Estate Tax - The Martial Deduction

Between spouses who are U.S. Citizens, there is an unlimited marital deduction for estate tax purposes

Problems:

1) The second spouse is going to die too eventually and then the marital deduction won't help.

2) What if your spouse is not a U.S. Citizen?

3) What if you don't want your spouse to get all the money outright?

1) Credit Shelter Trust allows each spouse to take advantage of his or her unified credit

2) Giving the money into a "Qualified Domestic Trust" (QDOT) qualifies for the marital deduction

3) A Qualified Terminable Interest Property trust (QTIP) qualifies for the marital deduction even though it's not going directly to the spouse

Credit Shelter Trust

Only relevant for couples with more money than the unified credit amount.

Divide the assets into two sections:

> "A"- The maximum allowable unified credit of the decedent spouse
>
> "B" – The rest of the estate
>
> "A" goes into trust for the children (or whomever). The surviving spouse can get the income and a right to withdraw up to 5% annually and enough to support her if she needs it. That way, it's not part of the second spouse's estate. So, when she dies, it won't be taxed. (It's not hers.)
>
> *Note: It could also go straight to the children, but people usually don't want that*
>
> "B" does to the spouse (or to a QTIP for the spouse). It's not taxed because of the marital deduction.
>
> When the second spouse dies, the "A" money goes straight to the kids (no tax) and the "B" money is taxed because it's the second spouse's money.

Qualifies Domestic Trust (QDOT)

Problem: Government does want people giving big fortunes to foreign spouses who won't be subject to U.S. tax jurisdiction.

Solution: I.R.C. § 2056(d):

→ No marital deduction for foreign spouse unless it's put into a trust that will be subject to U.S. tax law jurisdiction or unless the spouse becomes a U.S. citizen.

Qualified Terminable Interest Property (QTIP)

- Qualifies for the marital deduction even though it's not going to the spouse outright

- Goes into trust for the benefit of the children, BUT:

    1) Spouse must get an interest in all the income from the trust for life
    2) No one other than the spouse can have an income interest and no one can appoint (give) to any other person anything from the trust
    3) The spouse must have the power to demand that the trust be used in a manner so as to be income producing
    4) The trustee may have the power to give the spouse any amount for any reason

Important: The QTIP is part of the second spouse's estate. So, when she dies, that money will be taxed. So, if any money has to be spent, it is better off being spent from the QTIP assets, and not from the credit shelter trust assets.

Other Issues

Deductions

- Charitable

- State Death Tax Deduction

- Estate expenses

GSTT Tax

The 2001 Act

- Estate Tax exemption now $5,000,000 ($10m per couple)

- Back to $1,000,000 exemption in 2013

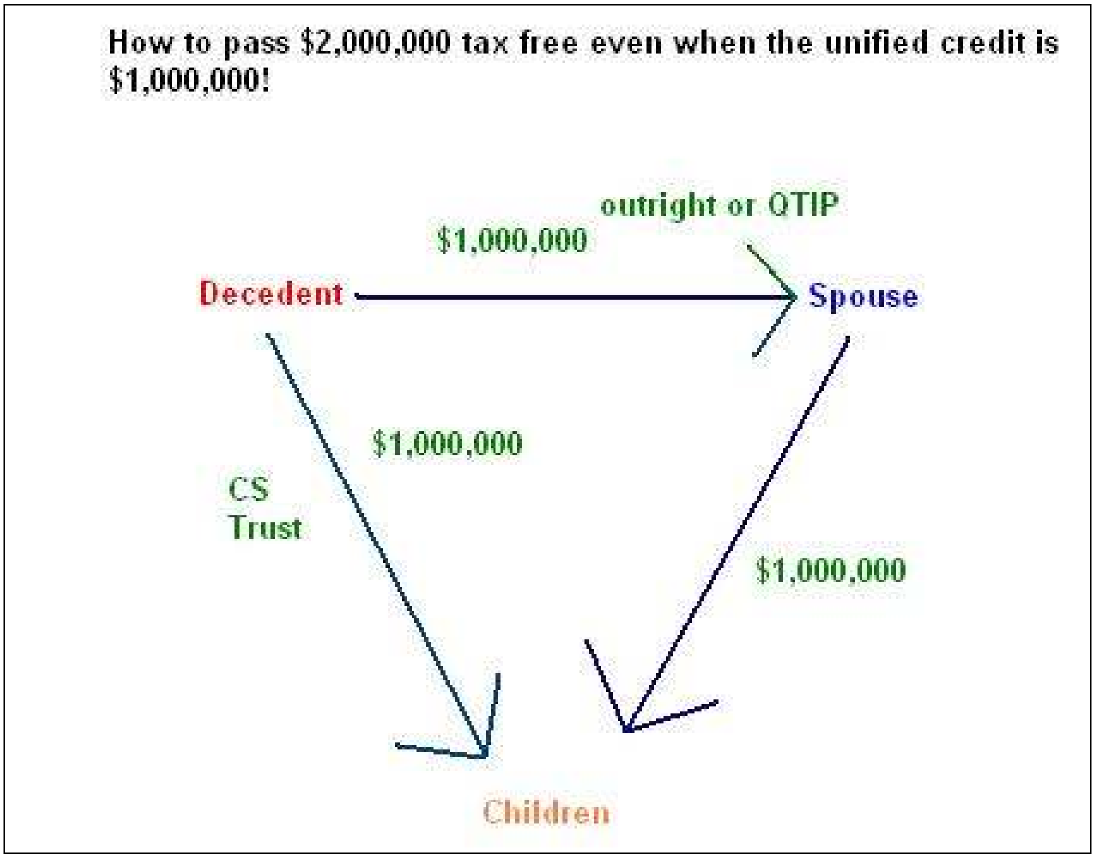
- Estate Tax in Flux and depends on who is in power.

    If Democrats do well in 2012, you may see the estate tax exemption return to $1,000,000 and maximum rates go back up to 55%

    If Republicans do well in 2012, you may see the estate tax repealed all together

    Something in between is most likely

CS Diagram


How to pass $2,000,000 tax free even when the unified credit is $1,000,000!
outright or QTIP
$1,000,000
Decedent
Spouse
$1,000,000
CS
Trust
$1,000,000
Children