ESLICK FINANCIAL GROUP
How wealth works.

M INTELLIGENCE

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Eslick Financial Group, Inc. provides sophisticated insurance and wealth management services to families, business owners, corporate executives, professionals, and other successful high income and high net worth individuals. Our team of professionals utilizes a customized process of defining, understanding, researching, evaluating, and informing our clients of innovative and uniquely integrated solutions tailored to their diverse financial goals. Our desire is to help make the otherwise complex, more understandable as it applies to your unique situation.

Understanding the Generation Skipping Transfer Tax

What is the Generation Skipping Transfer Tax?

Federal gift and estate tax laws apply to transfers of wealth. When a transfer bypasses a generation in favor of a subsequent generation (e.g., from grandparents to grandchildren), such transfers are subject to an additional Generation Skipping Transfer (GST) tax.

The intent of the GST tax is to capture the two layers of transfer taxes that would have been incurred had the original gift been passed from the first generation to the second, and then from the second to the third.

GSTs are taxed at a flat tax rate equal to the top federal estate and gift tax rate. GST taxes are applied in addition to any federal estate or gift taxes.

When does the GST Tax apply?

The GST tax is applied when wealth is transferred to a "skip person." The IRS defines a skip person as a transferee who is two or more generations younger than the transferor. This generational difference is measured as either:

- A family relationship (e.g., a transfer from a grandparent to a grandchild) OR
- A transfer between unrelated individuals who are more than 37½ years apart in age

Transfers Made in a Trust

For transfers made in a trust, GST tax is triggered when all the beneficiaries are skip persons or when distributions can only be made to skip person beneficiaries.

Exceptions to the GST Tax

Not all transfers to a skip person are subject to the GST tax. For example, under Internal Revenue Code Section 2503, certain transfers made for qualified medical or tuition expenses may be exempt from taxation. A qualified tax advisor can determine if a particular transfer will be subject to GST tax.

The GST Annual Exclusion

Taxpayers receive a federal gift tax exclusion each year (currently $14,000 per donee, per year, in 2015). Some transfers that qualify for the gift tax exclusion may also qualify for a GST annual exclusion (also $14,000 in 2015).

Gifts made directly to a skip person are eligible for both the annual gift tax and the annual GST tax exclusion.

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Gifts made in a trust may qualify for the annual gift tax exclusion if they are gifts of present interest (e.g., "Crummey" Gifts). However, these gifts will only qualify for the annual GST tax exclusion if:

- The trust benefits only the skip person AND
- The trust is written in such a way that assets benefitting the skip person are included in the skip person's estate

The Lifetime GST Exemption

In addition to any annual GST tax exclusions the taxpayer may qualify for, each U.S. citizen has a lifetime GST exemption (currently $5.43M in 2015, indexed annually for inflation) that may be used to shelter transfers to a skip person from the GST tax.

When a gift is made directly to a skip person, the exemption is automatically applied. When a gift is made in a trust, the taxpayer must make an affirmative election to allocate the GST exemption on a gift tax return (IRS form 709). Assuming the gift is fully covered by the exemption, the intent is often to make the entire trust an "exempt trust," so that the initial gift and all future asset growth passes free of the GST to the junior generations.

Use of the GST Exemption with an Irrevocable Life Insurance Trust

An irrevocable life insurance trust that benefits multiple generations is perhaps the most effective use of the GST exemption. With the assistance of a qualified attorney and planning team, a trust can be established and funded with a GST exemption allocation made to shelter the funds from GST tax. The trustee may then use these funds to acquire one or more life insurance policies, with the trust named as the beneficiary for the proceeds.

With proper planning from an experienced life insurance professional, the death benefits from the insurance may be significantly higher than the total premiums paid and may benefit multiple generations, thereby maximizing the use of the GST exemption.

For More Information

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