Using trusts in your estate plan

What is a trust?

A trust is a form of property ownership that separates beneficial ownership from legal ownership. A trustee is the legal owner of assets while one or more beneficiaries enjoy the benefits of property held in trust. The trust's creator (settlor or grantor) sets the terms of the trust, which the trustee carries out for the benefit of the beneficiaries. Although the instrument creating a trust governs most of its administration, state law also plays a role.

Types of trusts and their taxation

The terms of the trust will suit its purpose and will impact its taxation. Below are some terms used to describe different types of trusts for tax purposes. Your attorney and accountant can more fully describe such trusts and their uses.

- **Grantor trust:** A "grantor trust" is a trust over which the settlor (or in limited cases a beneficiary) has reserved a power or benefit causing the settlor (or beneficiary) to be treated as owning the trust's assets for federal income tax purposes.
- **Non-grantor trust:** A non-grantor trust is a trust that is not a grantor trust and is a separate taxpayer.
- **Completed gift trust:** A completed gift trust (a colloquialism) is a trust that has received a gratuitous transfer, which is a gift subject to the federal gift tax system (even though the application of certain deductions and exclusions may cause no gift tax to be due).
- **Incomplete gift trust:** An incomplete gift trust (a colloquialism) is a trust for which its creator has retained the ability to alter the trust, its beneficiaries or the enjoyment of trust income or assets. A gratuitous transfer to such a trust is not a gift for gift tax purposes.

Common uses of trusts in estate planning

Property management/avoiding probate

Probate is the legal process by which the appropriate government agency or court (it is different from state to state) determines that a document is a will. Property held in a revocable trust will avoid probate as it is owned by the trustee and not the decedent. Generally, you would be the trustee of a revocable trust that you create for your own benefit. Upon your death, the successor trustee steps in to administer the trust and its assets for the benefit of the trust's next beneficiaries. Should you become incapacitated, the successor trustee will step in to manage the property in the trust.

Trusts are flexible and customizable tools that can help you achieve your planning goals.

If you would like to learn more about using trusts in your estate plan, contact any member of your PNC Private Bank® team.

Life insurance planning

If a life insurance policy is owned by someone other than the insured, the insured has no incidents of ownership in the policy, and if the death benefit is not payable to the insured's estate, then the death benefit will be paid free from federal estate tax.

An irrevocable life insurance trust can own a life insurance policy, and if the above conditions are satisfied, the death benefit will not be included in the insured's gross estate.

Saving estate tax

Making gifts to trusts during your life up to your gift tax exclusion amount can remove the appreciation on the amount transferred — from the date of the gift until your death — from your gross estate.

Making annual exclusion gifts to trusts can remove the value of the gift and its appreciation from the date of the gift until your death from your gross estate.

Using a freezing technique, such as a grantor retained annuity trust or sale to an intentionally defective grantor trust, can limit the amount of growth from those assets included in your gross estate to a rate of return set by the IRS.

Assets owned by a grantor trust (see above) grow income tax free inside the trust, allowing the compounding base to grow more quickly, keeping a greater amount of appreciation out of your estate and reducing your estate by the income tax that you pay on the trust's income.

Building multi-generational wealth

The federal government imposes a generation-skipping transfer (GST) tax on the transfer of property to someone more than one generation below the "transferor," such as a grandchild. Many states allow trusts to last for very long periods, including "forever."

A citizen or resident of the United States has an exemption from the GST tax which can be allocated to a transfer in an amount sufficient to exempt the transfer from that tax. If GST exemption is allocated in an amount equal to the full value of the assets transferred in trust, (subject to exceptions) for so long as the property remains in trust, it will not be subject to estate or GST taxes.

Creditor protection

Property held in a spendthrift trust created for the benefit of someone other than the grantor is generally exempt from the claims of the beneficiary's creditors.

Some states allow the creation of asset protection trusts. Depending on state law, it may be possible for a grantor to retain a discretionary interest in such a trust while shielding the assets of the trust from their creditors.

Young beneficiaries

Directing your property to be managed and administered by a trustee for a minor beneficiary allows you to set terms and conditions for the use of the property and to determine when, if ever, the property is distributed to the beneficiary.

Guidance is available

Trusts are flexible and customizable tools that can help you achieve your planning goals. However, because trusts are so flexible, expert advice is often necessary to determine how best to fit a trust (or different types of trusts) into your plan. Working with your lawyers, accountants and financial advisors, you can build a plan that best uses trusts to benefit your family. PNC has been serving as trustee for over one hundred years. If you would like to learn more about using trusts in your estate plan, contact any member of your PNC Private Bank® team.