

## **Glossary of Terms**

### **Accumulation Trust**

A trust that may pay out its income currently or accumulate it for distribution in a future year.

### **Adjusted Basis**

The taxpayer's cost basis of an asset reduced by depreciation or depletion deductions taken, for income tax purposes.

### **Alternative Valuation Date**

A date (other than death) to value all of an estate's assets. Usually, the Alternative Valuation Date is six months after the date of death, but if estate assets have been disposed of within those six months, then it is the date of such disposition.

### **Annuity Interest**

A fixed annual payment for one's lifetime or a term for years. Usually in estate planning this is referred to in regards to a specific type of trust, such as a charitable remainder annuity trust. See also "Private Annuity."

### **Attorney-in-fact**

The person authorized to represent the principal under a power of attorney.

### **Bargain Sale**

A sale, typically among family members or between an individual and a charity, at less than the full fair market value of the property. The difference between the sale price and the full fair market value is considered a gift from the seller to the buyer.

### **Basis**

The amount representing the taxpayer's cost of an asset, against which any amount realized on its sale or other disposition is compared to determine the amount of taxable gain, if any, and which may be depreciated, if the asset is depreciable.

**Beneficiary-owned Sub-S Corporation Trust**

A trust that owns stock in one or more Sub-S corporations, and that may do so without jeopardizing the corporation's special tax status, because the trust is treated as owned entirely by someone other than its Grantor.

**Beneficiary-owned Trust**

A trust that is treated as owned by someone other than its Grantor.

**Buy-Sell Agreement**

A contract or provision in corporate documents or a partnership agreement under which one or more persons or entities (the partnership or the corporation) agree to buy the interests of the other parties to the agreement, at certain times (usually *in lieu* of other lifetime sales or transfers and at death), at a stated price and on stated terms.

**Capital Gains**

Gains recognized from the sale or exchange of capital assets (most property other than inventory and certain specifically excluded types of assets).

**Charitable Lead Trust**

A charitable trust under which the charity receives an annuity interest (a fixed dollar amount, or a percentage (at least 5 percent) of the annual or initial value of the trust assets), for a term of years, after which a non-charitable person or group receives the remainder interest.

**Charitable Remainder Annuity Trust**

A charitable remainder trust under which the non-charitable income interest is expressed as a fixed dollar amount or percentage (at least 5 percent) of the initial value of the trust assets, and which does not permit subsequent additions.

**Charitable Remainder Trust**

A trust under which an individual or group of individuals receives an income or annuity interest for life or a term of years, and a charity receives the remainder interest thereafter.

**Closely-Held Corporation**

A corporation, the stock of which is owned by relatively few persons (often under thirty-five), rather than being subject to public trading.

**Community Property**

A concurrent ownership of property between spouses under the law of some states under which each spouse owns an undivided one-half interest in all property acquired during the marriage (often with specific exceptions).

**Complex Trust**

A trust that does not have to distribute all of its income currently, makes a charitable distribution, or distributes principal and so is treated differently for federal income tax purposes.

**Concurrent Ownership**

The ownership of property by more than one person at the same time. Takes the form of community property, tenancy by the entirety, tenancy in common, or joint tenancy. Concurrent ownership also carries rights to receive property outside of a will or trust, so avoiding probate, but also causing the terms of the will or trust to be overridden on transferring assets at death. It is one of the most common sources of disputes between heirs.

**Controlled Corporation**

A corporation, the majority of the stock of which is owned by one or a very few persons.

**Cross-Purchase Agreement**

A Buy-Sell Agreement under which the other partners or stockholders agree to buy the interest of a deceased or transferring partner or stockholder. Distinguished from a Redemption Agreement.

**Crummey Trust**

A power granted an individual under a trust instrument, whereby the individual can, for a limited period following any gift to the trust (usually thirty through ninety days), withdraw all or some stated portion of the gift. The power is used to make gifts to the trust present interests qualifying for the annual gift tax exclusion.

