

(TEMPORARY) REPEAL OF FEDERAL ESTATE TAXES PRESENT IMMEDIATE
DRAFTING CONCERNS???

In 2001, Congress passed, and President Bush signed what has come to be known as “The Bush Tax Cuts.” Marginal income tax brackets were reduced, capital gains tax rates were reduced and the “death tax” was phased out over the next 10 years (more below). All provisions of “The Bush Tax Cuts” sunset expire on December 31, 2010.

With respect to federal estate taxes, the Exclusion Amount / Unified Credit Amount was increased in 1997 from Six Hundred Thousand dollars (\$600,000) to \$1 Million Dollars (\$1,000,000) over a 10 year period of time. Specifically, the Exemption Amount was increased to \$625,000 for persons dying in 1998; \$650,000 for persons dying in 1999; \$675,000 for persons dying in 2000, and so on, gradually working its way to \$1,000,000 for persons dying in 2007.

The Bush Tax Cuts accelerated this process, increasing the Unified Credit Amount to \$1 Million dollars (\$1,000,000) for persons dying in 2002 or 2003; \$1,500,000 for persons dying in 2004 and 2005; \$2,000,000 for persons dying in 2006, 2007 and 2008; \$3,500,000 for persons dying in 2009 and if you are lucky enough to die in 2010, there are no federal estate taxes.

On December 31, 2010, all provisions of the Bush Tax Cuts expire / sunset and on January 1, 2011, the Unified Credit returns to \$1,000,000 and the top tax bracket to fifty-five percent (55%).

Since 1981, married couples have traditionally been advised to utilize an “A B Trust” which allows each spouse to set aside the greatest amount that can pass free from federal estate taxes in the year of each respective spouse’s death. For purposes of discussion, let us assume a hypothetical couple with a combined total taxable estate of Four Million dollars (\$4,000,000). A typical A B Trust would provide that after the first spouse’s death, the greatest amount that can pass free from federal estate taxes shall be allocated to the decedent spouse’s Bypass Trust, and the balance of the marital estate would be distributed to the surviving spouse’s Survivor’s Trust. Assuming husband dies in 2006, when the Exemption equivalent / Unified Credit is Two Million dollars (\$2,000,000), then \$2,000,000 would be distributed to his Bypass Trust / Trust A and the remaining \$2,000,000 would be distributed to her Survivor’s Trust / Trust B.

On the other hand, what if husband died in 2010? If the greatest amount that can pass free from federal estate taxes is infinity for persons dying in 2010, then the entire Four Million dollars (\$4,000,000) would be distributed to his Bypass Trust (Trust A) and zero dollars would be allocated to wife’s Survivor’s Trust (Trust B).

The good news for their children is that no matter what the Unified Credit Amount is in the year of wife’s death, she has no assets in her taxable estate and there will be no federal estate taxes upon her death.

The bad news is if she wants to change her portion of the Trust, she cannot, because everything went to his Bypass Trust which typically says that she is entitled to all of the net income and only that amount of principal as is needed for her health, education, support and maintenance. The other problem is that the entire estate is in husband's Trust and when wife dies, the heirs get no step up in basis on any asset owned by Mom, because Mom does not own anything.

This dilemma has led many estate planning attorneys to write "emergency alert" letters to their clients advising them that they need to get in to see their attorney right now and amend their Trusts to provide that should either spouse die in 2010, that the amount of assets allocated to the deceased spouse's Bypass Trust would be "the greatest amount that can pass free from federal estate taxes or one-half of the estate, whichever is less."

This is unnecessary for any clients of Drobny Law Offices, because the formula clause we have used since 1981 already contains the limitation of restricting the deceased spouse's estate to the deceased spouse's half of community property and one hundred percent (100%) of the deceased spouse's separate property, up to the greatest amount that can pass free from federal estate taxes in the date of his/her death.

The other "warning" included in these emergency alert client letters that we have seen in articles, newspapers, magazines and on the internet is that the surviving spouse would have no access to or control of the deceased spouse's Trust. Again, that is simply fear mongering at its worst by unscrupulous attorneys looking to profit from potential client's fear. Virtually any Bypass Trust I have ever seen names the surviving spouse as the Trustee of not only the surviving spouse's Trust but the deceased spouse's Bypass Trust. Virtually every Bypass Trust I have ever seen allows the surviving spouse to access all of the income from the deceased spouse's Bypass Trust and as much of the principal as the Trustee (surviving spouse), in the Trustee's absolute discretion, deems necessary for the surviving spouse's "health, education, support and maintenance." What possibly could not be included under the words "support" and "maintenance?"

Furthermore, virtually every Bypass Trust I have reviewed provides that

"For the guidance of the Trustee, but not in limitation of the Trustee's discretion, I intend to provide first for the needs of my surviving (wife / husband) so that (she / he) will be able to live in the manner to which (she / he) has been accustomed, and that (her / his) health needs are adequately provided for."

It is truly unfortunate that millions of Americans are reading these articles and letters and spending thousands of dollars unnecessarily to have an attorney revise Trust documents that do not need to be amended. It is virtually unnecessary in every case I have reviewed.