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## Portability of the Estate Tax Exemption: Every Good Spouse Deserves (and Still Needs) a Trust

One of the more intriguing provisions of the new Tax Relief Act of 2010\* ("TRA") is a new "portability" system which, at first glance, appears to eliminate the need for estate tax exemption trust planning. These portability rules allow a surviving spouse to take a decedent spouse's unused estate and gift tax exclusions in order to avoid estate taxes on the second death, even without proper estate planning documents in place. A brief explanation appears to be in order.



For decades now, the primary estate planning tool for married couples has been the estate tax exemption trust, drafted into each spouse's living trust or last will and testament. This trust, often referred to as a "Family Trust" or "By-Pass Trust," preserves the estate tax exclusion amount of the first spouse to die for the benefit of the descendants. Perhaps a smidge more brief explanation.

Under the marital deduction rules, one spouse may leave unlimited millions to the surviving spouse with no estate tax liability – until the death of that survivor, of course. The estate tax exemption trust works by setting aside an amount of assets, not more than the then-current exemption amount, in trust for the benefit of the surviving spouse and/or family, so that those assets are not taxed at the second death. If a proverbial happy couple neglects to establish such an estate plan, then only the survivor's estate tax exemption applies, costing the family unnecessary tax liability.

The new portability rules may give succor to some who have not, alas, implemented the estate plan described above. Before complacency sets in, however, Mr. and Mrs. Happy must consider the risk factors presented with portability. First and foremost, portability is not permanent: the TRA is only in effect for 2011 and 2012, and Congress may enact new tax legislation next year without these portability terms.

Even if portability carries over into 2013 and beyond, the Happy couple should be aware of other essential considerations favoring estate tax exemption trusts for their new estate plan:

- The value of assets held in the estate tax exemption trust may appreciate substantially before the survivor's death, yet will suffer no estate tax;
- Since the generation-skipping transfer tax (GSTT) exemption is not portable, an estate tax exemption

trust must be used to retain the benefit of the full exemption for each spouse;

- The surviving spouse who remarries will lose the unused exclusion amount if he or she survives the later spouse (“de-portabilitized”);
- By contrast, the “portable” deceased spousal unused exclusion amount received by the surviving spouse is not indexed for inflation; and
- The deceased spouse’s assets may still receive “portable” estate tax exemption treatment, but there is no creditor or “predator” protection for them once owned outright by the survivor – and for currently non-taxable estates, the latter is a more compelling reason to have a spousal trust arrangement.



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These are the primary considerations which should give pause to Happy couples out there itching to amend the credit shelter trusts right out of their current estate plans. As for those thinking of preparing “I love you” wills for a “simplified” estate plan, the same timeless words of wisdom apply: that portability is not forever, and that every good spouse deserves (and still needs) a trust. Or something like that.

\* *The full citation of the bill is H.R.4853, “The Tax Relief, Unemployment Reauthorization, and Job Creation Act of 2010.”*

If you would like for any of our attorneys to speak to your group on a topic within our practice areas, please call Erin Hamberg at 757-605-5000.

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