

## Dynasty Trust

CREATING A MULTI-GENERATIONAL LEGACY  
USING LIFE INSURANCE



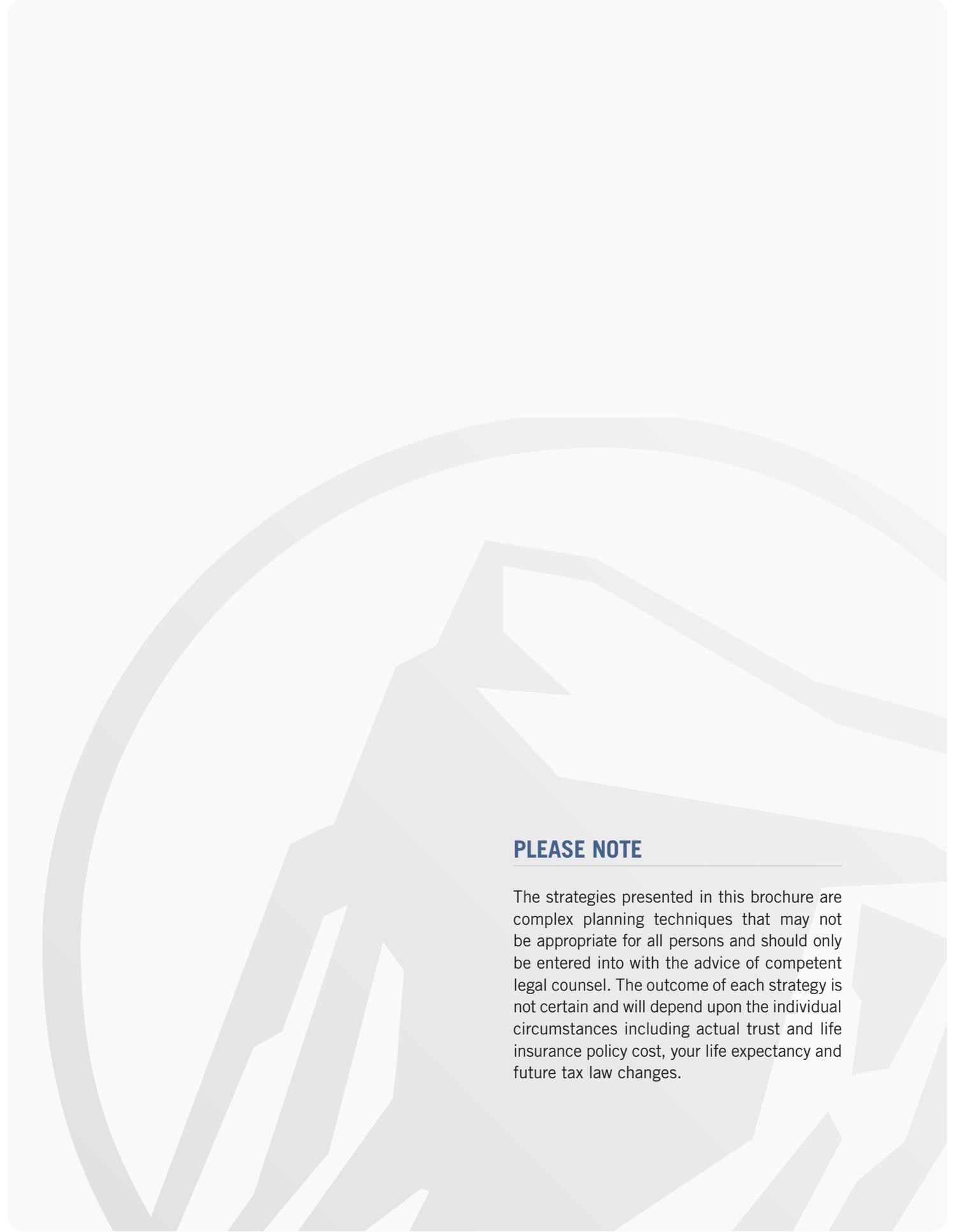
# Life Insurance



**Prudential**  
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The Prudential Insurance Company of America, Newark, NJ.

