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You Can Create Your Own Dynasty With a Multigenerational Trust

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How rich would you like to make your grandchildren? Or perhaps your great-grandchildren? Want to leave them \$50 million tax free? \$100 million? More? At a cost of less than one percent of that amount?

These are questions many estate planners are asking their clients these days, since it is possible and sometimes advisable to establish a trust which accomplishes just that. Such a trust is commonly called a “Dynasty” trust or “Megatrust” because its general objective is to accumulate huge amounts of wealth over several generations - just like the rich used to do it.

In the typical family estate plan (or as some put it, “non-plan”), one spouse leaves everything to the other, then the survivor leaves it all to the children, and then the children repeat that pattern. While this arrangement may appear to be the natural order of things, from an estate tax standpoint it is somewhat of a disaster where the initial estate exceeds \$600,000. And the further it gets over \$600,000, the greater the estate tax bite, and the worse the disaster. This is because the assets are first taxed in the surviving parent’s estate, then in the child’s estate, then in the grandchild’s estate, and then the great-grandchild’s estate, and so on, and so on.

The Dynasty trust is designed so that little or no tax is paid when it is established, and then no further estate taxes are paid for a hundred years or more. In the meanwhile, the funds in the trust can provide educational, support, or other benefits to children, grandchildren, great-grandchildren, etc. When you consider that the lowest effective estate tax rate is 37 percent and the highest 60 percent, it is easy to see how valuable it can be to avoid estate taxes over such a long period of time. Generally speaking, Dynasty trusts are not for families with estates of \$600,000 or less, and perhaps not even for estates marginally over \$600,000. In fact, they are most often used by families with estates over \$1,200,000, and families with estates of a couple million or more may be missing the boat if they don't have one.

There is little, if any disadvantage to such a trust, while the advantages are numerous. In addition to by-passing the taxable estates of your lineal descendants (though the beneficiaries can be anyone you chose), funds in the Dynasty trust can be impervious to creditors of beneficiaries and unreachable by divorcing spouses, while avoiding probate and legal entanglements in descendants' estates, and all the while providing benefits to those descendants.

The extent of such benefits provided by your Dynasty trust can be as broad or as narrow as you choose, or you can simply give the trustee "discretionary" powers to make distributions according to some standards or guidelines. Although this type of trust must be irrevocable (one that you cannot change), it is quite possible, if not advisable, to structure the trust so that changes can be made in the future by someone else (one or more persons you name or by other mechanisms) to accommodate future changes in the laws or in family or societal circumstances.

Although the Dynasty trust can be created on your death, most estate planners agree it is much better to establish it while you are alive (a Dynasty "living" trust), to the extent you can afford it. Since everyone is allowed to make lifetime gifts of up to \$600,000 without paying a gift tax (this is over and above the \$10,000 per donee per year tax free amount), the typical Dynasty trust is funded with a one-time gift of \$600,000 in cash, securities, real estate, or other property. In fact, wealthy families will place even more into such a trust, up to a total of \$1 million, to take advantage of what is called the generation skipping tax (GST) exemption. This is the largest amount one individual can place in a trust for grandchildren (or other younger beneficiaries)

without paying a special (generation skipping) tax. A gift of \$1 million to a Dynasty trust will generate a gift tax of about \$153,000, paid by the donor.

Once you get past the complexities and decide you can afford to do it, the numbers can be staggering. A Dynasty trust funded with \$600,000 and accumulating only 5 percent per year compounded after taxes will grow to almost \$7 million in 50 years, and about \$78 million in 100 years. Increase the initial funding to \$1 million and the amounts change to \$11 million and \$131 million respectively. Enough to make your descendants remember you fondly.

But why 100 years? Why not longer? Because in most states (all but three), there is a limit to the duration of a non-charitable trust. So if you start one now, somewhere around the year 2095, your Dynasty trust must terminate and the remaining funds distributed to the then living beneficiaries, who can then start their own Dynasty trusts, if money is still of any value.

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