

UGMA AND UTMA ACCOUNTS

Vehicles aimed to save for college or make gifts to minors.

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If you want to save for college, you may wish to consider an UGMA or UTMA account. These custodial accounts are typically created by parents and other relatives who want to gift minors without having to set up a trust.

Many parents and grandparents create UGMA or UTMA accounts as college savings vehicles. You can invest for a child's education while transferring income-producing assets to that child (and their presumably lower tax bracket).

The Uniform Gifts to Minors Act (UGMA) allows a child or teenager to take ownership of cash, securities or insurance policies. The successive Uniform Transfers to Minors Act (UTMA) extended the UGMA parameters: it lets minors receive gifts of art, real estate, patents and royalties, and other non-securities assets.^{1,2,3}

UGMA and UTMA accounts address a minor concern. You may be thinking, "Well, I know outright gifts to a minor aren't subject to federal tax, so why set up an UGMA or UTMA? Why don't I just gift the money or securities outright?"

Do you really want to do that?

Let's face it, you probably want control. Most likely you don't want your teenager buying and selling securities any more than brokerages do. You might also want to be certain that the cash you gift is not spent frivolously. If these concerns speak to you, UGMA and UTMA accounts may be worth a look.

In 2010, you can use these accounts to gift up to \$13,000 in money or property to a minor. In fact, you can gift up to \$13,000 each to multiple minors. If you stay under the annual federal gift tax exclusion amount each year, you will only trigger federal gift tax if you transfer more than \$1 million during your lifetime.⁴

You are the custodian; the minor is the owner. In colloquial terms, these UGMA or UTMA accounts are "trust funds" - yet they are not trusts that would require the involvement (or fees) of an attorney. While the minor owns the cash or property within the UGMA or UTMA account as soon as the asset transfer occurs, the custodian manages that cash or property until the child reaches the age of maturity (18 or 21 in all but a few cases).⁵

As custodian, you are not the only one who can make irrevocable transfers of cash or property *into* the account; parents, grandparents, relatives and friends may all do so. A sizable college fund may be built with an UGMA or UTMA account, whether the assets are held in cash or invested. When the account owner reaches "maturity", he or she may spend that money for college.

Is there a potential downside of UGMA or UTMA accounts? Yes. To repeat, you are the custodian, *the minor is the owner*. When that minor becomes an adult under state law, the account terminates and the account owner gets to spend the funds as he or she wishes. It's a free country ... and it is possible that today's college fund will become tomorrow's Corvette. So you do want the owner and the custodian on the "same page" when it comes to the intent of the account, and on good terms as well.⁵

Another potential issue to consider: if you are custodian of one of these accounts and you pass away before the account terminates, the assets within the UGMA or UTMA account may become part of your taxable estate.³

An under-publicized option worth checking out. UGMA and UTMA accounts may give your family the potential to create a nice pool of money for college while lowering your income taxes in the process.

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Citations

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