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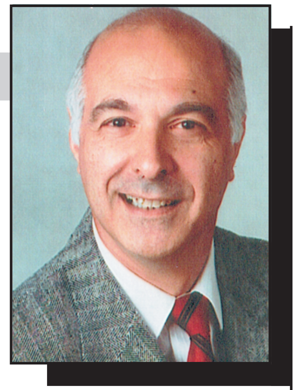
With four specific services, The Center provides complete unbiased planning. The Center does not sell any products; its main purpose is to provide advice. Local experts are retained to implement the plans developed by the Center. The Center for Financial, Legal & Tax Planning is located at 4501 W. DeYoung Street, Suite 200, Marion, Illinois 62959. Phone 618-997-3436; Fax 618-997-8370.



Bart Basi

The Bypass and Marital Trust Quagmire of 2010

For those in business, planning the future of your business and estate just got more difficult. The reason? There is no estate tax for the year 2010. Quite simply, it is currently repealed. While at first blush, the repeal of the estate tax seems as though it should be cause for celebration. On the other hand, for the professional planning estates of high net worth individuals and the spouse of high net worth individuals, it is a not-so-obvious hazard.

The Estate Tax Laws

Since 2001, taxpayers in the United States have seen ever increasing estate tax exemption amounts. To illustrate, in 2001, the estate tax exemption amount was $1,000,000. This meant that someone dying having an estate of $1,000,000 or less could leave the estate to someone other than a spouse and not have to pay any estate taxes. The exemption peaked in 2009 at $3,500,000. As of now, in 2010, the estate tax is officially repealed, but is slated to return on January 1, 2011 with an exemption amount of $1,000,000. To estate planning attorneys, this boomerang effect is causing some issues.

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Enter the Bypass Trust and the Marital Trust

Since the estate tax has been around, estate planning professionals have been utilizing what are known as the Bypass Trust and the Marital Trust. Each is a trust in its own form, both work together to achieve the same purpose, yet each is different in their function. When used in tandem, the Bypass Trust is a trust that upon the individual's death is funded to the extent of the maximum estate tax exemption available. If an individual had passed away in 2001, the Bypass Trust would have been funded with $1,000,000. The contents of the Bypass Trust are left to the children, utilizing the deceased individual's estate tax exemption.

The other trust, known as the Martial Trust is a trust that upon the death of the first spouse is funded by the excess of the estate over the exemption amount and is for the benefit of the surviving spouse. For example, a person dies with an estate worth $9 million in 2009. First, the bypass trust would be funded with $3,500,000 for the benefit of the children. The next $5,500,000 would be placed into a Marital Trust for benefit of the spouse. Upon the death of the surviving spouse, the estate itself would utilize the surviving spouse's exemption for estate tax purposes. In this case, the exemptions total $7,000,000, with $2,000,000 remaining subject to the estate tax. From this, approximately $900,000 would be taken for estate taxes. The end result is that the children are left with $8,100,000. The equation worked well for the time during the existence of the estate tax.

The 2010 Issue

A new problem arises in 2010. In 2010, the estate tax has been repealed. The applicable estate tax exemption is now $0 (zero). There are two possible scenarios. First, if a bypass formula stipulates "the maximum estate tax exemption applicable" is to be placed into this trust, then if the first spouse passes away in 2010, the bypass trust will be funded with $0, since there is no exemption in 2010. This then leaves the remainder in the Marital Trust for the benefit of the wife. If the wife dies in 2011, when the estate tax exemption is a mere $1,000,000, the same estate would be subject to approximately $4,100,000 in estate taxes, leaving the children with the net result of $5,900,000. This is quite a drop from the $8,100,000 they would have gotten two years previous.

Second, on the other hand, let's assume the trust is to be funded with "the maximum amount of value, not subject to the estate tax". In this scenario, the Bypass trust would be funded at the full $9,000,000 for the children, while making the spouse penniless. The effect of the second spouse dying in the year 2011 would be a full exemption from the estate tax since there would be no money in the estate.

Corrective Measures

While the best measure, to avoid confusion at least, would be to not die in 2010, a responsible estate planning professional should not bank on this. Many speculate that the estate tax will return in 2011 with an estate tax exemption of $3,500,000. It is our advice that you should 1) have your estate plan reviewed and your goals discussed with a tax professional and 2) amend your estate plan as necessary to deal with the issues that have been presented hereinabove.

Like the Y2K virus of 2000, this issue has largely taken the country by surprise. Nobody expected the estate tax phase out and repeal to reach this point. Unfortunately, 2010 will be interesting for estate planning. The Center's professionals routinely deal with complex tax and estate planning issues such as the one presented in this article. If you have any questions or would like to have your estate plan amended to deal with the issue that 2010 presents, be sure to contact the professionals at The Center for assistance.

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