

The time for action is NOW.

The \$5 Million Tax Break...

And How to Use It to Transfer Wealth to Loved Ones While Helping UT



In December 2010, Congress amended the federal gift and estate tax law regarding gifts to loved ones made in 2011 and 2012. The new law gives each taxpayer the right to pass up to \$5 million to loved ones before January 1, 2013, without owing a cent in federal gift tax. At \$5 million per individual (\$10 million per couple), this is five times the previous limit and represents the largest gift-tax exemption since before World War I.

While carefully considering any such once-in-a-lifetime, irrevocable decision, you may be interested to know that you can use all or part of the \$5 million exemption to create a charitable trust now that will make annual distributions to what you love at UT Austin for a number of years — and then pass significantly more than \$5 million to your loved ones in the future. The **charitable lead trust** has been part of the tax code since 1969, but now may be the perfect time to create and fund such a trust thanks to low interest rates and the large amount that can be passed to loved ones tax-free. For illustration purposes, let's consider several hypothetical situations.

A charitable lead trust that supports UT and then benefits children

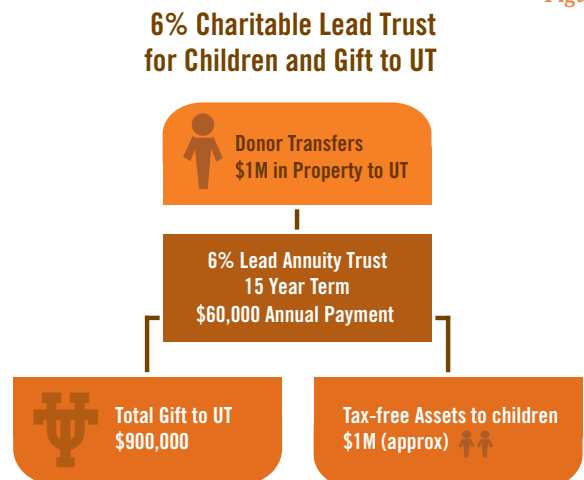
Tom would like to make a significant gift to UT Austin. He also wants to pass as much as possible to his children, free of gift and estate taxes. He creates a charitable lead trust lasting 15 years (can be any number of years) and funds it with \$1 million (there is no minimum or maximum amount) in cash or publicly traded securities. Each year, the trust distributes \$60,000 (can be any amount) to UT Austin to be used as directed in the trust document. At the end of the 15 years, his children named in the trust document receive the trust assets, which could be worth more or less than the original \$1 million. (See figure 1.)

Tom is actually making two gifts when he funds the trust with \$1 million: (1) the annual distribution to UT for 15 years, and (2) the gift to his children to receive the trust assets after 15 years. At the time the trust is funded, the economic value of the distributions to UT — \$900,000 over 15 years — is \$715,000. There is no gift tax on this amount because these are charitable distributions. The economic value of his children's right to receive the trust assets is \$285,000. So Tom only uses \$285,000 of the \$5 million he can pass gift-tax-free in 2011 or 2012 even though his children will receive more or less than \$1 million after 15 years. And there will never be any additional gift or estate tax when the trust assets are distributed to his children, even if the assets are worth much more than \$1 million.

If Tom were willing to allocate \$2 million of his increased gifting ability to a charitable lead trust now,

he could fund it with \$7 million without owing any gift or estate tax, either when the trust was funded or when the trust ends. If UT received 6 percent of \$7 million, or \$420,000 each year, a total of \$6.3 million would support what Tom chooses. The economic value of the distributions to UT is \$5.005 million and is

Figure 1



exempt from federal gift and estate taxes. The economic value of his children's right to receive the trust assets is \$1.995 million, less than the amount he can give away before the end of 2012 gift and estate-tax-free.

