

**In the Spotlight:**

Gideon Rothschild was honored in June by UJA-Federation of New York, Trusts and Estates Group of the Lawyers Division. Gideon was recognized for his many contributions in the field of Trusts and Estates, including his groundbreaking work in the area of asset protection planning. With Gideon Rothschild as honoree, the event was attended by over 400 professionals in the Trusts and Estates field. The evening was a huge success, raising over \$300,000 for the organization.

The members of Moses & Singer's Trusts & Estates group congratulate Gideon on his much deserved recognition.

Our partners have recently presented at the following events:

- Lori Douglass spoke at the National Funeral Directors and Morticians Association concerning "Business Succession Planning: Minimizing Family Disputes."
- Dan Rubin participated in a webinar entitled "Asset Protection Strategies" for the American Institute of Certified Public Accountants.
- Gideon Rothschild spoke at the NYU Summer Tax Institute on "Tax Planning for Non-Resident Aliens."
- Ira Zlotnick conducted a CLE program on Estate Planning 101 to the firm's attorneys.

A schedule of future speaking engagements is available on our website at http://www.mosessinger.com/news/events_new.php?pid=26.

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Planning For Grandchildren

Help in Paying for Grandchildren's Education: The HEET, An Exciting Estate Planning Tool

With education costs rapidly rising, some grandparents are turning to so-called Health and Education Exclusion Trusts (sometimes referred to as "HEETs") to help pay for their grandchildren's education.

Various Ways to Give

There are several ways that grandparents can help to pay for their grandchildren's education.

1. The simplest way is to pay the tuition directly to the school. The Internal Revenue Code allows individuals to pay an unlimited amount of tuition on behalf of another person without incurring gift or generation-skipping transfer tax consequences so long as the payment is made directly to a qualified educational organization. The payments can be made towards any level of education, from pre-school through post-graduate school, and any type of learning, from karate class to medical school. However, this option is, of course, available only while one is alive and cannot be used to pay for expenses other than tuition, such as room and board.

2. Another popular vehicle is the "Qualified Tuition Program," also known as a "Section 529 Plan" (named after the governing section of the Internal Revenue Code). This vehicle allows individuals to contribute up to \$12,000 (\$24,000 for husband and wife) into the plan each year. In fact, up to \$60,000 may be added in one year pursuant to a special election that can be made to front-load the plan with five years of such gifts (called "annual exclusion gifts"). All earnings are exempt from income tax during the accumulation phase. Any funds which are later used to pay for the beneficiary's higher education expenses, including room and board, will be free from federal income tax when distributed (and, depending upon the state in which the grandparent resides, possibly free from state income tax, as well). However, such plans can be used only for higher education expenses, must be set up for the benefit of a named individual, can only be funded with cash, may have a limited range of investment options and uses up one's annual exclusion gifts which might be used otherwise.

A Better Way to Give?

If, however, one wishes to provide for the education of as yet unborn grandchildren and

more remote descendants (as well as existing ones, of course), in a tax efficient manner, and if one is also charitably inclined, the HEET is an exciting option to consider.

So, How Does a HEET Work?

Like any other trust, a HEET requires (i) a grantor (here, the grandparent), during life or upon death, to give cash, securities, real estate, or some other type of property, in any amount (subject to tax considerations), to (ii) a trustee (which can be a friend or family member, or alternatively, an institutional trustee, like a bank), for the benefit of (iii) one or more beneficiaries (here, existing and future grandchildren and more remote generations of descendants).

Without more, however, the creation of such a trust would subject the grantor to the imposition of a generation-skipping transfer tax (the "GST tax"), which is a tax that is imposed, among other circumstances, when transfers are made to a trust where all of the beneficiaries are "skip persons" (generally meaning persons who are two or more generations younger than the grantor). Moreover, the GST tax is not insignificant – it is imposed at the highest federal estate tax rate, which is currently 45%!

The inclusion of a charity, including a family foundation or donor advised fund, as an additional beneficiary of the HEET, however, will prevent the trust from having only skip persons as beneficiaries and, therefore, the imposition of the GST tax will be avoided. It should be noted that although the

inclusion of a child, for example, as an additional beneficiary of the trust will also avoid the imposition of a GST tax upon the funding of the trust (since, again, not all beneficiaries will be skip persons), this will only defer the imposition of the GST tax until the death of the child – the idea behind the inclusion of a charity as an additional beneficiary of the trust is that a charity can have a perpetual existence. The amounts payable to a charitable beneficiary must not be insignificant, however.

Finally, distributions from the trust for the benefit of the grantor's grandchildren and more remote descendants (paid to the education provider) will not cause the imposition of GST tax since those payments qualify for the general exclusion from tax that applies to payments made directly to a qualified educational organization (or medical provider).

Since a HEET is an irrevocable trust which is structured as a completed gift for gift tax purposes, contributions will be subject to gift tax if funded during the grantor's lifetime (and will avoid inclusion in the grantor's estate when the grantor later dies), or will be subject to estate tax if funded upon the grantor's death. However, as with other types of trusts, various options exist for minimizing, or even negating, the gift or estate tax consequences of funding a HEET.