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## PLEASE NOTE

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The strategies presented in this brochure are complex planning techniques that may not be appropriate for all persons and should only be entered into with the advice of competent legal counsel. The outcome of each strategy is not certain and will depend upon the individual circumstances including actual trust and life insurance policy cost, your life expectancy and future tax law changes.

# The Dynasty Trust

There are many estate planning approaches that can help you to pass on your monetary wealth. But if you are also interested in passing on your traditions, values, and the other components that make up your real wealth, consider a Dynasty Trust strategy. In addition to helping you leave a legacy that includes both your monetary and non-monetary values, it can be designed to last into perpetuity.

## KNOWING IF THIS STRATEGY IS RIGHT FOR YOU

You have several options available to you for passing along your wealth. Certain factors can help you determine whether to consider the strategy presented here.

**This gifting strategy may benefit you and your family if you:**

- Have a net worth of \$7 million or more
- Are family oriented
- Have a conservative lifestyle
- Are involved in your community or have a favorite charity
- Have estate or income tax concerns

### REALITY CHECK

Family wealth rarely survives for long.

Typically

**70%** evaporates by the end of the second generation. By the end of the third?

**90%**<sup>1</sup> of the wealth is gone.

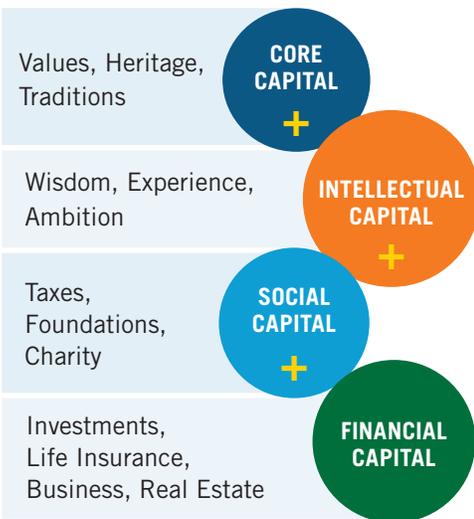


<sup>1</sup> “Lost Inheritance. Studies show Americans blow through family fortunes at a remarkable rate.” by Missy Sullivan. Wall Street Journal. March 8, 2013.



# Creating a Dynasty Trust

## YOUR REAL WEALTH...



To create a Dynasty Trust, you give or bequeath your assets to the trust to benefit your heirs. (You can also sell assets to the trust.) Your spouse, descendants, or even charities can be designated to receive income or borrow money from the trust.

By allocating your Generation-Skipping Transfer Tax (GSTT) exemption to gifts or bequests, you can help reduce future transfer taxes on the trust assets when beneficiaries die.

## PASS ON YOUR REAL WEALTH

While a Dynasty Trust is primarily designed to provide potential tax benefits, it can also help you to pass on your real wealth. By making distribution provisions discretionary, you can attach “strings” to the income. Therefore, you could instruct trustees to provide income only to those heirs who adhere to your values. These controls established by you and your attorney can help you pass on not just your financial capital, but also the core, intellectual, and social capital that made you successful.

For example, beneficiaries may be required to:

- Meet certain academic standards
- Be employed
- Perform public service
- Avoid substance abuse
- Show family unity

## ENHANCE FAMILY WEALTH

A Dynasty Trust could also be a low-interest and less onerous alternative to commercial lenders for your heirs. In addition to benefiting family members, the income generated could help to grow the trust’s value. For example, loans could be provided to beneficiaries to help:

- Pay for graduate school
- Buy a home
- Start a business

Lastly, the trustee can purchase life insurance on your and/or your spouse’s life to help fund the capital needs of the trust at your death and to provide liquidity to your estate for estate tax and other wealth transfer costs. The trust can even own life insurance on the lives of the trust beneficiaries. At the beneficiary’s death, the trust receives new capital to help fund those beneficiaries’ transfer costs and further preserve wealth for the next generation.

