

Does Your Estate Plan Offer Full Generation Skipping Benefits?

A strategic insurance plan can provide tax-free dollars to your grandchildren or great-grandchildren that far exceed the premiums you pay.

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If a declaration of independence had to be written for wealth transfer and preservation, you would not find the phrase "all generation skipping trusts are created equal." A poorly drafted generation skipping tax (GST) trust simply bypasses one generation, while a more sophisticated plan provides for wealth to pass a multitude of generations with flexibility based on events or need.

The idea of a GST trust is to maximize your grandchild's or great-grandchild's future inheritances that otherwise could be subject to both federal estate and gift taxes of as much as 45 percent and an additional 45 percent generation skipping tax, using 2009 tax rates.

Congress created the generation skipping tax in 1986 as a way to prevent wealthy individuals from avoiding estate taxes over multiple generations. But the pain of Uncle Sam's cut can be limited by a carefully crafted GST trust enhanced by a life insurance policy. At your passing, such a trust normally can provide tax-free dollars to your grandchildren that far exceed insurance premiums paid.

Evaluating life insurance as a leveraged funding mechanism is only one consideration when it comes to establishing a generation skipping tax trust. A wise family patriarch or matriarch should have the vision to think about who will act as trustee several generations from now and decide how much flexibility to give subsequent generations to modify and control the trust and the future distributions from it.

In the most "liberal" fashion, beneficia-

ries are named as their own trustees and have the ability to name their "successors" as well. Trustees can be given the ability to tap the trust, both income and principal, for health, support, maintenance and education purposes. This is the broadest standard afforded under the Internal Revenue Code.

Beneficiaries may also be able to redirect distributions at their death. This is known as a "general power of appointment" (GPOA). In order for it to be applicable, the GPOA must "limit" the scope to which the beneficiary can appoint distributions.

The broadest possible scope would be to allow the beneficiary to make appointments as the beneficiary chooses, except for creditors



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of the beneficiary at his or her death. Obviously this is a rather broad GPOA, in that the beneficiary could do anything else that he or she chooses. A narrower "special power of appointment" can be anything less. For example, the trust might restrict distributions that could be made only to natural born or adopted issue of the trust creators.

Due consideration should be given to the income tax aspects of the generation skipping trust. A provision exists whereby the earnings of the trust can be deemed taxable not to the trust itself, but rather to the creator of the trust. In this way, the creator is responsible to pay the taxes on the earnings arising within the trust, while the creator does not actually receive any monies from the trust with which to pay it.

While this may sound incongruous, it is actually a benefit, because it allows the creator to further reduce his or her taxable gross estate without making taxable gifts to do so. This is known as a "defective trust."

There can be other important non-tax advantages to GST trusts. For example, an irrevocable trust, if properly structured, can usually provide valuable asset protection for your children and grandchildren from di-

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Life insurance often used to fund trust

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forces and creditors.

It makes sense to allocate your GST tax exemption while you are alive to benefit from the additional compounding of these gifted assets. Any asset growing in these trusts that exceeds the distribution will compound free of gift and estate taxes for generations.

Rules for establishing GST trusts vary on a state-by-state basis. In Florida, they can last 360 years, but in many other states these trusts may exist in perpetuity.

Once you determine that you want to establish some form of GST trust, you will need to decide what types of assets will be used to fund the trust. Life insurance is one of the preferred funding vehicles. Just insure your life and your spouse's life, hold the policy in an irrevocable trust, name your grandchildren as the beneficiaries and contribute enough money annually to the trust to pay the premiums. Additionally,

families often use insurance with some combination of additional growth-oriented assets to generation skip.

While GST trusts did not exist when the Declaration of Independence was crafted, there is no reason not to follow one of Declaration signer Ben Franklin's best-known maxims: "A penny saved is a penny earned." Declare your own independence — maximize the options that protect the money you wish to pass to your heirs from taxes.

Richard S. Bernstein, CEO of Richard S. Bernstein & Associates, Inc., is an insurance advisor for high-net-worth business leaders, families and charitable organizations. He is an advisor to the Trump Organization and many of America's wealthiest families. He has been nationally recognized for his knowledge, innovation and expertise by his peers.