WealthTRUST OKLAHOMA

A trust representative office of National Advisors Trust Company, FSB

Monthly Update for Administration of Trusts From a Trust Administrator's Perspective.

It is our hope that our Monthly Update will be helpful to you and your clients to better understand the administration of trusts from a Trustee's viewpoint

February, 2016

A FOLLOW-UP TO LAST MONTH'S NEWSLETTER

Last month's newsletter explained how well-intentioned gifting can cause very bad results.

This newsletter is to briefly mention a couple of other examples of how wholesale gifting is rarely the best choice someone can make in implementing their "estate plan".

UNEXPECTED INCOME TAX CONSEQUENCES

There is a very interesting scenario that I bet most of you have never thought of. You would be stunned to know how many times people will gift all of their cash and investments to an adult child, (resulting in the adult child being the sole owner of all of the money and investments), with the "understanding" that the adult child will use the money to pay all of the parent's living expenses.

Because the cash and investments would be taxed under the adult child's social security number, along with the adult child's own income from his or her employment, it almost always results in pushing the adult child into a higher tax bracket. That means that the parent's "former" money and investments are taxed at a higher rate than what would have been taxed to the parent if the parent still owned the cash and investments. This results in a decrease in net annual income, and can lead to having to dip into principal to have to pay for the parent's living expenses, when it might have been possible to avoid spending principal if the cash and investments were still being taxed at the parent's lower income tax bracket.

THE UNMENTIONABLE

The above example contemplates the parent gifting an adult child all of the parent's cash and investments with the understanding that the adult child will pay all of the parent's living expenses. What about the "unmentionable"? We all know what that is. "What if" after the parent makes the gift, the adult child has a change of heart and is not willing to use that money for the parent's living expenses? While you may not believe that ever happens, trust me, it does. Having been in the trust administration business for over 20 years, I have seen everything more than once.

LOSS OF "STEPPED UP" BASIS

Here is another reason why wholesale gifting of assets can have an adverse tax consequence.

When a parent changes ownership of an investment from the parent to the child, (child is the sole owner and not named as a co-owner in JTWROS), and that investment appreciates or increases in value, then for capital gains tax treatment, the adult child will lose the benefit of using a "stepped-up" basis if and when the adult child later sells that asset.

If ownership of the investment changes to the adult child as a result of the parent's death, and not by way of an outright gift during the parent's lifetime, then when the adult child sells the asset, the tax cost basis that the adult child could use would be the value of the asset at the time of the parent's death, instead of using the parent's tax cost basis, which could be (and most likely is) dramatically less than the value at the time of the death.

ONE LAST "WHAT IF"

What if the parent gifts the adult child cash, investments, etc., and that adult child has, or develops, creditor problems? Keep in mind that if the adult child is an owner of the asset, it will most likely might make that asset subject to the adult child's creditor attempting to garnish funds, investments, etc., to pay the amount owing the creditor. So you have to ask yourself, "did you really intend to put the assets at risk of loss"?

UNINTENDED RESULTS

These are just some more of the unintended results that can happen by a parent making wholesale gifts to adult children without first considering the potential or possible negative repercussions.

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***WealthTrust Oklahoma** is the Oklahoma Trust representative office of National Advisors Trust Company, FSB, which currently has more than $9 billion under administration. We hold a federal charter and are independent.*

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