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# Using Uniform Transfers to Minors Act Accounts for Gifts to Minors

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Transfers of property to minors pose significant challenges. Aside from the legal barriers to the ability of a minor to enter into binding contracts, even individuals who are approaching adulthood may be inexperienced in managing assets. A formal trust for the benefit of a minor, in which ownership and control are held by the trustee, can be complex and require its own income tax returns. For small or modest property transfers, a trust may not be a suitable choice.

The Uniform Transfers to Minors Act (UTMA), which has been adopted by almost every state, the District of Columbia, and the U.S. Virgin Islands, may offer a solution. South Carolina has not adopted UTMA, but uses the older Uniform Gifts to Minors Act.

Under UTMA, any type of property, including real estate, cash, stocks and bonds, limited partnership units, tangible personal property, bequests, and life insurance policies or proceeds, can be transferred to a custodian for the benefit of a minor. Depending on the state, the custodianship continues until the minor attains age 18 or 21. Some states, such as California and Florida, permit an election for the UTMA relationship to last until age 25.

Under UTMA, the custodial relationship is created by executing a simple instrument, the form of which is set forth in the statute. That instrument specifies which state's UTMA statute is to apply: the state of residence of the transferor, of the minor, of the custodian, or of the location of the custodial property. The property is under the control of the custodian, not the minor. The custodian must use the property for the sole benefit of the minor.

## Who Should Not Be a Custodian

For an asset to be held in UTMA form, all that is necessary is for it to be registered in the name of the transferor or some other adult, or a trust company, followed in substance by the words, "as custodian for __________ (name of minor) under the ________________ (name of applicable state) Uniform Transfers to Minors Act."

The minor's Social Security number is used for the UTMA account, and the income is reported using the minor's Social Security number. As a result of the changes made to the so-called "Kiddie Tax" in 2017, the federal income tax on the investment income of individuals under age 19, or under age 24 if full-time students, is no longer taxed at the parents' tax rate. Instead, beginning in 2018, the Kiddie Tax rates for income in excess of $2,100 will be the rates applicable to trusts and estates. Trusts and estates tax rates reach 37% at only $12,500 of income. This could be a trap for the unwary, and so caution is advised.

Gifts to UTMA accounts qualify for the annual gift tax exclusion, which is currently $15,000 per recipient. Because of the broad discretion conferred on the custodian regarding the use of the custodial property for the benefit of the minor, the UTMA transfers will be included in the donor's gross estate for estate tax purposes if the donor dies while serving as custodian. Therefore, a grandparent who makes gifts to the account should not be the custodian of an UTMA account for a grandchild.

Only one custodian is permitted at a time. An acting custodian can designate his or her successor, or a series of successor custodians.

In New York and some other states, a minor who is at least age 14 has the right to petition the court to

remove a custodian for cause and to designate a successor custodian. A minor who has attained the age of 14 years is also authorized to petition the court for an accounting of the actions of the custodian.

## Pros and Cons of UTMA Accounts

As you may have surmised, UTMA accounts are not a panacea. The main advantages are:

- Simplicity.
- Low cost to establish.
- Ease of administration and similarities among the states.

Some of the disadvantages of UTMA accounts include:

- Rigid distribution requirements upon attainment of adulthood.
- Loss of parental control of assets if a parent is not the custodian, but adverse estate tax implications if the transferor is also the custodian.
- Kiddie Tax rules that can affect the opportunity to save income taxes.
- Possible adverse impact on the child's eligibility for college financial aid.
- The prospect of the child receiving more money at termination of the UTMA account than he or she is competent to manage (or willing to use prudently).

Nevertheless, in certain circumstances, an UTMA account may be an appropriate device for transferring modest amounts to children.

## Section 529 Accounts

For some, tax-favored section 529 college savings accounts may be advisable. Funds in a 529 plan account must be used for "qualified education expenses" of the account beneficiary. Such expenses include tuition, fees, and often room and board for college, university, or post-secondary vocational school, as well as up to $10,000 annually of K-12 private or public school tuition.

The earnings of a 529 account grow free of income tax, and distributions are tax-free if used for allowable education expenses. Moreover, unlike an UTMA account, the owner of the 529 account can be the student's parent, without inclusion in the parent's estate for estate tax purposes. There are, however, restrictions on how the 529 account can be invested.

The impact of 529 accounts on college financial aid is complicated, and depends on who owns the account and the timing of distributions from the account.

You should consult with a knowledgeable advisor before establishing an UTMA or 529 plan account. For some beneficiaries, a traditional trust, having terms specified by the trust creator, may be a more suitable vehicle.

## who's who

**Abbe I. Herbst** is a shareholder in Anderson Kill's New York office. Ms. Herbst is admitted to practice in New York and New Jersey, and has broad experience in the areas of estate and tax planning and trust and estate administration. She is a member of numerous bar associations.
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