Could You Benefit from a Spousal Lifetime Access Trust?

JENNIFER PROPER
Managing Director, Wealth Strategies

Have you ever heard that irrevocable trusts are a great way to minimize estate taxes and keep more of your wealth in the family? Well, they are, but many people are uncomfortable with the fundamental premise of irrevocable trusts: They require you to permanently give up ownership and control of the assets you place in them.

Your apprehension is well-founded. Most people aren't excited about the prospect of relinquishing millions of dollars — a pain that's very real in the present — for an intangible future benefit, especially one they may not live long enough to witness.

A type of irrevocable trust called a spousal lifetime access trust, or SLAT, might help you get comfortable with using irrevocable trusts as a foundational estate planning strategy.

How SLATs Work

SLATs allow one spouse to establish an irrevocable trust for the benefit of the other spouse and other beneficiaries (likely children and grandchildren). The grantor spouse funds the trust with up to $12.92 million in assets (assuming the SLAT is created in 2023), taking advantage of as much of the lifetime estate and gift tax exclusion (commonly called an exemption) as possible.

Since the other spouse is the trust's primary beneficiary, the SLAT has a bit of a loophole: the grantor spouse retains indirect access to the trust's income and assets while both spouses are still alive and married. In other words, SLATs don't require the grantor to initially give up as much control as other irrevocable trusts do.

Who Should Consider a SLAT?

The ideal candidate for a SLAT is someone in a stable, long-term marriage who is willing to give up access to the assets that are placed in the trust. Your age isn't important; what's important is that you have enough assets that the estate tax is a significant threat. And if you have assets that could grow rapidly, such as shares of a privately held business that might be sold for a profit or taken public, you're an especially good candidate for a SLAT.

However, you don't want to put assets into a SLAT (or any other type of irrevocable trust) that you might need during your lifetime. For example, if your net worth is $25 million and you feel comfortable living off $13 million for the rest of your life (plus whatever future earnings you might have from work and investments), then you might be comfortable putting $12 million into a SLAT.

Benefits of SLATs

Here are the top reasons why we often encourage our clients to consider SLATs.

Indirect Access

Despite being an irrevocable trust, SLATs can allow the donor spouse to indirectly access the trust's assets on a limited basis because the beneficiary spouse can withdraw income or assets from the trust if necessary. This access can alleviate concerns about giving up control and about not having enough assets to maintain the living standard you're used to.

Extra Estate Tax Savings

SLATs are typically structured as grantor trusts. When you use some or all of your lifetime estate and gift tax exemption to transfer assets into a grantor trust, not only are the assets a tax-free gift to your beneficiaries, but so is all the future growth of those assets (which is why assets that could appreciate considerably can be an excellent funding source).

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A grantor trust allows the grantor — that's you, the person who funds the trust — to pay the tax on any trust income, such as stock dividends, even though you no longer own the assets that were used to fund the trust.

Structuring the trust this way means that you're not reducing the trust's value by using its assets to pay its income taxes. Instead, you're further reducing the value of your own taxable estate by using your personal assets to cover the trust's income tax liability.

Major Federal Estate Tax Savings

The present may be an especially advantageous time to fund a SLAT. In 2023, the federal lifetime estate and gift tax exclusion is $12.92 million per person, or $25.84 million per couple.

However, beginning in 2026, the exclusion is scheduled to drop back to $5 million per person, or $10 million per couple, with an adjustment for inflation. Therefore, it may make sense for you to discuss SLATs and wealth transfer planning now to take advantage of the historically high estate and gift tax exclusion amounts.

Generational Benefits

SLATs can provide tax benefits far beyond reducing your own estate taxes. They are typically designed to benefit not only the non-donor spouse, but also the donor's children (and grandchildren) as contingent beneficiaries (although a SLAT can also name the children as primary co-beneficiaries along with the spouse).

In fact, a SLAT can be structured as a dynasty trust to benefit future generations while avoiding generation-skipping transfer taxes.

Drawbacks of SLATs

SLATs, like other wealth-planning strategies, are not without risks.

Death

The limited access the grantor spouse retains to the trust's assets vanishes upon the beneficiary spouse's death. When the beneficiary spouse dies, the trust's assets pass to the contingent or co-beneficiaries. Even though these beneficiaries may be the grantor spouse's children, we want to avoid a scenario where a child needs to give their parent money. Not only is it uncomfortable, but it's also not tax-efficient.

Divorce

Setting up a SLAT takes considerable effort and expense. If you get divorced, you may feel that those costs were not worthwhile. More importantly, a divorce would terminate both spouses' access to the money in the trust.

The trust documents are drawn up so that the primary beneficiary's share passes to the contingent or co-beneficiaries upon divorce. Your ex doesn't get to keep your money, but you lose that indirect access.

Source Fund Limitations

You must have assets in your own name to fund a SLAT. The money cannot come from a joint account. It's not impossible to establish a SLAT when most of a couple's assets are co-mingled or the couple lives in a community property state, but it becomes a longer and more complicated process.

Reciprocal Trust Rules

While each spouse can create a SLAT to benefit the other, the trusts must be different enough to not run afoul of reciprocal trust rules. Violating those rules can undo the trusts and wipe out their tax benefits.

Final Thoughts

Spousal lifetime access trusts can be an excellent estate-planning tool, especially for people who are hesitant about the irrevocable aspect of the trust. Indirect access to trust assets and income through the beneficiary spouse, plus utilizing the SLAT's grantor trust status, can make this type of trust especially palatable.

Still, it's important to remember that a SLAT is an irrevocable trust, and it should only be funded with assets the grantor likely won't need as a source of income during their lifetime.

www.pitcairn.com | 800-211-1745

PITCAIRN®

Philadelphia
One Pitcairn Place, Suite 3000
165 Township Line Road
Jenkintown, PA 19046-3593

New York
Representative Office
99 Park Avenue, Suite 320
New York, NY 10016-1501

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