Two key considerations to note with Dynasty Trusts are the **Rule Against Perpetuities** and the **GSTT**.

## RULE AGAINST PERPETUITIES

The Rule Against Perpetuities is a complex rule designed to prevent trusts from lasting forever. However, a number of states have abolished or significantly modified the rule, including AK, AZ, CO, DE\*, DC, FL, ID\*, IL, ME, MD, MI\*, MO, NE, NH, NV, NJ, NC, OH, PA, RI, SD, TN, UT, VA\*, WA, WI, and WY. WY and UT have limited the duration of trusts to 1,000 years, FL and TN have limited it to 360 years, NV is 365 years and WA 150 years.

*\*Repealed with respect to personal property*

## GENERATION-SKIPPING TRANSFER TAX

The GSTT is levied on property transfers to persons two or more generations younger than the transferor. The tax compensates the Treasury for transfers that “skip” estate taxation at the intermediate generation (i.e. 2nd generation) level. The GSTT is equal to the highest marginal estate tax rate at the time of the transfer. GSTT annual exclusion rules differ from those for present interest gifts for gifts made in trust.

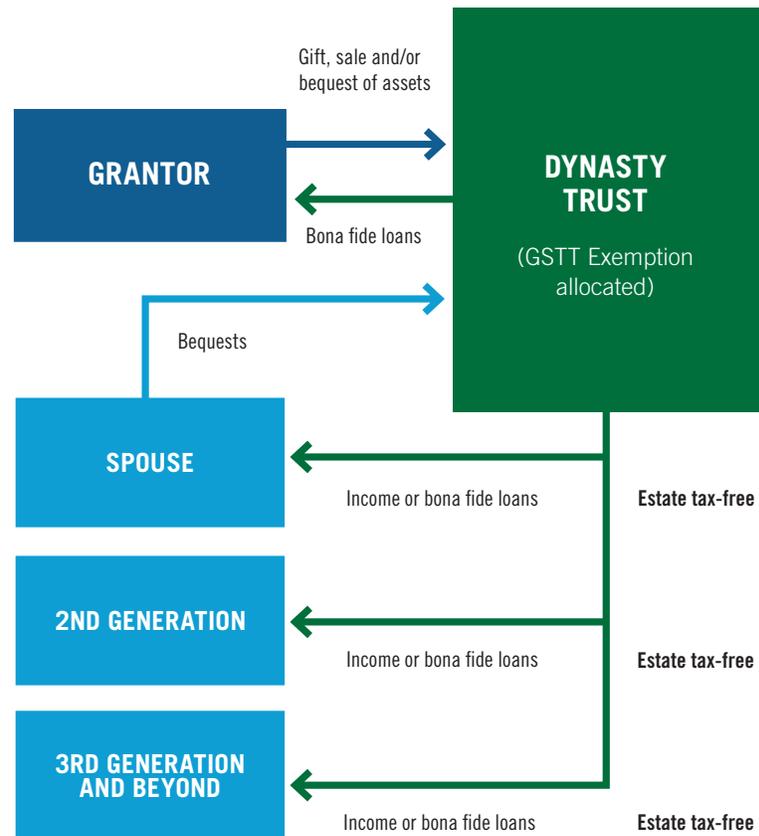
A generation skipping transfer can occur in one of three ways:

- 1 A transfer made directly to a skip person** (i.e., grandchild), either during lifetime or at death, is a direct skip. A transfer made to a trust in which all beneficiaries are skip persons is also a direct skip.
- 2 A taxable distribution** occurs when trust distributions are made to beneficiaries who are skip persons. If the trust terminates and distributes assets to skip persons, those assets are taxable distributions subject to GSTT rules.
- 3 A taxable termination** occurs when a trust loses its last non-skip person and only skip persons remain as beneficiaries. As long as the trust maintains a non-skip person beneficiary a taxable termination will not occur, but at the death of the last non-skip person, the value of the interests passing to the skip beneficiaries is taxable.

