

## What is a Generation Skipping Trust?

A Generation Skipping Trust is a Continuing Trust established for a child or other beneficiary which is intended to last for the beneficiary's lifetime. Such a Trust would typically be established under an individual's or couple's Living Trust agreement.

It should be noted that there is some confusing terminology as to Generation Skipping Trusts, or GST's. The "Skipping" does not mean that the child for whom the trust is held does not benefit from the Trust. It is possible to give a child almost complete control and benefit from such a trust, but rather, the Skipping refers to the fact that the Trust will not be subject to estate tax at the child's death.

As discussed above, there are various reasons for establishing a Continuing Trust, which could include a trust lasting the beneficiary's entire lifetime, to protect the beneficiary from himself or herself, and to reserve assets for specific use. However, even where parents feel completely comfortable with their children receiving their inheritance outright, the Generation Skipping Trust offers advantages to the children and their descendants.

For instance, a Generation Skipping Trust could be established for the benefit of a couple's child, rather than outright distribution. The child could act as her own Trustee, manage the trust assets, and distribute to herself whatever assets she felt was necessary. At her death, the assets could be distributed as she set forth in her Will. Effectively, she has almost as much control as she would have had she received the assets outright.

The advantages are that these assets would not be taxed in the child's estate at her death, because of the trust arrangement. The basic rationale is similar to that of a Credit Shelter Trust.

This savings can be very significant. For instance, let's assume a similar estate taxation system is still with us in the future, and that a child would have her own taxable estate at her death based on her own assets. If we had established a Generation Skipping Trust for her benefit at her parents' deaths, funded with \$2,000,000, and this trust, after accounting for any distributions the child makes from the trust, grew at 5%, then in thirty years, the Trust would be worth approximately \$9,000,000. The fact that this is in a Generation Skipping Trust rather than owned outright by the child would result in estate tax savings between \$4,000,000 and \$5,000,000. As noted, there is a planned one-year of repeal for estate taxes in 2010, which could be extended in the future, so the exact nature of the savings is uncertain, but it represents the best chance of reducing taxes given that uncertainty.

The arrangement also aids in keeping the child's inheritance separate from her husband, so that it will not be commingled, and possibly subject to division in the event of divorce. It may also offer protection from creditors.

The flexibility of such an arrangement is such that if a child does very well on her own, establishing this separate trust can save a great deal of estate taxes, as indicated above, and yet if a child has greater need of the assets, he or she can use as much as needed during lifetime.

There is a Generation Skipping Transfer Tax, GSTT, essentially designed to limit the amount of this benefit, and each individual currently has a \$1,100,000 exemption from the GSTT, and that is generally the amount that can be used to establish Generation Skipping Trusts from any one person. This amount, as noted below, will increase based on inflation through 2003, and thereafter be the same as the estate tax exemption.

I hope this helps you with your retirement planning, estate planning, tax planning, and financial planning journey. Let me know if I can be of assistance. I welcome the opportunity to be a part of your team.

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