



Leaving a lasting legacy with a dynasty trust

The idea of leaving a legacy that lasts for hundreds of years — or even perpetually — has a certain romantic appeal. But romance alone shouldn't be the driving force behind your estate plan.

A dynasty trust can preserve substantial amounts of wealth — and shelter it from federal gift, estate and generation-skipping transfer (GST) taxes — for generations to come. But a dynasty trust isn't an end in itself. First, you need to ask yourself what you hope to accomplish with your estate plan. Only then can you determine whether a dynasty trust or other estate planning vehicles will best help you achieve your goals.

A recent phenomenon

The concept of a trust that can last "forever" is a relatively recent one. Up until around 10 years ago, virtually every state applied the "rule against perpetuities," which limits a trust's life span. The rule is complicated, but in general it prevents trusts from lasting more than 100 years or so.

During the last decade, however, there's been a trend among the states to abolish or relax the rule against perpetuities. Today, around half the states have either eliminated the rule or extended the limit to several hundred or even 1,000 years.

Perpetual growth

Your contributions to a dynasty trust are considered taxable gifts, but you can minimize or avoid gift taxes by taking advantage of your lifetime gift tax exemption (currently \$1 million) and your annual gift tax exclusion (currently \$12,000 per recipient, \$24,000 for gifts by a married couple).

And don't forget that you've got a \$2 million estate tax exemption — or whatever is left of it — to use at your death. To transfer as much wealth as possible to your dynasty trust, allocate your remaining GST tax exemption to it to ensure that your dynasty trust can benefit your grandchildren and future generations without triggering harsh GST taxes.

Also consider leveraging your GST tax exemption by funding the dynasty trust with life insurance policies or property that's expected to appreciate significantly in value. So long as your exemption covers the value of your contributions, any future growth will be sheltered from GST tax.

After you fund the trust, the assets can grow and compound indefinitely. The trust should be designed to make distributions to your children, grandchildren and future descendants according to criteria you establish. So long as your beneficiaries don't gain control over the trust, the assets will bypass their estates. As an added bonus, you could structure the trust as a grantor trust so that you pay any taxes on the trust's income, and (at least during your lifetime) the assets are free to grow without being eroded by taxes.

Allowing a trust to grow for several generations can produce enormous amounts of wealth. For example, a trust funded with an initial contribution of \$1 million and earning an average annual return of 6% will be worth more than \$18 million in 50 years and almost \$340 million in 100 years (assuming no income taxes or distributions).

Practical considerations

If you think a dynasty trust might help you achieve your estate planning goals, talk to your advisors about the practical requirements for establishing one. You don't have to live in a perpetual trust state to take advantage of this technique; generally, it's just a matter of specifying the applicable state law in the trust agreement.

And there may be other requirements, such as being required to appoint at least one trustee who resides in the state whose laws govern the trust — a bank or other corporate trustee, for example — and locating at least some of the trust assets in that state. These rules vary from state to state, so choose carefully. Typically, the most attractive states are those that allow perpetual trusts and have no state income tax.

A lasting legacy

A dynasty trust can be a powerful tool for creating a legacy that lasts for decades or even centuries. Before establishing a dynasty trust, however, discuss your estate planning goals with your advisors and determine whether it's the right tool for the job.

Dynasty trust planning ideas

So, how can a dynasty trust help you achieve your estate planning objectives? Why would you want to preserve your wealth for distant descendants whom you'll never meet when you have children and grandchildren who can enjoy your generosity while you're alive to see it? There's no short answer to these questions, but here are a few ideas to consider:

Supplemental assistance. If your estate plan already provides for your immediate family with resources to spare, a dynasty trust can be a nice supplement to your plan, allowing you to provide for future generations as well.

Providing a safety net. You may be reluctant to turn your kids into "trust fund babies" by allowing them to live off their inheritances. You can design a dynasty trust to ensure that your children, grandchildren and future generations pursue their own careers while at the same time providing them a safety net in the event they're unable to pay for health insurance, medical care, education, housing or other necessities.

Sweetening charity. A dynasty trust can be a great tool for encouraging charitable giving. For example, you might provide for the trust to make "matching distributions" to beneficiaries equal to a percentage of the charitable contributions they make each year.

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