**Defective Trust**

A trust that is taxed as a Grantor Trust, usually because of a power inserted specifically to achieve this result, as with some life insurance trusts.

**Depreciation Deduction**

An income tax deduction for the wear, tear, and obsolescence of business and investment assets having a useful life.

**Direct Skip Gift**

A gift to the Grantor's grandchild or other person assigned to a similar or more remote generation (see "Skip Person"), upon which a Generation-Skipping Transfer Tax may be imposed.

**Durable Power of Attorney**

A Power of Attorney that does not end on the disability of the principal. Authorized in every state, but not in the District of Columbia.

**Estate Freeze**

The use of one or more techniques (such as a recapitalization of a corporation or partnership, or a Buy-Sell Agreement) to fix the value of a business interest or other property for estate tax purposes, causing all subsequent appreciation to inure to someone other than the interest's owner.

**Executorship**

This is the most limited and benign form of legal delegation. The individual or firm has been instructed to complete the settlement of an estate and to comply with a discrete set of directives that the client has authorized counsel to perform in his or her name even if the individual is deceased. Once the specified tasks have been completed, the Executor's work is usually finished.

**Family Attribution Rules**

Several tax rules under which stock or other interests owned by one family member are treated as owned by another family member, thereby limiting the possible techniques available to transfer assets from one generation to another that will work for unrelated parties, but are not available for family members.

**Family Corporation**

A corporation in which one or more family members are stockholders, often receiving their stock by gifts from other stockholder/family members.

**Family Partnership**

A partnership in which one or more partners receive their interests by gifts from other partners.

**Funded Life Insurance Trust**

A life insurance trust that holds significant assets other than life insurance policies.

**Generation-Skipping Transfer**

A transfer to a grandchild or other individual who is at least two generations below that of the Grantor, or to a trust for the benefit of such individuals, upon which a Generation-Skipping Transfer Tax may be imposed.

**Generation-Skipping Transfer Tax**

A tax imposed on a Generation-Skipping Transfer.

**Gift-Splitting**

A Grantor's making of a gift as to which the Grantor's spouse elected on a timely gift tax return (filed on or before April 15 of the year after the gift is made) to be treated as the Grantor of one-half of the gift, thus enabling the use of the Grantor's spouse's Unified Credit and annual gift tax exclusion.

**Grantor**

The person treated as the creator of a trust.

**Grantor Retained Annuity Trust**

A trust under which the Grantor retains an annuity interest for a term of years, followed by a transfer of the trust funds to the named individual or individuals.

**Grantor Retained Income Trust**

A trust under which the Grantor retains an income interest for a term of years, followed by a transfer of the trust funds to the named individual or individuals.

**Grantor Trust**

A trust that is treated as owned, in whole or in part, by its Grantor. Because the Estate Tax Code and Gift Tax Code are separate from the Income Tax Code, it is possible to have a trust that is income taxable to the Grantor (and

from which the Grantor can receive payments) but is excluded from the Grantor's estate.

### **Guardianship**

This is a more extensive and more generalized form of legal delegation, because it usually involves the care and maintenance of a living person and covers an unknown set of future circumstances over an unknowable period of time. As a result, the attorney is given much more flexible powers than those involved with an Executorship.

### **Holding Period**

The length of time a taxpayer is deemed to have held an asset. This is important in distinguishing between long-term and short-term capital gains.

### **Irrevocable Trusts**

In an irrevocable trust all rights to the property transferred to the trust are given up. The basic difference between an *inter vivos trust* and an outright gift is that the former provides the beneficiary with competent property management and with protection from himself and others who might misuse or waste the gift. Since outright gifts and irrevocable trusts differ only in terms of control over and protection of the beneficiary, the tax consequences are basically the same.

### **Installment Gift**

A gift made by selling property on the installment basis (receiving a note calling for a series of installment payments) and forgiving the payments annually.

