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IDGTs:

A Versatile Estate Planning Tool

Irrevocable trusts are great tools for estate planning. They can help grantors reduce the size of their taxable estate, protect assets from creditors and lawsuits and control when and how their wealth passes to beneficiaries.

One popular type of irrevocable trust is the intentionally defective grantor trust (IDGT). IDGTs are especially attractive for many individuals because they not only allow the grantor to make completed gifts, but also potentially go even further in reducing the size of their taxable estates. In the IDGT strategy, the grantor, not the trust, pays the income taxes on the trust's income. That can help continue to reduce the grantor's taxable estate without further estate and gift tax consequences.

A Helpful "Defect"

To understand IDGTs' flexibility, you need to understand their "defect." Trusts in which assets appreciate often must pay the associated income taxes from trust funds. But an IDGT's trust document contains language requiring that the grantor, not the trust, pay those taxes. The grantor's responsibility to pay the trust's income taxes enables the grantor to maintain a degree of control and flexibility over the IDGT while still removing assets from their taxable estate.

The Power of Swaps

IDGTs have another attractive feature as well: Grantors may swap assets with the trust in a strategy that can help minimize future capital gains tax liabilities. Typically, the grantor will fund the trust with assets that are expected to highly appreciate. Later, those highly appreciated assets, which are subject to capital gains tax upon distribution, will be removed and replaced with cash or other low-cost-basis assets. If the grantor then retains the highly appreciated assets in their name until death, those assets will receive a step-up in tax basis to fair market value as of the date of death. This reduces the capital gains tax due when those assets are eventually sold.

When Paying the Taxes Is a Good Investment

The requirement to pay income taxes for an IDGT might seem like a burden to the grantor, but it can be well worth it. Allowing the trust assets to grow tax free can also enable their value to compound more rapidly, maximizing what the trust's beneficiaries will eventually receive. For example, hypothetical trust assets that start at $10 million, earn 7% a year and each year pay the top federal income tax rate of 37% would appreciate to nearly $38 million over 30 years. Without that tax burden, those assets would total $76 million*.

Why to Consider an IDGT (or Other Strategies) Now

The federal estate and gift tax exemption stands at a historically high $13.61 million per person, or $27.22 million per married couple, but it's set to expire on Dec. 31, 2025.[1] Unless Congress extends those exemption amounts, they will revert to $5 million per person, adjusted for inflation, starting in 2026. Consequently, it may make sense to fund an IDGT or other trust type before that time to maximize your lifetime exemption. It's true that transfers into trusts above the current estate and gift tax exemption are subject to federal estate tax. But potential asset appreciation over the years could exceed that tax bill.

YOUR WEALTH ADVISOR CAN HELP

Intentionally defective grantor trusts are just one tool in the estate planning toolbox. Your wealth advisor and team can work with our in-house trust professionals to help you decide whether using an IDGT is the best strategy for achieving your goals.

For more information visit: **mariner.com**

Source:

[1]"IRS provides tax inflation adjustments for tax year 2024"

*This hypothetical example is for illustrative purposes only and is not intended to be representative of actual results or any specific investment, which will fluctuate in value. The determinations made by this example are not guarantees and no investment fees or expenses are included in the calculations, which would reduce the figures shown. Please keep in mind that it is possible to lose money by investing, and actual results will vary.

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