

How Grandparents Can Care For Future Generations in a Tax-Advantaged Way

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Grandparents that provide financial support for their grandchildren should be aware that there are certain tax advantages available to them.

Grandparents may provide supplementary assistance for their grandchildren because they have the means to do so while others may find that the financial support is a matter of necessity. In the latter circumstances especially, grandparents should be aware of the tax benefits that are available to them.

Most high net worth families are familiar with the \$14,000 annual Federal gift tax exclusion, which is the amount an individual can gift to another individual without incurring a gift tax. That figure doubles to \$28,000 for married couples.

For grandparents that have a greater role in their grandchildren's care, the combined gift exclusion may woefully be less than the actual amount of support they provide and the tax benefits afforded to parents. Fortunately, there are some provisions that can permit grandparents to provide support for younger generations while minimizing the tax burden.

In a previous article, we discussed how payments made directly to qualified educational programs do not count against the annual exclusion amount. And, although gifts made to 529 educational plans do count against the annual exclusion amount, grandparents may make five years of contributions in one lump sum payment. This means a single grandparent could pay \$70,000 to a 529 Plan and it will be spread over five years (while married grandparents can contribute \$140,000). If the maximum amount is paid, the grandparents cannot make any further gifts to that individual for the next five years.

Grandparents may also treat qualified healthcare expenses (expenses that are paid directly to the healthcare provider) as they do qualified education expenses. The annual exclusion amount, combined with education and healthcare expenses can certainly go a long way in alleviating any gift tax burden.

In the event that grandparents provide support that exceeds education and healthcare, a single grandparent may be able to file as head of household. However, this would require that their grandchild live with them for more than half of the year. Filing as a head of household can put the grandparent in a lower tax bracket which means that they will be eligible for a higher standard deduction and lower overall income taxes.

Another option is for grandparents to establish a 2503(c) Trust for each grandchild under their care. Grantors may make gifts to the trusts up to the annual exclusion amount. Even though those dollars may be for future interest — such as when the child turns 21 — the grantor can still treat the gift as having “present interest.”

With planning and care, grandparents that play a greater role in providing for their grandchild's financial support can capitalize on certain tax opportunities available to them.

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