



Advanced Markets

# *Central Intelligence*

April 2021

## **This issue includes:**

- American Rescue Plan Act of 2021 brings third wave of COVID-19 relief provisions
- IRS extends federal income tax return filing due date because of ongoing pandemic
- State Supreme Court finds nonjudicial trust modification invalid as violating material spendthrift provision
- Appeals Court finds “Spouse” is not a class designation in trust
- Trustees not required to reimburse trust beneficiaries for taxes incurred



## **American Rescue Plan Act of 2021 brings third wave of COVID-19 relief provisions,** American Rescue Plan Act of 2021, §1319, enacted March 11, 2021.

### **Facts**

After numerous rounds and negotiations, the U.S. Congress finally passed the American Rescue Plan Act of 2021 with a straight party-line vote on March 10, 2021, and President Biden signed it into law the next day. The Act comprises 628 pages of wide-ranging legislation. While a complete discussion of the voluminous material is not possible here, this summary will address several details most likely to be of interest to our readers and their clients.

### **Individual taxpayer provisions:**

- **Recovery rebates.** Available to eligible individuals in the amount of \$1,400 (\$2,800 in the case of joint-return filers) plus \$1,400 for each of the taxpayer's dependents. The rebate is phased out with Adjusted Gross Income (AGI) between \$75,000 to \$80,000 (\$150,000 to \$160,000 for joint filers) based on 2020 returns. The definition of "eligible individuals" specifically excludes nonresident aliens, trusts, estates, and dependents. (Taxpayers claiming another as a dependent are entitled to a rebate for each dependent, however.) The payments are being processed as an advance rebate of overpaid taxes (without interest), but are not generally subject to reduction for amounts due to federal or state agencies.
- **Unemployment compensation.** Although unemployment compensation is generally includible in taxable income for federal income tax purposes under the Internal Revenue Code, the Act provides that for 2020 income tax purposes, for taxpayers with AGI under \$150,000, up to \$10,200 (\$20,400 for joint filers) of unemployment compensation received is excluded. Note that the AGI limit is a hard stop; the benefit is completely available below \$150,000 and completely not available at \$150,000 and above. Also, this AGI limit is the same for individual, joint, head-of-house, etc., filers.
- **Student loan discharge.** The Act provides that a taxpayer's income for federal income tax purposes excludes certain discharges of student loans after December 31, 2020, and before January 1, 2026. Eligible loan discharges are for post-secondary education if the loan is (a) insured or guaranteed by a federal or state entity, (b) issued by a private lender, or (c) issued by certain educational organizations.

### **Business provisions:**

- **COBRA premium subsidy.** COBRA premiums for "assistance-eligible individuals" from April 2021 through September 2021 may be entirely covered by a subsidy provided by the Act. The subsidy will not extend beyond an individual's maximum period of coverage if it ends before September 30, 2021. Group plans are required to provide notice of the subsidy to certain qualifying individuals.
- The Act provides for targeted "economic injury disaster loan" advances from the Small Business Administration. The advances will be treated as tax-exempt income, excludible from gross income for income tax purposes, and will ratably increase the basis of owners of a pass-through entity.
- The Act also provides for "restaurant revitalization" grants from the Small Business Administration to eligible restaurants, food trucks, and other food service providers. These grants will also be treated as tax-exempt income for tax purposes.

The Act contains numerous other provisions (paid sick and family leave credits, extension of the employee retention credit, extension of several unemployment benefit provisions into September 2021, modifications to PPP provisions, including an addition \$7.25 billion in funding, etc.).

