

## A&B, Marital, or Living Trusts

Besides a will, A&B/marital/living trusts (hereinafter A&B trusts) are the most commonly used estate planning tool and one we recommend in nearly every estate plan. This assumes that you are married. If you are not married, you would simply have one living trust which would have the same advantages in Number 1) directly below. If you are not married, you cannot take advantage of Number 2) directly below, which discusses maximizing estate tax exemptions among spouses.

### **What are the benefits of A&B trusts?**

1) The first benefit of having A&B trusts is that your estate will not be probated through the court system. Your will does end up being probated, but the assets of the estate pour through your will to the A&B trusts. When that happens, your estate will typically be probated in an “unsupervised” manner where the court does not have to probate everything in your estate; and when this happens, you save (depending on the state) between 1-8% (4-6% is average) of the **entire value of your estate** in probate fees.

2) A&B trusts maximize your estate tax exemptions. In 2006, there is a \$1,500,000 estate tax exemption per spouse. That exemption increases until 2010 when there is no estate tax; and then in 2011, the estate tax is right back at the \$1,000,000 (unless Congress re-passes the estate tax repeal).

If one spouse dies without the A trust in place, the entire estate will then become the property of the surviving spouse. What happens when the first spouse dies? The \$1,500,000 estate tax exemption died with that spouse, and the remaining spouse now only has \$1,500,000 total in exemptions to use.

### **Let’s look at an example –**

Clients Dr. Smith and spouse are 50 years old. Total estate worth equals \$4,000,000. \$1,000,000 of the estate is the value of the marital home. Assume that the clients have a will but no A&B trusts.

**If Dr. Smith dies tomorrow, what happens?** The entire \$4,000,000 estate per Dr. Smith’s will goes to the surviving spouse.

**What estate taxes are due?** None, because there is an unlimited estate tax exemption when passing wealth to a spouse.

Then shortly after Dr. Smith dies, the spouse dies. **What happens?** The \$4,000,000 will pass through the will (and will go through probate) to the heirs. Forgetting the probate fee of up to 5%, because they did not have A&B trusts, what are the estate taxes due? **\$2,000,000 or 50% of the entire estate**, which is \$4,000,000 at the second spouse's death.

## **What would have been the estate taxes due if the couple had A&B trusts?**

When Dr. Smith died in 2005, the \$1,500,000 worth of assets (including the \$1,000,000 home) would become the property of the A trust and not the spouse. Per the language of the A trust, the living spouse gets to stay in the house until death, at which time the house will pass to the heirs. When the \$1,500,000 was poured into the A trust, the language in the trust designated that the \$1,000,000 house and \$500,000 in other assets were transferred by using the deceased spouse's \$1,500,000 estate tax exemption.

*Now assume the second spouse dies the next day.*

## **What happens and what estate taxes are due?**

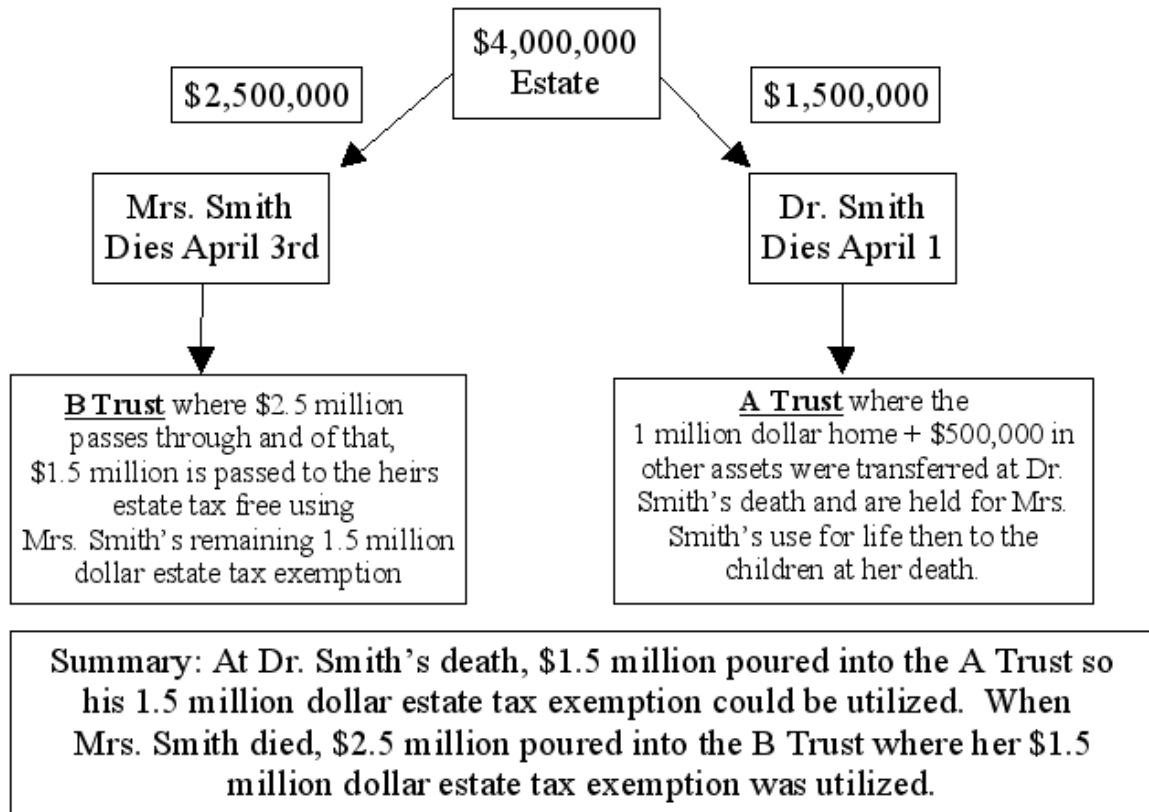
The remaining assets will be poured into the B trust (to avoid probate) and \$1,500,000 worth of those assets will be given to the heirs through the use of the second spouse's \$1,500,000 estate tax exemption. That leaves a total taxable estate of \$1,000,000; and, therefore, the heirs now only need to find \$500,000 to pay estate taxes.

