

## **Prepaying Tuition As An Estate Tax Strategy**

If you have a large estate and want to pay for a student's tuition, but think you may not live long enough to pay those bills as they come due in the future, there is a new tax strategy available for you.

In a recently released private-letter ruling by the Internal Revenue Service, the IRS told a taxpayer that prepayments of multiple years of tuition for the taxpayer's grandchildren wouldn't be considered a gift for tax purposes. The taxpayer in question proposed prepaying tuition bills for each of six grandchildren through 12th grade.

Under current law, you can hand out as much as \$12,000 a year per person to anyone you want without even having to report it to the IRS. Yet it doesn't count against that annual limit if you pay for someone else's tuition or medical expenses, no matter how large your payments may be provided those payments are made directly to the educational institution or medical-services provider.

The net effect is that you can move large amounts of money out of your estate tax-free, without even having to report your gifts to the IRS and without eating into any of your estate tax or lifetime gift-tax exclusion amounts.

The lifetime gift-tax exclusion amount is \$1 million. The basic federal estate-tax exclusion amount is \$2 million this year.

One thing you might want to do before committing to such a strategy is to make sure the student involved is going to hold up their end of the deal. Here's why:

- All tuition payments would be nonrefundable
- Once paid, would become the school's property, even if the students stopped going there
- The student is not entitled to any additional rights or privileges over any other student, and the payment does not guarantee enrollment.

Some schools are adopting policies to protect against this risk. These policies generally include transferring the money to another school, if, for example, the student transfers. But the IRS has not specifically ruled on this issue and such an agreement may not pass IRS scrutiny.

One of the main attractions of the direct-prepayment strategy is its simplicity. There is no need to hire a lawyer to draft complex trusts or other sophisticated wealth-transfer techniques.