## **IRS extends federal income tax return filing due date because of ongoing pandemic, IR-2021-59, March 17, 2021.**

### **Facts**

The Treasury Department and Internal Revenue Service announced today that the federal income tax filing due date for individuals for the 2020 tax year will be automatically extended from April 15, 2021, to May 17, 2021. Individual taxpayers can also postpone federal income tax payments for the 2020 tax year due on April 15, 2021, to May 17, 2021, without penalties and interest, regardless of the amount owed. This postponement applies to individual taxpayers, including individuals who pay self-employment tax. Penalties, interest, and additions to tax will begin to accrue on any remaining unpaid balances as of May 17, 2021. Individual taxpayers will automatically avoid interest and penalties on the taxes paid by May 17. Individual taxpayers do not need to file any forms or call the IRS to qualify for this automatic federal tax filing and payment relief. Individual taxpayers who need additional time to file beyond the May 17 deadline can request a filing extension until October 15 by filing IRS Form 4868. Note, however, that this relief does not apply to estimated tax payments that are due on April 15, 2021. These payments are still due on April 15. Also note that the federal tax filing deadline postponement to May 17, 2021, applies only to individual federal income returns and tax payments otherwise due April 15, 2021, and not to state-tax payments or deposits or payments of any other type of federal tax. Taxpayers are required to file income tax returns in 42 states plus the District of Columbia and state filing and payment deadlines vary and are not always the same as the federal filing deadline. Taxpayers should check with their state tax agencies for those details.

## **State Supreme Court finds nonjudicial trust modification invalid as violating material spendthrift provision, *In re Trust Created by McGregor*, 308 Neb. 405, March 4, 2021.**

### **Facts**

Decedent created a revocable trust that became irrevocable upon his death (the "Trust") in October 2009. Trust provided that his surviving Spouse was to receive income from the Trust during her lifetime and upon Spouse's death, Trust assets were to be divided into subtrusts for each of Decedent's two adult children, A and D. Thereafter, during A and D's respective lifetime, the trustee of the subtrust for each child beneficiary was authorized to make distribution for the beneficiary's "health, education, support, or maintenance." At death, the beneficiary child of each subtrust held a limited power of appointment to direct transfer of any or all assets then remaining in the subtrust for the benefit of any party other than the beneficiary, its creditors, or its estate. The Trust also provided that the assets "shall remain in trust" and that the Trust would be "irrevocable and not revoked or amended in whole or in part by the trustee, beneficiary or any other person." The Trust also provided that the subtrusts for A and D each be construed as "a non-support discretionary spendthrift trust that may not be reached by the beneficiaries['] creditors for any reason." In 2011, Spouse, A, and D entered into a trust-settlement agreement under which the parties agreed and consented that upon the death of Spouse, assets funding the subtrust for A and D would be distributed directly to each beneficiary outright and free of further trust. (The agreement also provided for specific property disposal not required in the Trust and necessary balance for equalization.) In 2017, however, Spouse sent communications purporting to revoke the settlement agreement. Shortly thereafter, the children filed an action to compel compliance with the agreement. The lower court held that the agreement was nonbinding for several reasons including, significantly, because the agreement violated the spendthrift provision of the Trust, which the court found to be a material provision. The children appealed the decision to the Nebraska Supreme Court.

## Holding

The Court affirmed the lower court's holding that the agreement was not binding because it violated a material provision of the irrevocable Trust. The Trust provided A and D only limited powers of appointment (and only at the death of the beneficiary), specifically withholding the power to appoint assets to the beneficiary of each trust of its estate or creditors. The agreement would in very real effect re-write the limited power of appointment at death to be a general power of appointment at any time. (The lower court also considered that because remaining assets would be distributed per stirpes to a beneficiary's issue if not otherwise appointed, these as-yet undetermined potential beneficiaries were unrepresented in the agreement and thereby stripped of their interests.) Like many jurisdictions, Nebraska law provides that a nonjudicial settlement agreement is valid only to the extent that it does not violate a material purpose of the trust and, further, that a "spendthrift provision in the terms of the trust is presumed to constitute a material purpose of the trust." (For these purposes, a spendthrift provision means "a term of a trust which restrains both voluntary and involuntary transfer of a beneficiary's interest.") By design, a trust is protective to the extent of the settlor's discretion and will and must be respected as such if lawful, possible, and not contrary to public policy. In this case, Decedent's intent is clearly stated and there is no evidence to override the statutory presumption that the spendthrift limitations be considered a material provision.

