

Benefits of Keeping Property in Trust

In last month's article about Dynasty Trusts, I noted that there are advantages to leaving property in trust as opposed to distributing it outright to beneficiaries. If property is distributed outright to a beneficiary, all of the property is subject to the claims of the creditors of the beneficiary. If the beneficiary is immature, the beneficiary can create voluntary creditors by imprudently spending the money. (Think for a moment what you would have done with a large sum of money at age 18. Not many would have invested it.)

Creditor Protection

Even if the beneficiary is mature, he/she may encounter involuntary creditors. Marriage may lead to divorce. In Massachusetts, the law is not clear that a divorcing spouse can not reach property in trust, but much more often than not, the trust property is protected. An auto accident can lead to a lawsuit and more involuntary creditors. If the property remained in trust, these creditors could not reach the property, yet it could continue to benefit the beneficiary.

Estate Tax Savings

Considering that people live much longer than in years past, property often does not pass from one generation to the next until children are reaching their own retirement. They may not "need" the money, but would prefer it to benefit their children; however, gift tax rules limit the amount that they can transfer to their children. Property in trust can avoid inclusion in the estates of the children, saving substantial estate tax and allowing an unlimited amount to benefit the grandchildren of the decedent. Moreover, a trust can provide for the children if circumstances ever changed and they needed the property. Keeping property in trust is actually much more flexible than distributing it outright.

Income Tax Savings

If property remains in trust, there are income tax planning opportunities too. Because a trust can distribute income and the income tax liability associated with it, money can be used to pay a grandchild's college tuition. The grandchild is not likely to pay much, if any, income tax if this is the majority of his/her income. Alternatively, if the property were distributed to the child of the decedent, he/she would be taxed on the income, likely at a higher rate, even if the income were used for the grandchild's tuition.

Control from the Grave

Even with all of the benefits of keeping property in trust, many people view this as control from the grave and avoid this technique for two reasons. First, there is no mechanism for making good distribution decisions. Second, there are no qualified people to make the decisions. In next month's article, I will address the reasons why some people choose not to keep property in trust and how, with moderate controls in place and capable trustees, the benefits to keeping property can be obtained without the detriments. Before creating a trust or otherwise providing for the disposition of your property, I suggest that you consult with an estate planning attorney.

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