### **Installment Sale**

A sale in which the seller receives a note calling for a series of installment payments, rather than a sale wholly for cash.

### **Joint Tenancy**

A type of concurrent ownership under which each owner owns an undivided interest in the whole property, and when one owner dies, the surviving joint owner(s) succeed to his or her interest.

**Personal Holding Company**

A closely-held corporation that primarily serves to own the stock of other corporations.

**Pick-up Tax**

A state death tax measured by the allowable federal estate tax credit for state death taxes.

**Power of Appointment**

A right held by one person to designate who shall possess or enjoy property that person does not own. For example, a trust may give an income beneficiary (such as a surviving spouse) the right to designate the remainder of the trust assets at the end of the Trust to a specified class of beneficiaries, such as "among my children." Estate and gift taxations are governed by §§ 2041 and 2514.

**Power of Attorney**

A document authorizing one person to represent another in specified transactions.

**Private Annuity**

The sale, usually by one family member to another, of property or the payment of money in exchange for an agreement to make a stated periodic payment, *e.g.*, weekly, monthly, annually, for the rest of the seller's life.

**Qualified Conservation Contribution**

A gift, deductible for income tax purposes, of a remainder interest or perpetual restriction for any of the following charitable purposes: 1.) preserving land areas for outdoor recreation by the general public; 2.) preserving land areas for education of the general public; 3.) protecting in a relatively natural habitat fish, wildlife, plants, or similar ecosystems; 4.) preserving open space for scenic enjoyment; or 5.) preserving an historically important land area or certified historic structure.

**Qualified Payment**

A right to a fixed and cumulative distribution with respect to preferred stock or a partnership interest, the value of which is taken into account in determining the value of a transferred interest in the same enterprise, under the special valuation rules.

**Qualified Subchapter-S Trust (QSST)**

A trust that, because it meets certain requirements, may be a shareholder of a Sub-S Corporation.

**Recapitalization**

A change in the stock, partnership, or debt interests of a corporation or partnership, sometimes accomplished to artificially freeze the value of one party's interest.

**Redemption Agreement**

A Buy-Sell Agreement under which the corporation or partnership agrees to buy out the interest of a shareholder or partner. Distinguished from a Cross-Purchase Agreement or a Hybrid Agreement.

**Remainder Interest**

The right given a beneficiary of a trust (or the beneficiary of certain non-trust arrangements, such as life estates or terms for years) to receive the trust fund upon some event, such as the death of another beneficiary.

**Reversionary Interest (or Reversion)**

A right retained by a trust's grantor (or by the creator of certain non-trust arrangements, such as life estates or terms for years) to receive the trust fund upon some event, such as the death of the beneficiary.

**Right of Survivorship**

A right as to property owned as joint tenants or as tenants by the entirety, whereby one joint owner succeeds to the interest of a deceased joint owner.

**Self-Destructing Trust Clause**

A provision in a life insurance trust under which, if any of the proceeds are included in the insured's gross estate (as when the insured dies within three years of having given the policy to the trustee), the proceeds are paid back to the insured's estate or to the insured's surviving spouse.

**Self-Settled Trust**

A trust, which is established with the funds of the beneficiary - typically, a tort victim or a person receiving an inheritance.

**Simple Trust**

A trust that is required to distribute all of its income currently, that does not pay principal and that makes no charitable distributions.

**Special Allocation**

A provision in a partnership agreement by which tax or other benefits are allocated among the partners otherwise than in accordance with their percentages of partnership interest generally.

**Split-Gift**

A gift as to which the Grantor's spouse elected on a timely gift tax return (filed on or before April 15 of the year after the gift is made) to be treated as the Grantor of one half of the gift, thus enabling the use of the Grantor's spouse's Unified Credit and annual gift tax exclusion.

**Split-Purchase**

An arrangement under which two persons buy property together, one buying a life interest and the other buying the remainder interest.

