Using Trusts to Manage Your Wealth—Introduction

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An Overview of Trusts

- Millions of Americans use trusts to plan for the future with great flexibility and to address a host of specific concerns, including
  - Privacy
  - Tax management
  - Providing for multiple generations
- No matter what your financial objectives, concerns or net worth, trusts can—and should—be a fundamental part of your planning for the future
- Trusts can help you
  - minimize unnecessary taxes
  - put wealth to use in exactly the way you want
  - accumulate assets for retirement and your beneficiaries
  - and much more

What is a Trust?

- A trust is a separate legal entity, like a corporation
- Trusts hold assets for you or for the benefit of others
    - The person who creates a trust is known as the "**grantor**" or the "**trustor**"
    - The person or people or charities for whom a trust is created are known as the "**beneficiaries**"
    - Assets inside a trust are managed by a **trustee**, who has legal responsibility for managing and overseeing trust assets in accordance with your wishes
        - The **trustee** is also responsible for making distributions according to the instructions in the trust document
  - In some jurisdictions, the functions of a trustee can be separated so that, for example, one trustee deals with day-to-day administrative matters and distributions, and another deals exclusively with investment management responsibilities
- The trust document specifies how your assets should be managed, and how, when and to whom your assets will be distributed
- *Many people think only the wealthy can benefit from trusts, but this is simply not true*
- Trusts are highly flexible and can provide for an almost unlimited combination of needs, circumstances and objectives
- The trusts described in this presentation are primarily for personal purposes; this presentation does not describe or deal with trusts created for institutional use or securitizations, or other business purposes

Who can benefit from creating a Trust?

- Because they can be designed to satisfy specific needs and circumstances, trusts can address the concerns and objectives of most people
- ***Business owners and other individuals who wish their financial affairs to be private***
  - Wills have to go through a public probate proceeding
    - Armed with information from a probate proceeding, for example, a competitor might be able to force the sale of the decedent's business at a below market price
  - Unlike wills, trusts can shield assets and their disposition from public scrutiny
- ***Retirees, widows, widowers***
  - A trust can provide a monthly check, freedom from making investment decisions, and the burden of bookkeeping details
  - It can also provide for the management of financial affairs in the event of illness or incapacity, and tax savings on future gifts to charity
- ***Owners of highly appreciated assets***
  - When highly appreciated assets are sold, a large chunk of the gain may go to taxes
  - Certain kinds of trusts can shelter property from taxes on income and capital gain and thus avoid or defer the tax bite, or at the very least can shift the burden of the tax to a different generation
- ***Spouses in second marriages***
  - A trust can protect the interests of children from a previous marriage, and spare friends and family members from legal conflicts

Who can benefit from creating a Trust?

- ***Parents of children with special needs***
  - Trusts can ensure that children, and others with special needs, will have their financial concerns properly addressed
- ***Dependents***
  - Trusts offer a method of providing regular income to dependents (and the possibility of tax savings)
  - They also offer control through the choice of mandatory or discretionary payments as you may specify to suit the dependents’ changing support, educational and medical needs
  - In addition, trusts can provide for the orderly passage of your property without the expense, delay, or publicity of probate, and for professional investment management for family members who lack this skill
- ***Individuals concerned about becoming ill***
  - Trusts ensure that their financial affairs will be handled properly
  - They also forestall the need to name a guardian or conservator to oversee these responsibilities
- ***Unmarried couples***
  - A trust can provide a significant other with income for life while keeping assets in the grantor’s family
  - Upon death of the loved one, assets can revert back to a family member or to a specific charity, depending on the wishes of the grantor
- ***Individuals who need help in handling their finances***
  - Trusts can manage the assets, provide “spendthrift” provisions and oversee all responsibilities regarding record keeping and tax preparation for those unwilling or incapable of handling their financial affairs
    - A “spendthrift” trust is structured to protect trust assets from being used to satisfy the existing debts of a beneficiary as well as to prevent the beneficiary from using trust assets to secure new loans

What can trusts do?

- Ensure the orderly and private transfer of your property
- Manage your estate tax exposure
- Secure the cost of providing for an elderly relative, parent or disabled child
- Help finance a loved one’s education
- Create a portable and highly flexible pension plan
- Avoid probate costs
- Protect assets from creditors’ claims
- Provide a structured way to administer your personal and financial affairs should you become incapacitated
- Make a tax-advantaged charitable gift
- Manage assets for the benefit of heirs and other beneficiaries
- Provide the continuation of alimony or child support payments
- Save a business from an untimely liquidation or disadvantageous sale by concentrating voting and managerial control

What are some other benefits of trusts?

