



## 2009 Estate Tax Legislative Update

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In 2009 the federal estate tax exclusion amount increased from \$2 million to \$3.5 million for U.S. citizens or residents dying after January 1, 2009. Under the present law, the estate tax is scheduled to disappear entirely in 2010 and reappear in 2011 with a \$1 million exclusion amount. However, during his campaign, President Obama indicated his intention to enact a permanent federal estate tax exclusion amount before 2010, with analysts predicting that legislation will be brought for the indefinite continuation of the \$3.5 million exclusion amount.

No matter which scenario occurs, these changes necessitate a review of your current strategy. Depending upon your wealth, the increase in the exclusion amount may alleviate the need to combat federal estate tax. However, the New Jersey exemption, which remains relatively low at \$675,000, may call for any of a number of strategies to lower your state tax exposure which will be discussed later in this article. In terms of the federal estate tax and its 45% tax rate, there are many new considerations to examine.

One strategy, probably the most utilized, is the by-pass (or credit shelter) trust. Under both federal and NJ law, there is an unlimited marital deduction (essentially an estate tax exclusion ) between

spouses: when one dies, the survivor inherits all of their assets (or half the joint assets) tax-free. When the survivor dies, that estate is afforded a \$3.5 million exemption on its assets. But remember, each individual is now eligible to pass \$3.5 million estate tax free to beneficiaries of his or her choice. In the previous scenario, the spouse passing first lost out on his or her exclusion amount.

One strategy involves having both wills direct, upon the passing of the first spouse, the first \$3.5 million of assets into a by-pass trust established under the will. The trust's ultimate beneficiaries will not include the surviving spouse (usually children are the beneficiaries) but can pay income to the surviving spouse during their lifetime. The remainder of the passing spouse's assets pass tax-free, under the marital exemption, to the surviving spouse. Upon *their* death, the first \$3.5 million of his/her estate is *also* passed tax free. So by creating the by-pass trust, the amount passing tax free in the original scenario doubled from \$3.5 million up to \$7 million. This same strategy can be employed for estates only concerned with NJ estate tax by simply changing the funding amount of the by-pass trust from \$3.5 million to \$675,000. With this general understanding of the by-pass trust strategy, we can now

discuss how the increase of the exemption amount can affect an estate plan.

Whether it is a house, bank accounts or other assets, most married couples title their property in joint names. When one dies, the survivor takes full title to the asset by operation of law. This can present a problem in that there may not be enough assets in the sole name of the spouse that is first to die to fully fund the by-pass trust. For example, a couple jointly owns a \$5 million home and the husband has \$1 million in a money market account in his sole name. He passes and his will directs that the first \$3.5 million dollars of his estate flows into a by-pass trust. By operation of law the house transfers to the surviving wife thereby, only leaving \$1 million to fund the trust. If the home was titled in both of their names as tenants in common, half of the home's value (\$2.5 million) plus the \$1 million money market account would flow into the trust, fully funding it at \$3.5 million. Many couples who have already done estate planning may have properly titled enough assets in each spouse's sole name to fully fund the by-pass trust under a \$2 million exemption no matter which spouse passes first. However, the increase in the exemption amount requires that *all* assets be reexamined to ensure that each spouse has enough assets

in their own name to fund the by-pass trust. This should not create much of a problem for couples possessing assets well in excess of \$7 million.

However, this could present a problem for couples whose assets are just in the range of federal estate tax imposition. The language of most wills direct that upon the death of the first spouse, the by-pass trust will be funded to match the amount of the federal estate tax exclusion. If a couple had \$3 million in assets, all in the name of the first spouse to die, the by-pass trust would take all the assets and leave the surviving spouse with virtually no assets in their name. This may not be the result the couple was planning for under the prior, lower exclusion amount.

There are several more issues, some complex, that have now arisen as a result of the increase in the estate tax exclusion amount, and we would be happy to review your estate planning documents with you during a free consultation at our office.

*Adam Dubeck focuses on matters related to Elder Law, Wills, Estates & Trusts, and Estate Planning. He is a former Associate Counsel of the Office of the Public Guardian for Elderly Adults of New Jersey, and carries a CSA designation from the Society of Certified Senior Advisors. He can be reached at the number below, or via e-mail: [adubeck@steinlegal.com](mailto:adubeck@steinlegal.com).*