

Current Estate Tax Laws May Make Previously Drafted Estate Plans Inefficient

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The increased exemptions provided by the current estate tax law (\$5.34 million per person for 2014) provide clients with a great opportunity for the tax free transfer of assets both during life and at death. However, the dramatic increase in these exemptions over the past few years and the addition of the portability concept (which allows one spouse to utilize his or her deceased spouse's unused exemption) makes the review of plans drafted before the January 2013 implementation of the current law extremely important.

Traditionally, the most efficient way for married couples to reduce estate taxes was to rely on the creation of a credit-shelter or "Family Trust" on the death of the first spouse. Upon first death, the Family Trust is funded with the decedent's assets (up to the estate tax exemption amount). For example, if the combined marital estate equaled \$4M, on the first death, the Family Trust would be created with the decedent's full \$2M of assets. The benefit of this type of funding is that assets in the Family Trust are not subject to estate taxes on the death of the survivor. While this type of plan is still an effective way to save on estate taxes, fewer and fewer couples need tax-based plans due to the current high exemptions. If you currently have this type of "formula" plan, it is important to contact your attorney to discuss whether it is still appropriate.

Failure to update a previously drafted plan may result in the overfunding of Family Trusts and the unnecessary creation of Marital Trusts, which may in fact lead to tax inefficiencies and unnecessary administrative costs. Specifically, under the current law, the creation of a Family Trust upon the death of the first spouse may no longer provide any estate tax advantage and its funding may risk the loss of certain income tax benefits upon the second death. Furthermore, in cases where Marital Trusts are used, the high exclusion may result in a smaller Marital Trust than anticipated, which may be inefficient and overly burdensome. If tax planning was the main purpose behind choosing this type of plan, an update may be necessary to ensure that this unnecessary funding of trusts does not occur and that your spouse is not left with an overly burdensome administration.

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