not responsible for my spouse’s care.

Reality: You are responsible for your spouse’s care. The law generally deems spouses as one entity, but does provide some protections for spouses. Pre-nuptial agreements and separate accounts are generally disregarded.

Myth: I can make my own decisions.

Reality: You may not be able to make your own decisions. You can address who can make those decisions for you through powers of attorney and health care directives.

Where LTC is generally provided

Most long-term care is provided in one of four different settings:

1. **Home.** Most people would prefer to receive LTC at home. It is estimated that 80% of home care is unpaid. Any payment arrangement should be written to minimize conflicts between the caregiver and other family members. There are significant tax issues involved, including whether the caregiver is an employee or independent contractor and employment tax obligations.

2. **Assisted living facility (ALF).** These facilities are generally not licensed to provide medical care and are not subject to federal regulation. A portion of ALF expenses qualifies for the medical expense deduction and the facility should be able to provide information on the amount attributable to medical care.

3. **Nursing home.** Skilled nursing facilities participating in Medicare or Medicaid must meet requirements under federal law, giving nursing home residents far more resources in dealing with the facility than residents of other facilities not subject to those rules.

4. **Continuing care retirement community.** These offer a continuum of housing options, from independent housing, to assisted living, to nursing home care. They can allow spouses with different care level needs to remain near each other.

Mr. Krooks noted that ALFs and nursing homes often seek to have a third-party, such as a child, guarantee payment and require binding arbitration to resolve disputes. Nursing homes cannot require a third-party guarantee. He recommended that the admission agreements be reviewed carefully.

Ways to Pay for LTC

Mr. Krooks reviewed the options to pay for LTC expenses.

1. **Private pay.** Persons paying for LTC using their own funds should take advantage of the medical expense deduction to the extent possible. In addition to income and savings, resources to pay the expenses personally include reverse mortgages and life insurance accelerated death benefit features.
2. **Medicare.** Medicare pays for very limited short-term rehabilitation care after being admitted to a hospital for a qualifying stay. It does not cover custodial care. There are numerous deductibles and co-pays that must be considered.

3. **Medicaid.** Often confused with Medicare, Medicaid is a federal/state program that allows standards to vary by state. It is not easy to qualify for eligibility. Mr. Krooks reviewed some of the eligibility rules, exempt assets, spousal planning, and trusts that can be used in planning.

4. **LTC insurance.** Long-term care insurance covers LTC costs, including custodial care. Obtaining it generally requires a rigorous physical and cognitive exam and pays benefits based on a daily rate. Mr. Krooks recommended working with an insurance person who specializes in LTC coverage because the coverage is complicated and specific on what is and isn’t covered. Hybrid policies combining LTC coverage with life insurance coverage or an annuity benefits avoid the perceived waste of money if LTC benefits are not used.

5. **VA benefits.** Mr. Krooks noted that few people receive VA LTC benefits and that they are very hard to qualify for.

9:50-10:40

**Theory Meets Reality: A Practical Look at the U.S. Income Taxation of U.S. Grantors and Beneficiaries of Foreign Trusts [INT][TRU]**

**Presenter:** M. Read Moore  
**Reporter:** Beth Anderson

Differences in trust law and trust administration outside of the United States often make advising U.S. clients on U.S. tax issues related to foreign trusts quite challenging. This presentation addressed the principal U.S. income tax issues affecting U.S. settlors and beneficiaries of trusts administered outside the United States with an emphasis on frequent conflicts between U.S. tax law and the realities of trust law and trust administration outside of the United States. This Report covers some of the more significant parts of this presentation.

This presentation discussed the income tax recognition and reporting differences between grantor and non-grantor foreign trusts.

The presentation started with a few important definitions such as what does it mean to be a foreign trust. A foreign trust must meet two tests – court test and control test. If no US court has jurisdiction over the trust and a non-US person has decision making control over the trust (for example the ability to remove and replace the trustee), then the trust is a foreign trust for US income tax purposes.

**I. Determining the Grantor of a Foreign Trust**
This presentation discussed the difficulties of tracking and identifying the grantor of a foreign trust. The grantor of the trust is the person who makes a gratuitous transfer of assets (not necessarily a taxable gift) to the trust. Determining the grantor of a foreign trust can be tricky because foreign trusts are often created by declaration or deed of transfer and may not name the grantor or describe where the assets in the trust came from.

Offshore trusts may have a nominal grantor such as a lawyer or a friend that creates the trust as an accommodation to the true grantor. There may be some due diligence and investigation behind the trust to see who made the gratuitous transfer of assets.

