

# TRUST TOPICS

## Non-Tax Benefits of Trusts

### Advantages of Gifts in Trust over Outright Gifts

This Trust Topics focuses on the non-tax benefits of trusts and describes some of their more subtle tax benefits, concluding with a list of advantages that trusts have over accounts set up for minors under the Uniform Transfers to Minors Act.

There is a myth that trusts are useful only for saving taxes or for protecting minors or spendthrifts. On the contrary, leaving property in trust rather than outright can provide significant non-tax benefits for all beneficiaries, including surviving spouses and adult or minor children.

#### GENERAL BENEFITS

Gifts in trust have the following advantages over outright gifts:

**Claims of Creditors.** Assets held in trust are generally protected from the claims of the beneficiary's creditors. The value of this protection has increased in today's litigious climate. Lawyers, doctors, architects, corporate directors, and other professionals and executives worry about exposing their assets to claims of litigants. Many individuals seek to protect their assets from future creditors by engaging in complex, costly and risky strategies. By leaving assets in trust, rather than outright, you accomplish this objective for your beneficiaries in a simple, cost-effective and safe manner.

**Claims of Spouses.** If a beneficiary divorces his or her spouse, a divorce court has the ability to divide property between them. Assets inherited outright by an individual would ordinarily not be subject to division by the court; however, if that inheritance is commingled with other joint or "marital" assets, it might be subject to equitable division. By placing the inheritance in trust, you guarantee that it will not be subject to division by a divorce court.

Additionally, most states grant your beneficiary's surviving spouse an automatic right to take property from your beneficiary's estate, even if your beneficiary has intentionally disinherited that spouse. If you leave property in trust, however, the surviving spouse generally has no right to the property when your beneficiary dies. You can provide your beneficiary with the ability to benefit his or her spouse, without giving the spouse any automatic rights to that property.

**Keeping Funds in the Family.** You have the ability to select the ultimate recipients of property left in trust after your beneficiary's death. You may desire this result, especially if your beneficiary has no spouse or descendants and you wish for other members of your family or charity to benefit from the property.

**Disability or Death.** Assets held in trust can continue to be managed without interruption should your beneficiary become disabled or when he or she dies. This may not be the case for property owned outright by your beneficiary. Upon becoming disabled, an expensive, lengthy and potentially embarrassing court proceeding is

generally required to appoint a guardian to manage the property owned outright, unless your beneficiary has given a power of attorney to an individual. After a guardian has been named, continued court supervision over the management of investments and disbursements is usually required.

At your beneficiary's death, the probate process may cause delay in the executor's ability to collect, manage and distribute the property owned outright. Assets in trust are available immediately to pay debts and estate taxes. There is also continuity of professional management when assets are held in trust.

**State Income Taxes.** Through careful planning, a trust may not be required to pay state and local income taxes on accumulated income and capital gains.

**Professional Management.** Funds held in trust are more likely to be professionally managed, especially if a trust company is appointed trustee or co-trustee. Trust assets are also protected from anyone exerting undue pressure on your beneficiary for investment capital or charitable contributions.

## **BENEFITS SPECIFIC TO SPOUSES**

In addition to the above advantages, bequests in trust for spouses have two advantages:

**Intended Beneficiaries.** You may have a clear idea of whom you would like to receive your estate after your surviving spouse's death. If you leave that bequest in trust, your intended beneficiaries will receive the property. This is important if your current spouse is not the parent of your ultimate beneficiaries. It is also important if your surviving spouse remarries. As described above, a new spouse would have rights in the property that your surviving spouse owns outright.

**Post-tem Tax Planning.** A marital bequest in trust affords the most flexibility for estate tax planning.

## **BENEFITS FOR MINORS**

Many individuals make annual gifts to minor children under their state's Uniform Transfers to Minors Act ("UTMA"). Making those gifts in trust provides the following additional advantages over UTMA gifts:

**Control.** Custodial gifts become subject to your beneficiary's control upon his or her reaching age 21 (an age which is quite young). Gifts to a properly structured trust may be left in trust beyond age 21.