## Takeaway

While the law of most jurisdictions provides mechanisms to modify even irrevocable trusts to remedy inefficiencies or better serve the clear intent of the settlor, such a possibility will almost always have clear limits. In the end, the clearly stated will of the settlor defines the range within which valid modifications must fall. A well-written trust can bend but will be hard to break.

**Appeals court finds "Spouse" is not a class designation in trust, *Carol Ochse and William W. Ochse, III, individually and as trustees of the William W. Ochse III Family 2008 Trust, Appellants v. Cynthia Cadwallader Ochse*, No. 04-20-00035-CV, 2020 Tex. App. LEXIS 8922, November 18, 2020.**

## Facts

In 2008, Mother created an irrevocable Trust for the benefit of her only Son. At the time the Trust was created Mother was unmarried and Son was married to X. Son and X had a daughter (GD) and a son (GS). The Trust provides that the intent of the settlor (Mother) was to create the Trust "for the benefit of her son, her son's descendants, and her son's spouse." The Trust also provided that any contribution to the Trust "shall be subject to a right of withdrawal by each member of the class composed of the primary beneficiary of such trust, the then living descendants of such primary beneficiary and the spouse of such primary beneficiary." The trustee of the Trust is authorized to make distributions for the benefit of "the primary beneficiary of such trust, the then living descendants of such primary beneficiary and the spouse of such primary beneficiary" according to an ascertainable standard. The Trust appoints Son as initial trustee of Trust and X as successor trustee (with an independent co-trustee) and names X as initial trustee of subtrusts for the benefit of GD and GS. The Trust also provides that if any trust thereunder is without a trustee, then X alone is to serve as trustee, if possible. In 2012, Son and X divorced after a marriage of 30 years; three years later, Son married Y. In 2018, GD and GS filed suit seeking to remove Son as trustee of the Trust, alleging breach of fiduciary duties. The suit joined X as an interested party due to her status as a beneficiary of the Trust. X sought a judicial declaration that the terms "primary beneficiary's spouse" and "son's spouse" in the Trust solely referred to her because she was Son's spouse at the time the Trust was executed. Y intervened and sought a declaration that those terms in the Trust referred to whomever might be married to Son at any given time meaning, presently, Y. The trial court granted summary judgment to X that the terms "primary beneficiary's spouse" and "son's spouse" are unambiguous and specifically refer to X and no other party or potential party. Son and Y appealed to the Fourth Court of Appeals.

## **Holding**

In the absence of any language in the Trust addressing the competing interpretations, the Court determined that it was to interpret the terms within the Trust provisions according to local precedent and, if none, in such a way as would harmonize all provisions of the Trust and give effect to all provisions, so that no provision would be rendered meaningless. In the first instance, the interpretation of “spouse” in the Trust as a status or class is inconsistent with Texas legal precedents on the use of “class gifts” in trust. Where a class is intended under such precedents, the language was clearly describing the intended class; such was not done by the relevant Trust provisions. The Court considered this reasoning dispositive of the questions before it. Furthermore, however, in the second instance, the appointment of X by name as a trustee or successor trustee of several subtrusts under the Trust strengthens the conclusion that the settlor contemplated only X as the spouse who would be a party to the Trust as beneficiary and trustee. It is for this reason that the interpretation of “spouse” as a status or class beneficiary fails to harmonize all provisions of the Trust and give consistent meaning to all its provisions. Thus, the Court affirmed the ruling of the lower trial court that X was an interested party in the litigation as a beneficiary and successor trustee of the Trust.

## **Takeaway**

Choose your words carefully when your instrument is to be irrevocable. If it is or may become important to interpret a term more broadly than its common-sensical usage might imply, then the draftsman must take care to be clear of such intent. Many states have precedential “default” interpretations that must be overridden if a different meaning is intended. In this case, for example, if the intent was truly to create a class of beneficiaries, the draftsman would likely have defined “spouse” as the person to whom the primary beneficiary is married to and living with at any given time, if any.