The initial transfer(s) to the Dynasty Trust are limited by the transferor's lifetime gift and GSTT exemption. Lifetime gifts to the Dynasty Trust will reduce the transferor's gift, estate, and GSTT exemptions on a dollar-for-dollar basis. For tax year 2014, the estate, gift and GSTT exemptions are \$5.34 million, respectively. This amount is indexed annually for inflation.

## DYNASTY TRUST

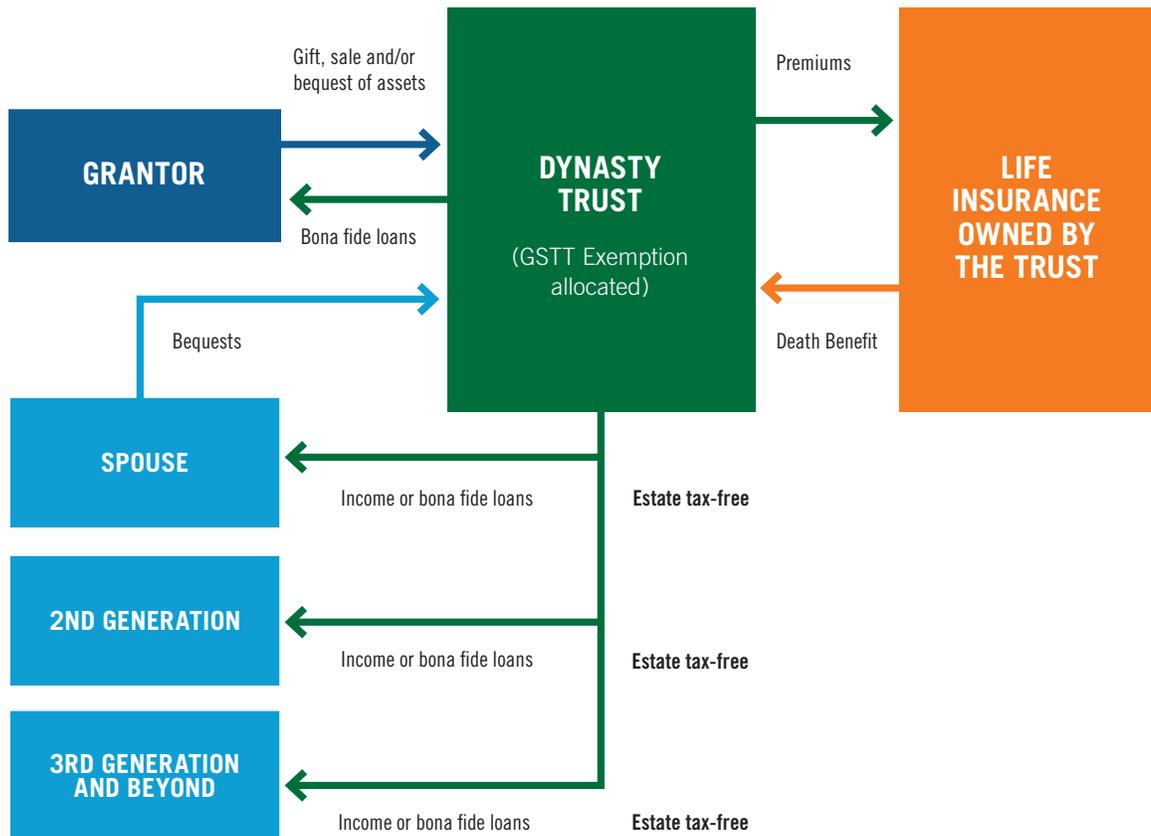
This chart shows the design of a Dynasty Trust. As you can see, the Grantor and Spouse fund the trust to benefit each subsequent generation.