Control

- You set the terms under which beneficiaries will receive your wealth, allowing you to guide the generations that your trust will support
- You can specify the timing, amounts and conditions under which the trustee will make distributions to beneficiaries
- Alternatively, you can give the trustee(s) the discretion make distribution decisions according to your general instructions

Protection

- Assets put in a trust can be protected from both your and your beneficiaries' potential future creditors

Tax benefits

- Properly designed trusts can provide transfer and income tax savings to help preserve assets across multiple generations

Privacy

- In some states, a trust's existence and value may be kept confidential from the trust's beneficiaries until you wish otherwise
- This information also may be kept out of the public eye for as long as the trust lasts

Financial education

- The right trustees will help beneficiaries learn how to spend and budget wisely
- They also will teach beneficiaries about markets and investments

It is important to consult with your legal and tax advisors to establish a trust properly and to draft a trust agreement that is well suited to you and the people and/or charities you wish to benefit

What kind of assets can be owned in trusts?

You can use a broad array of financial vehicles in trusts, which can also hold non-financial assets

- Publicly traded, over-the-counter, or private stocks and bonds
- Real estate
- Mutual funds
- Art
- Collectibles
- Capital management accounts
- Life insurance and annuities
- Personal possessions
- And more

Take the next step

To help make trusts work for you, take an inventory of your assets and examine your long-term financial objectives

Then sit down with your J.P. Morgan representative and discuss the following questions:

1. Have you ever used or had a trust before? If so, are you pleased with the trustee's handling of your affairs?
2. Does your current estate plan take advantage of the many credits and exemptions available to you?
3. Are your children adequately provided for?
4. Are your affairs in order should you become ill or disabled?
5. Aside from your spouse, do others depend on you for income?
6. Do you wish to apply some of your assets in a special way to benefit your community, your church or your profession?

Your J.P. Morgan representative can help you formulate a plan, whether in the form of a goals-based plan to help you clarify your thinking or by working with your tax and legal advisors to help make sure your plan accurately reflects your wishes

Appendix

What are the most common kinds of personal trusts?

- There are two broad categories of trusts: “inter vivos” or “lifetime” trusts, which are created while you are alive, and testamentary trusts, which are created at your death
  - There are two common types of *lifetime* trusts:
    - A **revocable (“living”) trust** is the most common kind of trust; it generally acts as a combination of a property management vehicle for you while you are alive and an alternative to a Will to distribute assets when you die
    - **Irrevocable** trusts are also common, but serve very different purposes from revocable trusts—when you create an irrevocable trust you are usually making an immediate gift of the assets in the trust to the trust’s beneficiaries
  - **A testamentary trust** is created after your death by the terms of your Will
    - A testamentary trust, because it is formed at your death, provides no lifetime benefits

Revocable Living Trusts

- Established while you are alive, a revocable trust is a legal agreement under which the **trustee** (usually yourself) manages assets for your benefit during your lifetime and then, after your death, for others whom you designate
- Revocable trusts have become popular for many reasons:
  - You can be the trustee of the trust while you are alive and competent, so you do not have to give up control of your assets in order to obtain the benefits of a trust
  - Since there's nothing to probate to the extent your assets are owned in a living trust, upon your death trust assets are free from probate costs
    - In some jurisdictions, the public probate process alone can consume as much as 6% of your estate and take years in court to settle
  - Joint revocable trusts, which are common in community property states, allow straightforward administrative convenience without requiring significantly complicated arrangements for a couple's community property
  - In most cases, you can own your home in your revocable trust and still have a mortgage, qualify for "homestead" benefits (in states that have them) and federal capital gains tax benefits, and generally be treated as if you owned the home yourself
  - You can place just about any type of property in a living trust, and either withdraw or reinvest all of the income generated by trust assets during your lifetime
  - Since a living trust is a private agreement, information concerning its contents remains private
  - Should you become incapable of handling your own personal finances, for example, the living trust can pay your medical bills and living expenses
  - You can modify the terms of a living trust, change beneficiaries or terminate the arrangements as your goals change
  - You can elect to have the trust cease following your death or continue for your beneficiaries
- There are no income or transfer tax advantages to revocable living trusts

Irrevocable Trusts

- Other trusts are generally irrevocable, created either while you are alive or on your death by your Will
- The substantive terms of an irrevocable trust generally cannot be changed, and property generally cannot be removed from the trust
- A properly documented irrevocable trust can save you a substantial amount in state income taxes or estate and inheritance taxes
  - This savings is generally not available with a revocable trust
- Irrevocable trusts can be flexible and can be ideal for a wide range of individuals, including those who have dependents with special needs, are marrying for the second time, or who want to provide effective pre-nuptial protection for their children
- Some specialized irrevocable trusts are described below; many can be created either during your lifetime or upon your death, but some are most effective if created while you are alive

Irrevocable Trusts

Gift Trust

- An irrevocable gift to a trust generally uses either your annual exclusion ($17,000 per donor per donee each year) or a portion of your federal transfer tax exemption ($12,920,000 in 2023), and is available to the beneficiary under the terms set out in the trust
- An irrevocable gift during your lifetime removes both the gifted assets and any growth on them from your balance sheet and from your taxable estate

