

AVOIDING \$100,000 IN NEW YORK STATE ESTATE TAXES
(AND POSSIBLY \$400,000 IN FEDERAL ESTATE TAXES)
THROUGH THE USE OF NEW YORK ESTATE TAX EXEMPTION TRUSTS

by Neil R. Lubarsky, Esq.

Does your will leave everything to your spouse if your spouse survives you? When you and your spouse add together the value of all of the items included in your taxable estates, including your house, your investments, your pension plan or IRA balances, and the full amount of death benefits payable under your life insurance policies, does the total figure exceed \$1,000,000? If the answer to the two questions posed above is yes, you will be exposing your family to a substantial amount of unnecessary New York State estate taxes which can be avoided by changing your will.

Let us look at the following example involving Mark and Linda, a married couple, who have wills leaving everything to the surviving spouse. Such wills are commonly known as "all to spouse" wills. Assume that Mark and Linda own a house worth \$1,000,000, and own investment assets worth \$1,000,000, giving them a taxable estate of \$2,000,000. If Mark, upon his death, left all of his assets to Linda, and Linda subsequently died owning the couple's house and investment assets, leaving a taxable estate of \$2 million, Linda's estate would have to pay approximately \$100,000 in unnecessary New York State Estate taxes.

The reason for Linda's substantial tax exposure is that the New York State estate tax exemption, the amount which she can leave free of New York State estate tax to her children, is limited to only \$1,000,000. Every dollar in excess of such \$1,000,000 amount which Linda leaves to her children is subject to New York State estate tax. Since Linda died with a taxable estate of \$2 million, the second \$1,000,000 left to her children is subject to New York State estate taxes in the amount of approximately \$100,000. In fact, because of the unorthodox manner in which the New York State Estate tax is structured, a couple with as little as \$1,100,000 in combined assets and life insurance would be subject, without, any estate tax reduction planning, to \$38,000 of unnecessary New York State estate taxes.

Had Mark and Linda properly planned their \$2,000,000 estate, the \$100,000 of estate taxes which they faced could have been avoided. By changing their "all to spouse" wills, in one of the ways described below, and by dividing their assets equally between themselves, Mark and Linda could have avoided ever having to pay this \$100,000 of New York State estate taxes to the government,

thereby passing on an additional \$100,000 to their children.

One method of changing "all to spouse" wills in order to minimize estate taxes, is for Mark and Linda to each leave, upon death, their one-half share of the couple's assets, directly to their children. This approach, however, is often undesirable from the perspective of the surviving spouse, who usually wants to continue to control all of the couple's assets, and who may need to receive the income generated by all of the couple's assets in order to live comfortably.

Fortunately, there is another method of changing "all to spouse" wills which meets the needs of the surviving spouse for control and income while at the same time minimizing the family's estate tax liability.

The solution involves the use of wills containing "estate tax exemption trusts". Under such a plan, assets of the first spouse to die are placed in a trust. During the life of the surviving spouse, the surviving spouse can control the investment of the trust assets. All of the income generated by the assets in the trust is ordinarily paid to the surviving spouse. If desired, the surviving spouse can be given the right to pull additional amounts of assets out of the trust. If a house is placed in such trust, the surviving spouse can be given the right to live in such house for the rest of his or her life without interference and without having to pay any rent.

When the surviving spouse ultimately passes away, all of the assets in the "estate tax exemption trust" pass directly to the couple's children or other beneficiaries without any estate tax being imposed on these assets. The use of wills containing "estate tax exemption trusts", as opposed to the use of "all to spouse" wills, ordinarily results in a family avoiding approximately \$100,000 dollars of New York State estate taxes which would otherwise have to be paid to the government, and may also lead to the legal avoidance of federal estate taxes.

The newly enacted Federal Estate Tax Law allows, for people dying during the 2011 and 2012 years, a \$5,000,000 exemption per person, and has provisions allowing, under some circumstances, a surviving spouse to additionally use the unused estate tax exemption of the first spouse to die. As a result of the current federal estate tax exemption, if Mark and Linda both died in 2011 or 2012, they would not pay any federal estate tax, regardless of how their Wills were structured. The Federal Estate Tax Exemption, however is currently slated to drop to only \$1,000,000 per person after December 31, 2012. If either of Mark and Linda die after December 31, 2012, which is a likely scenario, and there are no further changes in the law, the estate tax exemption trust discussed above

would end up saving the couple approximately \$400,000 in federal estate taxes.

An additional benefit of having a will containing an "estate tax exemption trust" rather than an "all to spouse" will involves the protection that wills containing certain types of "estate tax exemption trusts" can provide, if specifically drafted for such purpose, against all of the couple's assets having to be spent down on long term care costs. Should Mark predecease Linda, leaving his assets to an "estate tax exemption trust" which was specifically structured with an eye towards protecting family assets against long term care costs, and should Linda later need nursing home care, the assets placed in such a specifically structured trust would not have to be spent on Linda's care in order for Linda to qualify for government assistance.

Neil R. Lubarsky is an estate planning, tax and elder law attorney with offices in Purchase, New York. Mr. Lubarsky is a member of the Bar in both New York and Connecticut, and has been practicing law for 30 years. He can be reached at 914-997-8558.