- Irrevocable trust that can be designed to last into perpetuity to which you, as grantor, can gift, sell or bequest valuable assets.
- Your GSTT Exemption can be allocated to help reduce estate taxes and other transfer costs among trust beneficiaries.
- Your spouse can be an income beneficiary and/or receive indirect access to trust assets via the trustee. He or she can also bequeath assets at death to the trust.
- Distributions can be structured as discretionary and based on incentives (i.e. “strings attached”).
- Can provide cheap source of capital and/or bonus income to trust beneficiaries who follow your rules and adhere to your values.
- Can help you pass down non-monetary wealth (i.e. core and intellectual capital) such as your values, traditions, responsibility, ambition and work ethic.
- Can help protect wealth from mismanagement, divorce, financial creditors and estate taxes among trust beneficiaries.

*There may be federal and/or state gift tax consequences with the funding of a Dynasty Trust and the gifts necessary to pay the premiums may reduce the size of the estate and/or the amount of lifetime gift tax exemption and/or estate tax exemption amount. Additionally, Dynasty Trusts may restrict the beneficiaries' rights to access trust principal.*

This chart shows how a life insurance policy can help to enhance the value of a Dynasty Trust. As you can see, trust assets are used to purchase a life insurance policy on the life of the Grantor (and potentially the spouse and beneficiaries). The death benefit provided by the life insurance policy adds to the value of the trust.



- The trustee can purchase life insurance on the grantor, the grantor's spouse and potentially some trust beneficiaries (if there is an insurable interest), and/or invest the gifted amounts to help enhance the ultimate value received by current and future beneficiaries.

**Life insurance owned by the trust could have a number of potential benefits:**

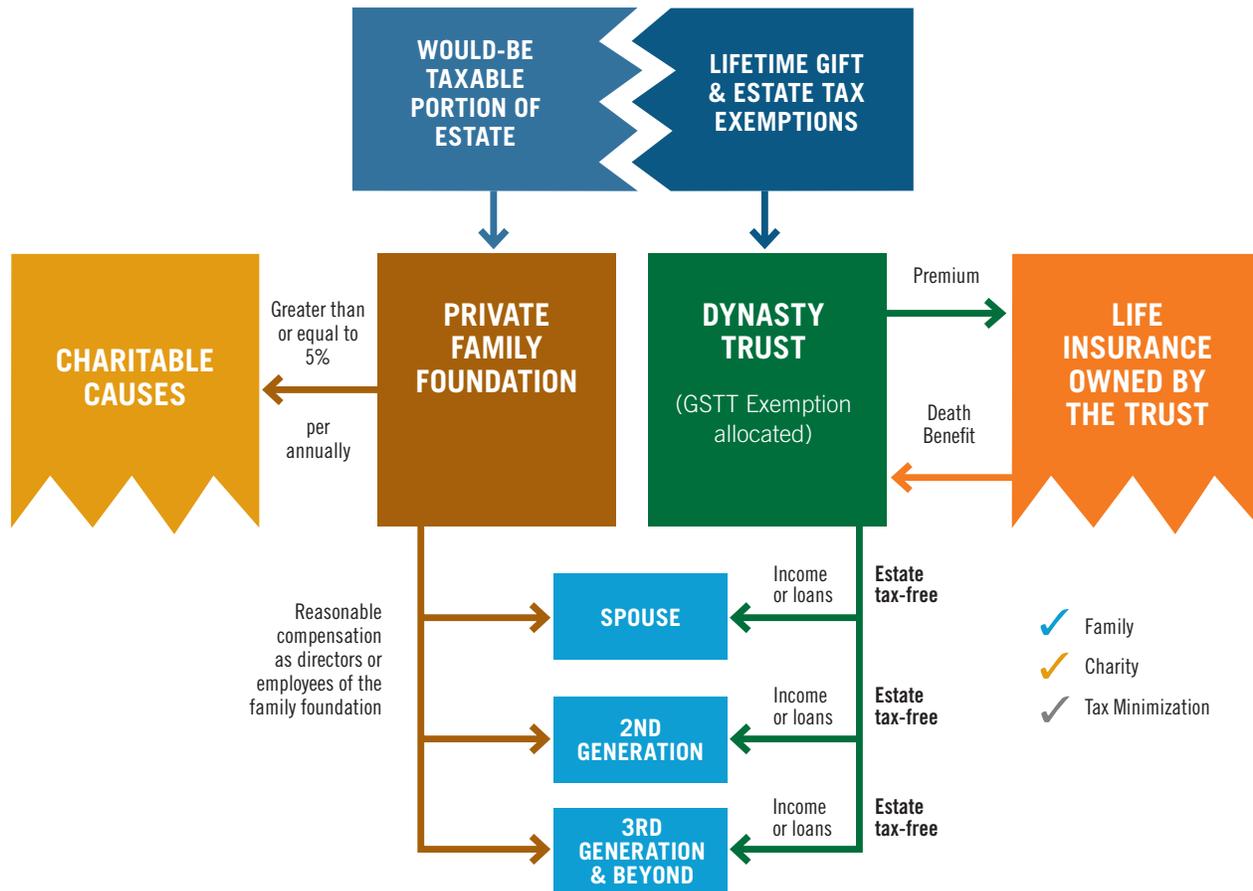
- Can provide for your beneficiaries after your lifetime
- Immediate leverage at death for your beneficiaries and liquidity to help fund the trust
- Death benefit generally received income tax free
- Potential for high internal rate of return in the event of a premature death
- Can be guaranteed which can help establish an element of predictability regarding the capital ultimately received by the trust.
- Can help remove volatility from wealth transfer and balance out volatility in other estate assets at death
- Can help provide liquidity for estate taxes of the 1st generation as well as for trust beneficiaries if the trustee purchases policies on them as well.