**Sprinkling Trust**

A trust in which the trustee may pay income (and sometimes principal) to any of a number of beneficiaries, usually in any proportions the trustee deems appropriate.

**Taxable Termination**

When an interest of a trust beneficiary who is a child (or similar generation) of the Grantor of the Trust ends and that causes the trust to vest in one or more beneficiaries who are grandchildren (or of a generation at least two below that of the Grantor) then the ending of the interest will result in a Generation Skipping Transfer Tax being imposed.

**Tenancy by the Entirety**

Concurrent Ownership between spouses in which each spouse owns an undivided interest in the whole, with a right of survivorship, and which can be terminated only by the consent of both spouses or the termination of the marital relationship. To form a Tenancy by the Entirety, the fact must be explicitly stated on the deed or other transfer document, otherwise the law presumes that the spouses hold the property as joint tenants.

**Tenancy in Common**

A type of Concurrent Ownership of property whereby each party owns an undivided fractional interest in the property, with no right of survivorship. The fractional interest need not be equal. For example, a father could hold a 2/3 interest in land, and the son holds 1/3. Tenancy in Common does not pass outright to the surviving tenant (as does joint tenancy interests) but passes under the respective tenant's will.

**Term Life Insurance**

A type of life insurance that provides pure life insurance protection and no cash values.

**Three-Party Gift / Leaseback**

A Gift / Leaseback in which the Grantor gives property to the Grantee, and then the Grantor's corporation leases it back from the Grantee.

**Two-Party Gift / Leaseback**

A Gift / Leaseback in which the Grantor leases the property directly from the Grantee.

**Trusteeship**

This is the greatest level of legal delegation of control. Here, the trustee is provided with the actual legal title of property - for the benefit of another - with the most extensive powers and the most discretion with respect to exercising those powers. Trustees are held to the highest duty of care and loyalty and are required to exercise their powers only in the best interests of the beneficiaries. Their role is defined and guided by the Trust documents and, if the Trust is silent on an issue, by the extensive Common Law traditions and/or statutory authority, Trusts attempt to anticipate the future, sometimes for several generations, and must be flexible and not rigid to avoid falling apart - and failing to achieve their original intent - when facing the challenges of the future. Consequently, the need for sound thinking, practical experience, reasoned drafting and the right kind of law firm is paramount.

**Unfunded Life Insurance Trust**

A life insurance trust that holds no significant assets other than a life insurance policy.

**Unified Credit**

A credit allowed against both the federal estate and gift taxes. To the extent the credit is not used against an individual's lifetime gift tax liabilities, it is available to offset estate tax obligations. The credit in 2002 was \$345,800, equivalent to an exemption of \$1 million, and in 2004 it was \$1.5 million. It is scheduled to increase for estate tax purposes to an exemption equivalent of \$1.5 million in 2004, \$2 million in 2006, and \$3.5 million in 2009.

**Uniform Gifts to Minors Act**

A uniform law, adopted in every state, under which gifts of cash or "securities," and sometimes other types of property, may be given to a named custodian on behalf of a minor Grantee.

**Uniform Gifts to Minors Act Custodian**

The person who holds property for a minor under the Uniform Gifts to Minors Act.

**Uniform Simultaneous Death Act**

A uniform law, adopted in every state, that creates a presumption of an order of death when it is impossible to determine which of two related persons died first.

**Uniform Transfers to Minors Act**

The 1984 revision of the Uniform Gifts to Minors Act, under which more and different types of property may be the subject of gifts to minors through custodians and more types of transfers (by trusts and estates) are permissible.

**Will**

A will is the most valuable instrument in estate planning. A will can do many things including: designate who should receive certain property, prescribe whether the property should be transferred outright or by other means, coordinate the amount transferred to a spouse, appoint guardians for children, executors and/or trustees, and provide the fiduciaries with adequate powers to carry out the administration of estate assets.