**Death.** If your minor beneficiary dies, the gifted assets would by law pass back up to the minor's parents—one-half to the mother and one-half to the father. This is true regardless of who made the gifts. This result may not be desirable, not only because it defeats the estate and gift tax reasons for making the gifts, but also because the parents may no longer be married to each other at the time of the child's death. By gifting assets to a trust, you can instead direct that your minor beneficiary's siblings receive the property at the beneficiary's death.

### **OTHER ADVANTAGES**

In spite of the above advantages, some individuals are reluctant to create trusts for competent, adult beneficiaries unless there is a significant tax benefit to doing so. They cite cost and inflexible provisions as two factors weighing against using a trust.

### **Significant Benefits for Minimal Cost**

We believe that the cost to create and manage a trust is minimal compared to the benefits derived from a trust. In fact, at Fiduciary Trust Company International, the cost of managing a trust—our trustee commission—is identical to our charge for investment management services; there is no additional fee.

### **FLEXIBILITY**

Trusts need not be—nor should they be—inflexible. Trusts are most powerful when they give the trustee the latitude to adapt to current circumstances, thereby allowing the trustee to carry out the grantor's wishes most efficiently and effectively. The key to ensuring flexibility lies in the drafting of the trust. Trust provisions should be flexibly drafted so that the beneficiary can receive maximum enjoyment from the trust property without destroying the trust's protective qualities. One method of creating flexibility is to give certain powers to the beneficiary. For example, the beneficiary can be given any one or more of the following rights:

- to demand a withdrawal each year from the trust of an amount equal to the greater of \$5,000 or 5%;
- to demand that trust principal be paid to his or her own spouse or children;
- to dispose of the trust property under his or her will; and
- to remove a trustee and designate successors.

All of these powers give your beneficiary a degree of control over trust property. If carefully worded, they will not destroy the trust's benefits. In addition, these provisions allow a financially sophisticated trustee to adapt the trust's investment strategy to changing circumstances in the markets or in the beneficiary's life.

### **IN SUMMARY**

Trusts can be much more than vehicles to protect a spendthrift beneficiary or to save taxes. Trusts can be powerful estate planning tools to provide for surviving spouses, adult or minor children, and other beneficiaries—especially for the most financially sophisticated of these beneficiaries.

**FIDUCIARY TRUST COMPANY INTERNATIONAL** was founded in 1931 to specialize in investment management and administration of assets for individuals and families. A bank charter permits Fiduciary Trust to act as executor and trustee, providing continuity of management through multiple generations.

Fiduciary Trust's investment management services were extended to foundations and endowments during the 1930s. In the early 1960s, Fiduciary Trust began investing internationally, making it one of the first American firms to develop global investment capabilities. Fiduciary Trust offers the following services to clients throughout the world:

- Investment Management
- Trust and Estate Administration
- Strategic Wealth Planning
- Manager Selection and Oversight
- Master Custody
- Private Banking
- Tax Reporting and Services

If you would like more information regarding Fiduciary Trust's services, please contact your portfolio manager or one of our representatives:

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<b>WASHINGTON, DC</b>	Stephen C. Thormahlen	(888) 621-3464
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**About the Author.** *Gail E. Cohen, Esq.*, Executive Vice President and General Trust Counsel and Head of Global Wealth Management, is responsible for all aspects of Fiduciary Trust's Wealth Management resources, including the departments responsible for client relationships, trust, estate, and tax in New York and across our regional offices. She has over 28 years of experience in the area of trusts and estates. Ms. Cohen is a member of the Board of Directors as well as member of the Management and Executive Committees. Before joining Fiduciary Trust in 1994, Ms. Cohen was a trusts and estates associate at the law firm of Debevoise & Plimpton. Previously, she was an associate at the law offices of Edward S. Schlesinger, P.C. She is a member of the Executive Committee of the Trust Management Association of the American Bankers Association and the Trust and Investment Executive Committee of the New York State Bankers Association. Ms. Cohen is a member of the New York City Ballet's Advisory Board, The Rockefeller University Committee of the Anti-Defamation League, and the Trust and Estates Steering Committee of the UJA-Federation of New York. Ms. Cohen received a B.A. from Mount Holyoke College and a J.D. *summa cum laude* from Brooklyn Law School. She is admitted to the bar in New York and New Jersey.



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