*Life Insurance contains fees and expenses, including cost of insurance, administrative fees, premium loads, surrender charges and other charges or fees that will impact policy values.*

*Guarantees and benefits within the policy are based on the claims paying ability of the issuing company.*

## DYNASTY TRUST

This chart shows how a Dynasty Trust in combination with a philanthropic strategy can potentially eliminate estate taxes. As you can see, the taxable portion of the estate is passed to a non-profit Private Family Foundation. The assets in the Family Foundation are used to benefit charitable organizations and to pay family members that work for the foundation.



- The strategy can be employed in conjunction with philanthropic strategies, such as a Private Family Foundation, to help reduce estate taxes and give you and your family the ability to allocate your social capital to causes that are consistent with your values. It can also unite family members in charitable decision making from generation to generation instilling in your family a sense of excitement about supporting specific social and charitable causes.
- The would-be taxable portion of your estate can be directed to the Foundation estate tax free with the amounts equal to your lifetime gift and estate tax exemptions passing to the Dynasty Trust. This approach could help preserve wealth by allowing your family to minimize taxes by choosing to distribute to charity.
- Additionally, a foundation can provide a few incidental benefits to your family including being paid reasonable compensation as employees or directors and recognition in the community which could be particularly beneficial if you desire to perpetuate your name after your lifetime. There could also be opportunities for employee-family members who own or manage a separate, for-profit business by attracting recognition among the community's more prominent figures through fund-raising activities.

*There may be federal and/or state gift tax consequences with the funding of a Dynasty Trust and the gifts necessary to pay the premiums may reduce the size of the estate and/or the amount of lifetime gift tax exemption and/or estate tax exemption amount. Additionally, Dynasty Trusts may restrict the beneficiaries' rights to access trust principal.*

# Important Considerations For This Strategy

## DYNASTY TRUSTS

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- Restricts beneficiaries' access to trust principal.
- If made a grantor trust for income tax purposes, more wealth may grow inside the trust.
- After the grantor's death, though, any distributable net income retained by the trust will be subject to trust income tax rates which increase to the maximum 39.6% rate more quickly than for individuals. The 3.8% net investment income tax also applies to trusts if the trust's adjusted gross income for the year exceeds the dollar amount at which the highest tax bracket begins.