Decanting by trustee can result as the trustee becoming the grantor because foreign trust was created by a decanting from one trust to another. Regulations direct that the grantor of the original trust is the grantor of the new trust.

II. US Income Tax Treatment of a Foreign Grantor Trust and Establishing Grantor Trust Status

The presentation discussed the benefits and reporting requirement when a US beneficiary receives a distribution from a foreign grantor trust. The non-US resident foreign grantor of the foreign trust is responsible for the income generated on the assets in the trust, and the US beneficiary receives a tax-free distribution.

Although the US beneficiaries are not taxed on distributions, they must report the distributions to the government on a Form 3520 showing why the trust is a foreign grantor trust and why income taxes are not paid. There is a 35% penalty for failing to report non-taxable income. Form 8938, which is used by US person who have to declare interests in Foreign trusts, does not apply to foreign grantor trusts.

Congress knows this is a good deal, so there are completely different rules for foreign grantor trusts that make it more difficult to create foreign grantor trusts and US grantor trusts. For example, Sec. 678 does not apply to allow a beneficiary to be a deemed grantor. A beneficiary of a foreign trust can only be a grantor of the trust, if the beneficiary exercises a general power of appointment over the assets and creates a new trust.

Grantor Trust rules are different for Foreign Trust. They follow Sec. 672(f), and only two kinds of trusts qualify. First, Grantor or Grantor’s spouse is the sole beneficiary of the trust (sole benefit trust). The other is a “revocable trust”. If a non-resident alien has the power to reinvest the property either alone or in conjunction with another party. What does it mean to have the power to reinvest the trust assets. Most other countries do not have revocable trusts. Revest is the key word instead of revoke. Look for a direct or indirect power to control the assets and get the assets back. Look for the power to revest either because the settlor is a beneficiary and the settlor has the power to control the trustee or has an unlimited power to remove/replace trustee and can appoint themselves as trustee.
Cannot toggle back and forth between grantor trust status, once it is lost is it is gone forever. Can still have a foreign grantor trust if the grantor is incapacitated so long as agent can exercise powers on grantor’s behalf.

III. US Income Tax Treatment of a Foreign Non-Grantor Trust

Most of the time foreign trusts are not a US tax payers, but beneficiaries that are US tax payers and distributions from a foreign non-grantor trust are subject to tax based on Subchapter J. The trust’s DNI must be computed but the rules for DNI are different for foreign non-grantor trusts, and the throw back tax applies, as do more reporting obligations.

Generally compute DNI just like a domestic trust but must include realized capital gains. Also add back foreign tax paid and include foreign source income (world-wide income not just US income). Throwback Tax is a tax that existed for domestic trusts when tax rates were lower than individuals. This created a bracket game between accumulating income or making distributions to individual. This tax still applies to any distribution from a foreign non-grantor trust and any distribution from a domestic trust that was once a foreign trust. Applies when a beneficiary of non-grantor foreign trust gets an accumulation distribution. An accumulation distribution is a distribution in excess of DNI or the fiduciary accounting income. Based on UNI (undistributed net income). When a trust makes a distribution of UNI, then tax is triggered based on the UNI received. The computation is complex, and includes an interest charge on top of the throwback tax at the federal underpayment rate compounded daily. Total taxes cannot be more than 100%.

The foreign non-grantor trust rules are very specific about transactions that look for characterize distributions in another manner. Loans can be deemed distributions if specific rules are not followed. Use of property held in the trust is a deemed distribution unless rent is paid. Step-transactions or using an intermediary (non-resident family member) to received distributions then make gifts to the US beneficiary are collapsible and deemed distributions to the US beneficiary.

US beneficiaries receiving distributions of any amount must disclosed the value and tell the IRS how the distribution should be treated. If not defined, the assumption is that the distribution was UNI with a set premium tax. Computing DNI and UNI can be very difficult because trustees of foreign non-grantor trusts do not file 1041, or issue K-1. Often Trustee’s don’t keep the correct accounting records so it may be very different to compute US income taxes.

The Reporters:

Our on-site local Reporters who are present in Orlando in 2018 are Joanne Hindel Esq., a Vice President with Fifth Third Bank in Cleveland, Ohio; Kimon Karas Esq., an attorney with McCarthy, Lebit, Crystal and Liffman Co. LPA in Cleveland, Ohio; Craig

The Report Editors in 2018 are Joseph G. Hodges Jr. Esq., a solo practitioner in Denver, Colorado, who is the Chief Moderator of the ABA-PTL discussion list. He is being ably assisted in those duties this year by Reporter Bruce A Tannahill Esq.