GENERATION-SKIPPING IRREVOCABLE TRUST FOR BENEFIT OF GRANTOR'S CHILDREN AND OTHER DESCENDANTS

(Funding: Assets Other than Life Insurance)

HIGHLIGHTS OF THE PLAN

This specimen generation-skipping irrevocable trust is designed to hold and manage property for the benefit of the grantor's children and other descendants throughout their lives. Trust assets can be used to provide for education and medical expenses, support and maintenance expenses, money for home purchases, funding for starting or operating a business, or other family needs. The trust can operate very much like a family bank.

The trust should be used in circumstances where:

1. The grantor's children are to be the direct beneficiaries of the trust. (If the grantor is married, his or her spouse does not participate in the trust.)

2. After the death of the grantor, the trust assets are to be held, managed, and administered as a separate generation-skipping trust estate, for the benefit and use of the grantor's children and descendants.

The incentive for use of an irrevocable trust, such as the specimen generation-skipping trust document, is the potential for removing the growth on trust assets from the estate of both the grantor and the grantor's spouse. In order to help accomplish this, it is recommended that the trust be funded with assets that will grow in value. Trustees will also keep a bank account in which to deposit monetary contributions from the grantor and invest the money in accordance with the terms of the trust.

The specimen trust form contemplates that the trust will have taxable income during the grantor's lifetime. The specimen trust contains a provision that permits the grantor to substitute assets of equal value for other assets of the trust. Under IRC Section 675(4)(c), such a power to substitute assets would cause the grantor to be taxed on trust income, thus creating a "defective" trust for income tax purposes. However, such a power would not cause the assets to be includible in the grantor's estate for transfer tax purposes. The purpose of such a provision is to use the grantor's money to pay taxes for the trust without having to pay a transfer tax on the funds used for that purpose. This technique has the effect of transferring additional funds to the trust without paying a transfer tax on the funds. If desired, the trust may be drafted without this provision and still be valid for all other purposes.

Although the specimen trust form does not contemplate that life insurance will be purchased by the trust, the document incorporates Crummey withdrawal provisions in order to qualify contributions to the trust for the gift tax annual exclusion. It is important to note that the specimen trust form utilizes Crummey withdrawal provisions to provide a gift tax exclusion under Internal Revenue Code Section 2503(b) up to the $5,000 or 5% lapse protection amount under IRC Sections 2514(e) and 2041(b)(2).

By limiting the Crummey power to the lapse protected amount, the beneficiaries will not become grantors of the trust for transfer or income tax purposes, thus avoiding certain transfer and income tax problems for the beneficiaries. If the trust were to allow beneficiaries with Crummey withdrawal powers to make withdrawals equal to the full gift tax annual exclusion, the power could cause gift, estate, and generation-skipping tax issues for the beneficiaries. There are other methods of drafting Crummey withdrawal powers, and grantor's counsel should be consulted in all cases regarding withdrawal provisions.

The specimen trust illustrates just one method of providing for the grantor's children; however, the trust provisions must be designed to fit the individual circumstances of each case.