## LIFE INSURANCE

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- Contains fees and expenses, including cost of insurance, administrative fees, premium loads, surrender charges and other charges or fees that will impact policy values.
- Death benefit proceeds are not paid to the trust until the insured's death.
- Family wealth ultimately received by the Dynasty Trust may be reduced if the policy lapses.

## PRIVATE FAMILY FOUNDATIONS

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A Family Foundation is a not-for-profit entity established by an individual, family or business exclusively for charitable purposes. It must be educational, religious, scientific, or literary as set forth in IRC §501(c)(3). The donor, or donor's family, is able to retain control over assets contributed including investment and grant making decisions. The donor, or donor's family, can receive reasonable compensation for services rendered as directors of the foundation. Essentially, it is a family run charitable business.

Income tax deductions for amounts contributed are typically limited to 30% of adjusted gross income (20% for public traded securities contributed). It can provide the donor and their family with the ability for family philanthropy to last for multiple generations. Family Foundations are subject to strict IRS guidelines including a requirement to distribute at least 5% of the foundations assets per year to a qualified charity. The IRS also strictly prohibits self-dealing preventing disqualified individuals from engaging in transactions with the foundation. Disqualified individuals include: donor, donor's spouse, children and their spouses, parents, and any employees of the foundation. Self-dealing transactions include: buying from or selling to the foundation, personal use of foundation assets, borrowing from the foundation, retaining foundation assets on private premises. Foundations also cannot own stake in a family-owned business and are subject to annual IRS charitable reporting requirements.



# Important Considerations

## BEFORE IMPLEMENTING THIS STRATEGY

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- Any investment that you plan to purchase or pay for during retirement involves the planning and use of your income or other assets. You should be certain you will have sufficient liquid assets to support your current and future income and expenses before considering the purchase of a life insurance policy. Equity in the home should not be considered a liquid asset.
- You should develop a comprehensive financial plan to take into account current and future income and expenses in conjunction with implementing the strategy discussed here.
- We recommend that you consult your tax and legal advisor to discuss your situation before implementing the strategy discussed here.

## ABOUT THIS CONCEPT

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- This concept is only intended to be used for assets that will not be needed for living expenses for the expected lifetime of the insured. It is your responsibility to estimate these needs and expenses and it is recommended that you consider developing a comprehensive financial plan in conjunction with implementing the strategy being considered. The accuracy of determining future needs and expenses is more critical for individuals at older ages who have less opportunity to replace assets used for the strategy.

## IF YOUR FINANCIAL OR LEGACY PLANNING SITUATION CHANGES

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- If you can no longer make premium payments, the life insurance death benefit may terminate and the results illustrated may not be achieved.

## WHEN THIS STRATEGY MAY NOT BE IN YOUR BEST INTEREST

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- Depending on your life span, it is possible that the Trust beneficiaries may receive more by just investing the assets used to pay the life insurance premiums rather than by receiving the death benefit of the life insurance policy that was purchased.

## TAX AND OTHER FINANCIAL IMPLICATIONS

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- There may be tax and other financial implications as a result of liquidating assets within an investment portfolio to purchase life insurance. If contemplating such a strategy, it is important to understand that life insurance is a long-term strategy to meet particular needs.
- The sale or liquidation of any stock, bond, IRA, certificate of deposit, mutual fund, annuity or other asset may have tax consequences, early withdrawal penalties or other costs or penalties as a result of the sale or liquidation.

