

GOLDENBULLETS

Ryan M. Wilson
Fraser Trebilcock Davis & Dunlap, P.C./Lawyers
124 West Allegan Street, Suite 1000
Lansing, MI 48933
Telephone: (517) 377-0897
Fax: (517) 482-0887
Email: rwilson@fraserlawfirm.com

THOUGHT YOU'D LIKE TO SEE THIS:

SALES TO GRANTOR TRUSTS

Among the cutting edge tools and techniques of sophisticated estate planning, sales to grantor trusts rank high on the list. A “Grantor” Trust is an irrevocable trust deliberately designed to fall under rules that result in the grantor, the creator of the trust, being treated as the “owner” of trust assets, for income tax purposes only.

The result is that items of income, deductions, and credits of the trust are attributable to the grantor; therefore, the grantor is taxed on trust income and is entitled to trust deductions and credits.

This estate planning tool is also called an “Intentionally Defective Grantor Trust (IDGT).” This “defect” is an intentional provision, a power inserted into an irrevocable trust.

But why would an estate planning professional create a trust which was deliberately “defective?” The answer is that some of the nation's top planners feel that a favorable consequence of the grantor’s being treated as the same taxpayer as the trust is that a sale or other transaction between the grantor and the IDGT will not result in any capital gain (or loss). In fact, they posit that transactions between the Grantor and his/her trust are treated as though the grantor moved cash or other assets from one pocket to another, i.e., as if there was no transaction, for income tax purposes!

They feel this makes it possible to shift very large amounts of wealth to a younger generation, or to a close friend, and yet avoid or minimize gift tax consequences. For example, a grantor could sell property with built-in capital gains to a trust he/she creates for his/her children or a close personal friend, and since the transaction is considered a non-event for income tax purposes, he/she will not have any reportable gain for federal tax purposes. (Note that state law may differ!).

The trust, if it has the cash or other property to pay for the asset it is purchasing, can pay for the grantor/seller's property in a lump sum. But more commonly, the trust will pay the Grantor for the property it is buying with a promissory note. Usually, that note is payable over a relatively long period of time, in an installment sale or perhaps a self-canceling installment note (SCIN) or even a private annuity. Again, the theory is that income paid by the trust to the Grantor on the unpaid balance of the installment sale or SCIN or private annuity "loan" will not be reportable income because it's as if the Grantor were moving money from one pocket to another.

Yet, amazingly, even though the IRS considers the grantor as the owner of trust assets for income tax purposes, because the estate tax is a separate, distinct, and very differently operating body of law, and because the trust is deliberately drafted to fall outside its scope, a very different result should apply for estate tax purposes. The trust assets are not includible in the grantor's estate!

The bottom line is: An intentionally defective grantor trust is one which is "treated as owned by the grantor for income tax purposes, but not for gift or estate tax purposes."

The IRS is increasing its efforts to challenge IDGTs, so this technique does carry some risks. There are, of course, alternatives to this technique and, as in all of the tools and techniques of estate planning, costs and downsides.

AS ALWAYS, PLEASE FEEL FREE TO CALL TO DISCUSS THESE OR OTHER MATTERS OF CONCERN.

Note: UNIFORM DONOR CARD. There are four ways to make an anatomical gift: (1) last will and testament; (2) personal identification card issued by the secretary of state; (3) driver's license issued by the secretary of state; or (4) uniform donor card. I recently added a Uniform Donor Card form as a resource to our firm's website at www.fraserlawfirm.com. Our website has been recently updated with a whole new look. Please check it out.

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"Golden Bullets" is provided as a source of general information about current developments in the practice of estate planning and related topics. If you have questions regarding this issue or estate planning in general, please contact me prior to taking action.

Ryan M. Wilson (517) 377-0897
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