A charitable lead trust that supports UT and then benefits grandchildren

Juan and Ramona want to make a significant gift to UT Austin and want to pass as much as possible to their grandchildren, free of estate tax and transfer tax. They create a charitable lead trust lasting 20 years and fund it with \$1 million of cash or publicly traded securities. Each January the trust distributes 5 percent of the value of trust assets to UT to be used as directed in the trust document. At the end of 20 years the grandchildren named in the trust document receive the trust assets, which could be worth more or less than the original \$1 million.

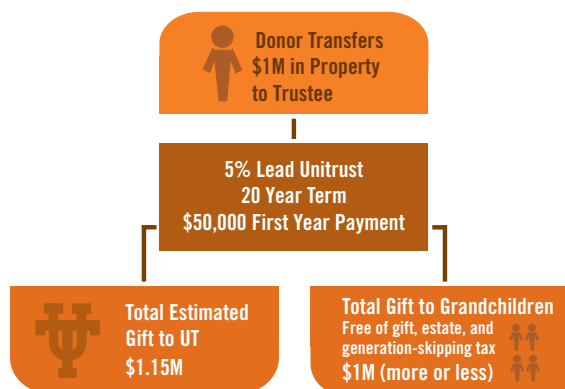
The new law gives each taxpayer the right to pass up to \$5 million to loved ones before January 1, 2013, without owing a cent in federal gift tax.

Juan and Ramona are actually making two gifts when they fund the trust with \$1 million: (1) the annual distribution to UT for 20 years, and (2) the gift to their grandchildren to receive the trust assets after 20 years. If the trust earns a 6 percent total annual return net of trustee fees, then UT would receive about \$1.15 million over 20 years. The economic value of the distributions to UT is \$630,000 when the trust is funded. There is no gift tax on this amount because these are charitable distributions. The economic value

of the trust ends. UT would receive about \$6.2 million over 20 years. The economic value of the distributions to UT is \$3.4 million and is exempt from federal gift and estate taxes. The economic value of their grandchildren's right to receive the trust assets is \$1.99 million, less than what they can give away before the end of 2012 free of gift, estate, and generation-skipping transfer taxes.

Figure 2

5% Charitable Lead Trust to Grandchildren and Gift to UT



A final word

As these illustrations indicate, you don't have to choose between providing for your loved ones and supporting the University – you can do both. UT's Gift Planning team can help you support your passion and create the kind of gift you've always wanted to make. Trusts can be created for any number of years or for the duration of your lifetime. And the amount distributed annually to the University can be either a fixed dollar amount or a fixed percentage of the value of the trust assets, revalued annually. Your Gift Planning team liaison will work closely with your professional advisers, and there is never any cost or obligation to use the educational services the team provides.

THE UNIVERSITY OF TEXAS AT AUSTIN

University Development Office

Gift and Estate Planning Team

P.O. Box 7458, Austin, Texas 78713-7458

Phone: 512-475-9632 Toll-free: 866-4UTEXAS(866-488-3927)

Fax: 512-471-3439

Website: giving.utexas.edu/giftplanning/

Email: giftplan@www.utexas.edu

IRS Circular 230 Notice: The University of Texas at Austin does not provide legal, tax, or financial advice. Consequently we urge you to seek the advice of your own legal, tax, or financial professionals in connection with gift and planning matters. This communication (including any attachments) is not intended to be used and cannot be used for the purpose of avoiding tax-related penalties.



of the right to receive the trust assets is \$370,000, even though the grandchildren will receive more or less than \$1 million. (See figure 2.)

They use only \$370,000 of the \$10 million they can pass tax-free in 2011 or 2012. And there will never be any additional gift, estate or generation-skipping transfer tax when the trust assets are distributed to their grandchildren after 20 years, even if the assets are worth much more than \$1 million.

If they were willing to allocate \$2 million of their increased gifting ability to an enhanced inheritance trust now, they could fund such a trust with \$5.4 million without owing any gift, estate, or generation-skipping transfer tax, either when the trust was funded or when