## ABOUT LIFE INSURANCE

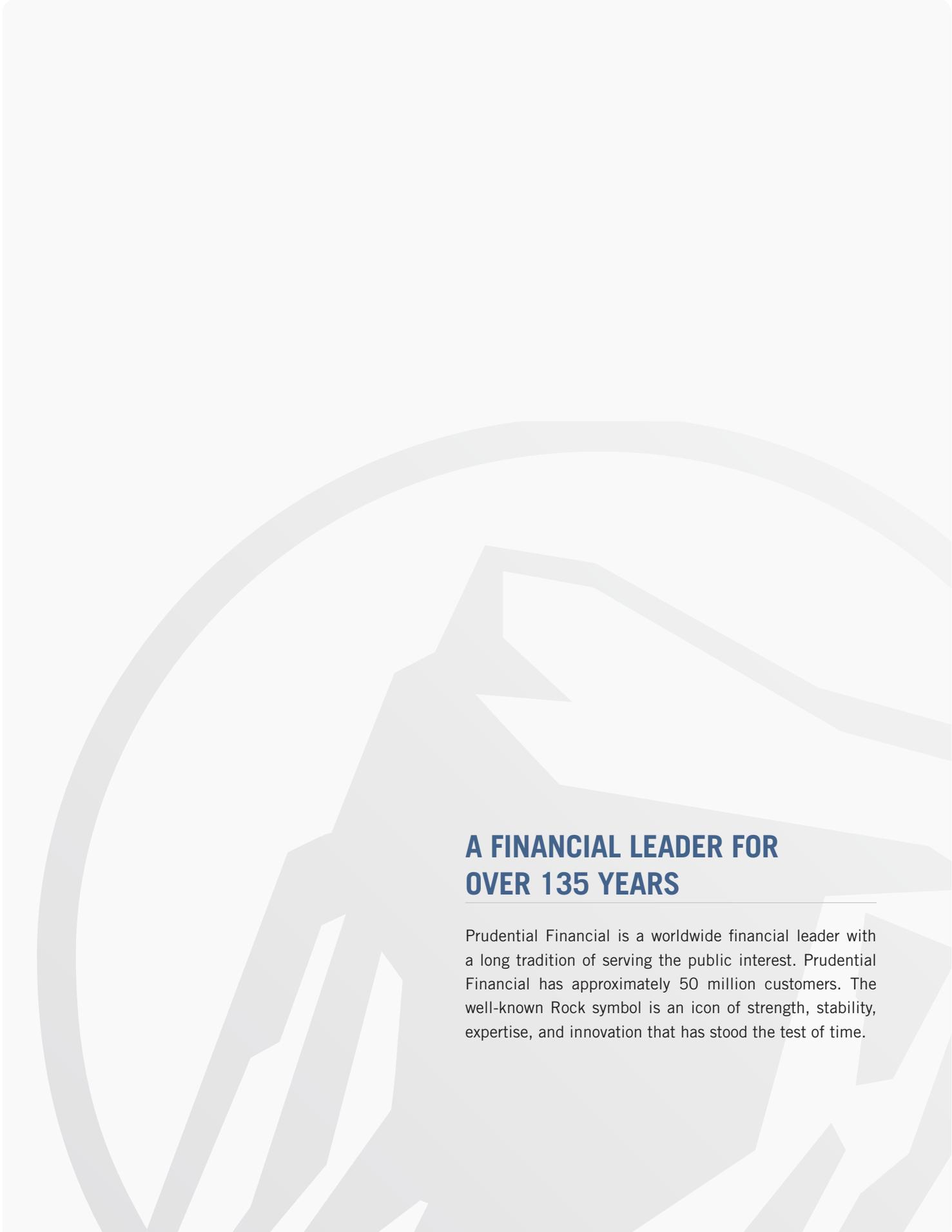
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- The death benefit protection offered by a life insurance policy can be a key component of a sound financial plan.
- It is important to fully understand the terms and conditions of any financial product before purchasing it.

## OTHER NOTES

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- You should consider that life insurance policies contain fees and expenses, including cost of insurance, administrative fees, premium loads, surrender charges, and other charges or fees that will impact policy values.
- If premiums and/or performance are insufficient over time, the life insurance policy could require additional out-of-pocket premiums to keep it in force.



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