

SUMMARY OF DISCLAIMER TRUST OPTION

Married couples do not *automatically* get two exemptions from the federal estate tax. They must *do something* to get two exemptions. Recent law provided a new method that married couples can use to obtain two exemptions from the federal estate tax: portability. There are both pros and cons of obtaining two exemptions by making the portability election.

The traditional method used by married couples to obtain two exemptions from the federal estate tax was to set up and fund a "Bypass Trust" on the death of the first spouse. If the Wills (or Living Trust) created by a married couple give the surviving spouse an *option* to create a Bypass Trust on the first spouse's death, the device used to exercise that option is called a "disclaimer." Wills of that type are usually referred to as "disclaimer Wills" or "optional Bypass Trust Wills." In addition, a Bypass Trust created this way is often called a "Disclaimer Trust." The idea of this estate plan is to allow the surviving spouse to shelter some of the assets owned by the first spouse to die from estate taxes on the surviving spouse's death and also to provide certain other benefits that trusts provide, which outright ownership does not provide (such as creditor protection). Thus, a Disclaimer Trust is a type of "Bypass Trust" that is created in a different way from a standard ("automatic") Bypass Trust, which is usually created via a tax formula.

A surviving spouse has 9 months from the date of the first spouse's death to decide whether to forego keeping some or all of the assets the deceased spouse leaves to him/her and, instead, have some or all of those assets pass into the Disclaimer Trust. Both gifts made to the surviving spouse in the Will and gifts made to the surviving spouse outside the Will (such as IRAs passing to the spouse by beneficiary designation) can be "disclaimed" so that they pass into the Disclaimer Trust. However, the Internal Revenue Service takes the position that if, after the death of the first spouse and before the 9 month period has ended, the surviving spouse re-titles any assets into his/her individual name, then that action by the surviving spouse eliminates the disclaimer option for those re-titled assets. Thus, the surviving spouse should be careful not to accidentally foreclose the disclaimer option by acting too quickly after the death of the first spouse. Nine months is usually sufficient time to make an informed decision regarding the disclaimer option.

If the estate tax exclusion amount (or, exemption) is greater than the value of a married couple's combined estate at the time of the first spouse's death, the surviving spouse may not need to exercise the disclaimer option. The exclusion amount for 2019 is \$11,400,000 per the Tax Cuts and Jobs Act passed in December 2017. (That amount will change in future years due to inflation adjustments. However, in 2026 the exclusion amount will revert back to \$5 million, adjusted for inflation.) On the other hand, if the surviving spouse will end up having an estate larger than **one** exemption amount, the disclaimer option is one option that should be considered to avoid a 40% estate tax on everything above one exemption amount when the surviving spouse dies. Assets held in a Disclaimer Trust are also protected from creditors' claims (such as a tort creditor who sues the surviving spouse for personal injuries and obtains a judgment against him/her). Finally, the assets in the Disclaimer Trust will pass to the couple's children on the death of the surviving spouse, rather than to a new beneficiary selected by the surviving spouse (such as his/her new spouse).