If the HEET is set up in a jurisdiction that allows trusts to continue in perpetuity, such as New Jersey or Delaware, the HEET can provide for the health and education costs of future

generations of grandchildren, great-grandchildren, and more remote descendants, in a tax efficient manner.

Summary

Obviously, HEETs are not for everyone. But in an era where the ever rising cost of education intersects with our clients' commonly expressed sentiment that the greatest gift they can give to their descendants is a quality education, the HEET is a tool which should not be overlooked. A HEET must be properly structured in order to provide the maximum benefits. If you would like to learn more about using a HEET as part of your estate planning, please call any of the attorneys in our department.

Leveraging Your Tax Exemptions When Gifting to Grandchildren

Background

Under current law, every individual may gift during his or her lifetime one million dollars (in addition to \$12,000 to any person per year) without the imposition of any federal gift tax. Every individual also has a two million dollar exemption from the generation-skipping transfer tax ("GST" tax) for gifts to grandchildren, great-grandchildren and beyond. The GST tax is a tax imposed on transfers to grandchildren and more remote descendants, or to trusts for their benefit, and is imposed at the highest federal estate tax rate (currently 45%).

It is generally advantageous to use the one million dollar gift tax exemption as early as possible

because doing so removes future appreciation from being subject to the estate tax. One method of using the exemption is to create and fund a trust for the benefit of one's spouse and descendants.

To illustrate, if a sixty-five year old funds a trust with one million dollars and the trust earns seven percent annually, the trust fund will double every ten years. If the donor lives to age eighty-five, the appreciation that will avoid estate tax at the donor's death will be three million dollars. The donor's family will save \$1,350,000 in federal estate tax (and potentially more in state estate taxes).

Further, if the donor allocated one million dollars of his GST tax exemption to the trust, no further GST taxes will ever be imposed upon such trust, no matter how large it grows, for as long as the trust will continue. If the trust is governed by the law of a jurisdiction allowing perpetual trusts, the trust may exist estate and GST tax-free for generations to come.

Again, assuming a seven percent return, and the donor's child surviving the donor by 30 years, that trust would grow to 32 million dollars during the child's lifetime. The amount that will escape estate taxation at the child's death will be over 14 million dollars!

The Problem

Often, one fully uses his or her lifetime gift tax exemption (\$1,000,000) without fully using all of his or her \$2,000,000 GST tax exemption because of a reluctance to pay the gift tax due on the \$1,000,000 difference in exemption amounts. If you are

married to a U.S. citizen, however, there is an estate planning strategy that will allow you to avoid the immediate gift tax.

The Strategy

How does this strategy work?

Assume our donor sets up a second trust for the exclusive benefit for his wife, Lucy, called a "Lifetime QTIP Trust". That trust would be set up in a state that permits trusts to last forever and qualify for the unlimited marital deduction. The marital deduction requires that the trust designate Lucy as the sole beneficiary during her lifetime and, at a minimum, that all income be paid out at least annually. The trust can also be structured so that the trustee will have discretion to pay principal to Lucy. Following Lucy's death, the trust would provide for continuing "discretionary" trusts for the benefit of their children and more remote descendants

Because transfers to the trust will qualify for the unlimited marital deduction, no gift tax is payable upon the funding of the trust. While the property transferred to the trust will be includible in Lucy's estate at her death, the trust property (including any appreciation thereon) will then and forever after be exempt from GST taxation. Moreover, in the ideal situation, the estate tax due will be paid from Lucy's other assets that are not exempt from the GST tax and this strategy will effectively double the size of the fund that will forever be exempt from estate and GST taxes for the benefit of their children, grandchildren and more remote descendants.

The Conclusion

The ability to create a trust that will avoid estate and GST taxation as long as it exists is a powerful estate planning tool. Although such a trust can be created under a will, there are a number of reasons why such a trust should be created during life (and as early in life as possible). Please contact us to explore how this strategy can achieve tax savings for your heirs. ■

In the Spotlight cont'd

This issue of the Wealth Preservation Advisor supplements our last issue focusing on efficient estate planning strategies to provide for grandchildren. For the charitably inclined who also want to help pay for their grandchildren's educational needs, the HEET may be the perfect solution. A Health Education Exclusion Trust (HEET) offers tax-favored benefits for certain health and education expenses while satisfying one's charitable goals.

Contact Us

If you have any questions about information contained herein, please contact any member of the Trusts and Estates and Wealth Preservation practice.

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Please feel free to forward our newsletter to your friends, family and business associates; they will likely find it as informative as you do. And, please consider referring us to anyone you know who has a need for our services – remember that someone was once kind enough to refer you to us!

Moses & Singer LLP's Trusts and Estates and Wealth Preservation practice provides a full range of legal services for the high-net-worth individual. In addition to substantial experience in the traditional areas of will and trust drafting and estate administration, the firm's attorneys utilize the latest techniques to implement effective plans for business succession and tax minimization. The firm is also recognized as a leader in wealth preservation strategies to protect client assets from future creditors and potential litigation exposure.

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