## **What was the benefit of the A&B trusts?**

**We saved the heirs in the prior example \$500,000 in estate taxes and \$200,000 in probate fees.** Not bad.

Now we hope that Dr. Smith and the spouse had life insurance in an ILIT to pay for the estate taxes; and in the ILIT section of this material, we will explain how that works.

The following is a schematic of what happens with Dr. Smith and his spouse when they died a few days apart assuming they died in 2005.



### **What if Dr. Smith and his spouse died in 2007 with no A&B trusts?**

While most of our clients intend on living for at least 20 years (beyond their present age), that is not always the case. In 2007 (four years before the estate tax exemption will default back to \$1,000,000), the estate tax exemption is \$2,000,000. When the first spouse dies, again the entire \$4,000,000 estate will transfer to the surviving spouse estate tax free. When the second spouse dies a day later without a trust, the estate will get to use one \$2,000,000 estate tax exemption (which is the estate tax exemption in 2007); and, therefore, the estate will have to pay estate taxes of \$2,000,000.

### **What if the couple had A&B trusts when the first spouse died?**

Two million dollars would have poured into the A trust (for the benefit of the surviving spouse until death), and \$2,000,000 would have gone to the surviving spouse without estate taxes. Then, if the second spouse died the next day, the remaining \$2,000,000 would pour through the B trust to avoid probate; and the second \$2,000,000 exemption would be used. That would mean the total estate taxes due would be **ZERO**, thereby saving the heirs \$500,000 in estate taxes.

## What are the estate tax exemptions through 2011 (unless Congress acts to change them)?

Exemptions and Maximum Tax Rates		
Year	Estate Tax Exemption	Highest Rate
2005	\$1.5 million	47%
2006	\$2 million	46%
2007	\$2 million	45%
2008	\$2 million	45%
2009	\$3.5 million	45%
2010	N/A (taxes eliminated)	0%
2011	\$1 million	55%

## What should A&B trusts cost?

### Size of the estate Cost

Up to 3 million \$2,750  
3 to 5 million \$3,500  
5 to 10 million \$5,000  
10 to 25 million \$7,500  
over 25 million \$10,000

We get upset when we hear that clients have paid \$25,000-\$50,000 or more for estate plans. Unless your estate is over 15 million dollars, you should be able to get an entire estate plan for less than \$15,000. If your estate is less than \$5,000,000, you should be able to get an entire estate plan done for around \$5,000. (That does not include a lot of specific asset protection planning or advanced planning with FLPs).

Attorneys very rarely will reinvent the wheel when it comes to estate planning. If you read this material carefully, you will know as much about the basics of estate planning as your attorney does; and we can state with confidence that you will know as much or more about advanced tax planning than most of the local attorneys and CPAs in your city.

If you are wondering why estate plans can get costly when the same shell documents are used over and over, it is because of the lingering liability with the estate plan. The malpractice liability for estate planning attorneys does not go away until you die, which could be 50+ years for some clients.

## **Revocable**

A&B trusts are revocable trusts. It is very common for an attorney to set up A&B trusts and not put anything in the trusts. We would say that 90% of the A&B trusts out there are not funded correctly. We suggest funding them with something when you implement them. It is very typical to transfer the family residence into the trusts. If, for whatever reason, clients want to take assets out of their trusts it is not a problem since the trusts are revocable (we will discuss irrevocable trusts in an upcoming section).

## **Conclusion**

We know it is a strong statement, but EVERYONE with any amount of assets should have A&B marital/living/revocable trusts (or just a single trust if you are not married) to avoid probate and maximize the estate tax exemptions. It is just that simple. If you do not have A&B trusts, you are doing your heirs a tremendous disservice and eventually will make the federal and possibly state government very happy at your death.

We advocate that you purchase a will at your earliest convenience.

To purchase a will by a pre-certified attorney, please contact us and we will help facilitate the process.