## **Trustees not required to reimburse trust beneficiaries for taxes Incurred,** *In re Davidson Magnifying Glass Non-Exempt Trust*, No. 351357, Michigan Court of Appeals, January 14, 2021.

### **Facts**

During life, Decedent created two trusts for the sole benefit of each of his two adult children, a son and a daughter. The provisions of each trust permit the beneficiary to transfer trust property to third parties under certain circumstances. The trusts’ provisions also direct the trustee of each trust to reimburse the beneficiary for certain transfer taxes that result from any such transfer of trust property to a third party. Pursuant to these referenced provisions, each beneficiary at different times elected to transfer specific property from the beneficiary’s respective trust to third parties and, in doing so, incurred U.S. federal gift taxes that were offset by “spending down” the beneficiary’s basic exclusion amount (often referred to as the “unified credit”) under IRC §2010. Each beneficiary requested reimbursement for the amount of gift taxes value of the basic exclusion amount reduction. The trustees of the trusts refused to reimburse the requested amount and the beneficiaries disputed the decision. The trustees each filed a petition with the appropriate probate court for limited supervision seeking instruction on the administration of the trusts and, specifically, the interpretation of the relevant trust provisions. The probate court determined that the trustees were not required to reimburse the beneficiaries for the amount of basic exclusion amount expended. The beneficiaries appealed the decision to the Court of Appeals.

### **Holding**

The Court stated that when construing a trust, a court’s sole objective is to ascertain and give effect to the intent of the settlor. This intent is gauged by the language of the trust provisions themselves unless there is ambiguity. A court may not construe a clear and unambiguous will or trust in such a way as to rewrite it, and, where possible, each word should be given its meaning. The relevant trust provisions states, under the heading “Payment of Taxes:”

