Protective

Estate tax concepts

# Dynasty trust

## The rationale

- Transferring wealth to the next generation can be difficult. Finding a way to leave significant wealth to future family members can be even more difficult. One solution is a dynasty trust.
- The repeal of state laws that limit how long a trust can last makes the dynasty trust possible. Many states have changed their laws to permit a trust that lasts for centuries (or even forever).
- Careful asset management and selective distribution rules ensure that wealth in the dynasty trust will last.
- The grantor who creates the trust ultimately controls how wealth will be distributed to beneficiaries over time.

## Creating the trust

- A dynasty trust is an irrevocable trust. While the grantor may not change the terms of the trust after its creation, a properly appointed "trust protector" may be granted the authority to make changes.
- The laws of the state where the trust is formed govern the trust's formation, administration, duration and termination.
- The purpose of a dynasty trust is to transfer wealth, conservatively manage investments and preserve capital over a long amount of time.
- The selective distribution rules limit a beneficiary's access to trust assets and provide control over trust distributions. These spendthrift provisions also protect assets from creditors (including former spouses).
- Each class of beneficiaries is outlined in the trust document and can include family members yet to be born.
- Choosing a trustee is important. At least one trustee must reside in the state where the trust is located, and one trustee should be a corporate entity for the sake of continuity (due to the long-term nature of the trust).

## Funding the trust

- Grantors often fund dynasty trusts with life insurance or assets expected to appreciate.
- The idea is to transfer assets with low value with the expectation that the value of the assets in the trust will increase over time.

## Tax implications

- The grantor can fund a dynasty trust over time using the gift tax annual exclusion ($19,000 in 2025). Gifts must be of a present interest to qualify for the exclusion. The grantor can satisfy the present interest requirement by granting each beneficiary a Crummey power over the gift.
- The value of assets gifted to the trust above the annual exclusion will be considered a taxable gift, to which the grantor can apply the applicable exclusion amount ($13.99 million in 2025).
- Because the trust is irrevocable, it will not generally be subject to estate tax.

- Because the beneficiaries only have an income interest, trust assets will not be included in any beneficiary's estate, so the trust avoids subsequent estate tax.
- The generation-skipping transfer tax applies because the life of a dynasty trust extends across several generations. Those taxable gifts can be covered using an allocation of the generation-skipping transfer tax lifetime exemption ($13.99 million in 2025).

## In summary

The dynasty trust allows the grantor to:

- Preserve and protect wealth
- Provide financial support for family members and future generations
- Avoid federal estate tax over many generations

# Summary

### What is a dynasty trust?

A dynasty trust is a tool for conserving family wealth through successive generations by minimizing the effect of federal transfer taxes. Many states changed their laws to permit a trust to last for centuries (or even forever). Careful asset management and selective distribution rules can ensure that assets in the dynasty trust will last through the years. The grantor who creates the trust controls how wealth will be distributed to beneficiaries over time.

### How does it work?

A dynasty trust is an irrevocable trust. Its terms, which cannot be changed after trust creation, must conform to state laws concerning trust formation, administration, duration and termination. Selective distribution rules limit a beneficiary's access to trust assets and provide control over distributions. Spendthrift provisions protect assets from creditors (including former spouses). The class of beneficiaries outlined in the trust document includes family members yet to be born.

At least one trustee must be located in the state where the trust is located. Due to the long-term nature of the dynasty trust, one trustee should be a corporate entity for the sake of continuity.

### How is it funded?

Grantors often fund dynasty trusts with life insurance or with assets expected to appreciate. The idea is to transfer assets with low value with the expectation that the value of the assets inside the trust will increase over time.

### How is it taxed?

The grantor can fund the dynasty trust over time using the gift tax annual exclusion. The value of assets gifted to the trust above the annual exclusion will be considered a taxable gift for which the grantor can apply the applicable exclusion amount ($13.99 million in 2025).

The assets in an irrevocable trust are generally not subject to estate tax at the grantor's death. Also, because the beneficiaries only have an income interest, trust assets will not be included in any beneficiary's estate, so the trust avoids subsequent estate tax.

The generation-skipping transfer tax applies because the dynasty trust extends across more than one generation. Those taxable gifts can be covered using an allocation of the generation-skipping transfer tax lifetime exemption ($13.99 million in 2025).