Life Insurance Trusts

- Life Insurance Trusts (often referred to as "ILITs", which stands for "Irrevocable Life Insurance Trust") keep the proceeds from a life insurance policy out of your taxable estate and provide beneficiaries with the means to pay estate taxes or replenish the assets consumed by taxes
- This can avoid, for example, a distressed sale of a business, farm, real estate or other special assets, and is frequently used where family assets are large and illiquid
- It can also offer long-term estate tax savings for your children and grandchildren, since a properly structured ILIT will also allow the insurance proceeds to escape estate taxation at your spouse's death

Special Needs Trusts

- Special Needs Trusts or Supplemental Needs Trusts are generally established for a specific purpose, such as to meet the varying needs of a disabled child
- Usually, Special Needs Trusts are organized so that the beneficiary continues to qualify for state or federal benefits but can augment those payments if necessary

Irrevocable Trusts (cont'd)

Minor's and Education Trusts

- These trusts are used to make gifts to children or grandchildren without a gift tax
- You may give a minor child up to $17,000 each year without filing a federal gift tax return or paying gift taxes
- These trusts provide significantly more control and flexibility than a conventional custodial account (a Uniform Gift to Minors Account (UGMA) or Uniform Transfer to Minors Account (UTMA))

Charitable Remainder Trusts (CRT)

- CRTs allow you to provide income for yourself or someone else from assets you designate for charity
- You receive an immediate income tax deduction for the charitable portion of the value of your gift to the trust, and you and/or others you designate receive income for life, or for a specified term of years, from the trust
- Ultimately, all property remaining in the trust goes to the designated charity
- If you contribute appreciated, low-yielding property to the trust, which then sells the property and reinvests the proceeds in a diversified portfolio, you can increase your income as well as defer capital gains taxes until you subsequently receive distributions
- The trust's assets are insulated from creditors and are free from federal and state estate taxes and probate
- Many individuals use CRTs as a highly flexible supplemental retirement plan
- Note that CRTs are highly complex and will require sophisticated accounting each year

Irrevocable Trusts (cont'd)

Charitable Lead Trusts

- Charitable Lead Trusts pay income to charities for a set period of time, after which the principal is paid to you or your designated beneficiaries
- Although the trust can provide income tax benefits, it is most frequently used to discount federal estate taxes and generation-skipping taxes

"Credit Shelter" Trusts (also called "Unified Credit" or "Bypass" Trusts)

- A Credit Shelter Trust is used to shelter the federal estate tax exemption from tax at the death of a surviving spouse
  - In 2023, the estate tax exemption is $12,920,000 (indexed for inflation)
  - The estate tax exemption is "portable" between spouses, which means that a trust is no longer essential to shelter the exemption amount
  - Nevertheless, there can be benefits to creating a Credit Shelter Trust rather than relying on the portability law
  - In states with a separate estate tax, Credit Shelter Trusts can help you maximize both federal and state estate tax exemptions
- If you're married with assets of $12,920,000 or more in 2023, a Credit Shelter Trust can ensure that you and your spouse maximize the federal estate tax exemptions available to you; and since the exemption amount is scheduled to be cut in half in 2026, consider whether you should consider this even if your assets aren't currently at that level

QTIP Trust (Qualified Terminable Interest Property Trust)

- QTIP Trusts are particularly useful for individuals with children from a prior marriage
- Assets are given in trust, free of estate taxes, to your surviving spouse for the spouse's exclusive benefit
- Upon the survivor's death, the assets are taxable in his or her estate, and the balance is delivered to the beneficiaries stated in the trust—this is most often used when the first spouse wants to make sure that the assets ultimately go to his or her preferred beneficiaries
- A special kind of QTIP trust, called a "QDOT" (Qualified Domestic Trust), provides the benefits of the federal marital deduction to bequests made to spouses who are not U.S. citizens

A word about trust taxation

- Trusts that pay their own taxes pay based on “compressed” tax brackets

Rate[1]	Trusts and Estates
10%	$0 to $2,900
24%	$2,901 to $10,550
35%	$9,851 to $14,450
37%	over $14,450

[1] The rate applies to taxable income as shown in the table (for 2023)

- Additionally, the Medicare surtax on “net investment income” of 3.8% applies to all trust income over $14,450
- Tax considerations should not determine whether you create a trust, but you should be tax-aware in your planning
- Some lifetime trusts do not pay their own taxes; instead, tax is paid by the grantor of the trust
  - In addition, if a trust makes a distribution to beneficiaries, usually those beneficiaries will pay tax on the income that is distributed at their rates, rather than the trust paying it at its rate
  - Decisions on who pays tax on trust income, and the coordination of trust accounting concepts like “distributable net income” with the concept of “net investment income” are complicated and are best left to your accountant or tax attorney

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