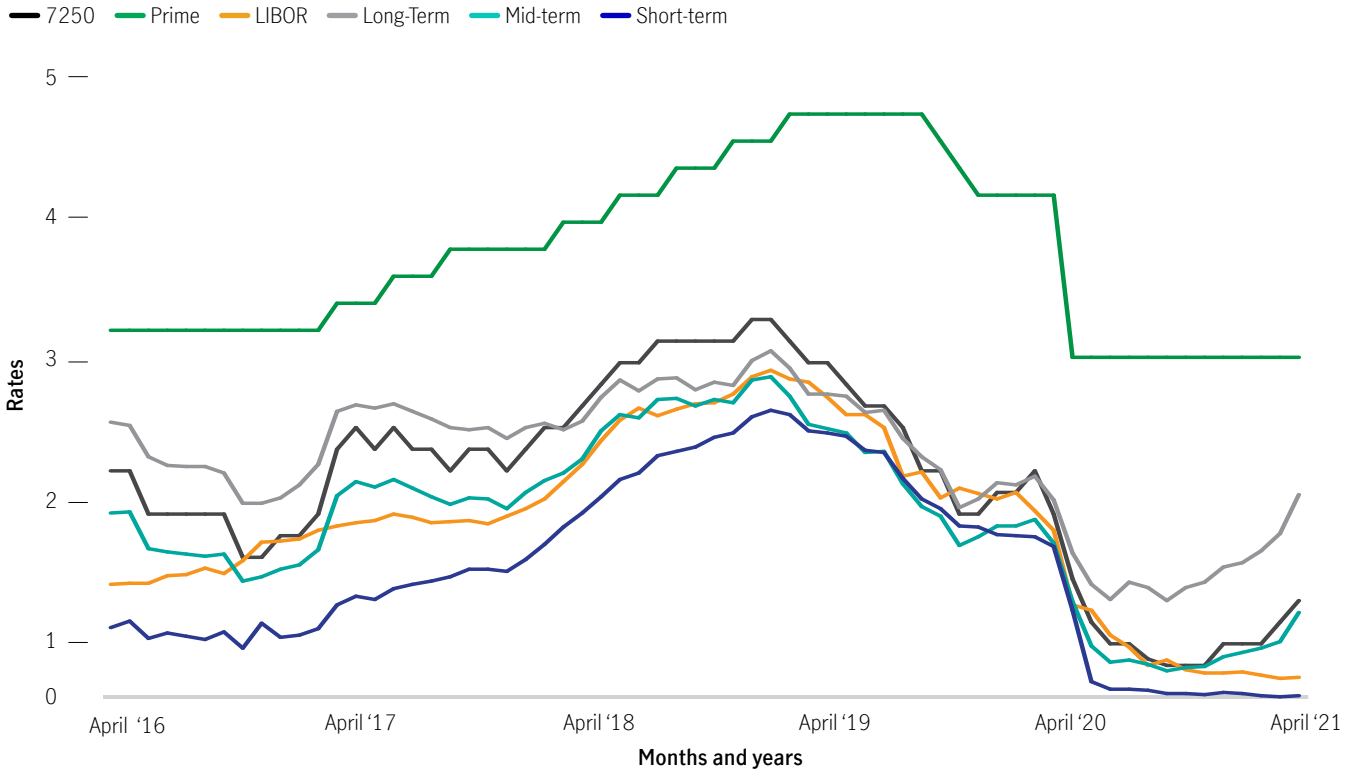
Following any transfer of Trust Property which results in any Transfer Taxes to the beneficiary of any trust created under this trust instrument, the Trustee shall reimburse such beneficiary or distribute trust property to such beneficiary ... . [T]he Trustee shall pay from the remaining property held in a trust for the beneficiary, directly to the appropriate governmental authority, to the beneficiary or to the Personal Representative of the beneficiary's estate, as the Trustee deems advisable, without seeking reimbursement or recovery from any Person, the amount by which the Transfer Taxes payable in any jurisdiction by reason of the transfer are increased.

“Transfer Taxes” are defined by the trust provisions to mean any gift taxes, including any gift, transfer or other similar succession taxes imposed by any state resulting from a transfer subject to federal gift tax[.]” Although the definition of “Transfer Taxes” includes “any gift taxes,” under the cited provision offset above, the taxes must also be “payable.” The parties vehemently disputed the meaning of the word “payable.” As the trusts do not define payable, the Court turned to the common usage of the word to determine its plain and ordinary meaning, which the Court finds “that which may, can, or must be paid.” From the totality of the common usage of the word “payable,” the Court holds that the beneficiaries are entitled under the trust provisions to be reimbursed only for the amount that they were required to pay in taxes, i.e., that amount of money that they were required to expend to discharge their tax obligations. Because a basic exclusion amount/unified credit is not an amount that was or ever will be required to be paid, it is not payable.

### **Takeaway**

While there can be some reasonable doubt whether this outcome in this case is likely to be what the settlor intended with the language of the trusts, that language is often all we have to go on. As we often reiterate, when drafting legal direction in a document, especially in a document like a will or trust where the grantor or testator is not likely to be available to provide extrinsic evidence as to intent, it is imperative to be clear and precise and to consider all possible interpretations of one's language.

**The following are historical graphs of various rates that are commonly used by the Advanced Markets Group.**



**Take a look at how rates compare this month to last month:**

	Short-term AFR	Mid-term AFR	Long-term AFR	7520	LIBOR	Prime
<b>April '21</b>	<b>0.12%</b>	<b>0.89%</b>	<b>1.98%</b>	<b>1.00%</b>	<b>0.28%</b>	<b>3.25 %</b>
<b>March '21</b>	<b>0.11%</b>	<b>0.62%</b>	<b>1.62%</b>	<b>0.80%</b>	<b>0.29%</b>	<b>3.25 %</b>

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MLINY040521982-1

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