

Drafting A Marital Deduction Trust For Second Marriages

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Introduction

It is not uncommon for a divorced person or a widow/widower to remarry. For example, if a widow has children from a prior marriage and wants to be sure that her assets will eventually be inherited by her children after her (new) husband dies, the estate planning attorney should not rule out the use of a marital deduction trust for the benefit of the (new) husband.

When designing a marital deduction trust for a second marriage situation where there are children from a prior marriage (or where the widow wants to control who inherits her estate after her (new) husband's death), consider the following eighteen planning ideas.

Checklist of Eighteen Planning Ideas

- 1) Consider using a qualified terminable interest ("QTIP") marital deduction trust for the benefit of the surviving spouse. See, Internal Revenue Code ("IRC") section 2056(b)(7).
- 2) Consider giving the surviving spouse a discretionary (or ascertainable standard, such as "health, education, support and maintenance") interest in the QTIP marital deduction trust principal.
- 3) Consider establishing an *intervivos* QTIP trust for the less wealthy spouse, with the wealthier spouse having a successive life interest in the *intervivos* QTIP after the less wealthy spouse dies. See, IRC section 2523(f).
- 4) Consider a reverse QTIP election for the marital deduction trust if the deceased spouse has "excess" unused generation skipping transfer ("GST") tax exemption available at his or her death. See, IRC section 2652(a)(3).
- 5) If local law permits, consider a unitrust definition of marital deduction trust income. A unitrust will provide the surviving spouse with a an annual income interest that is based on a fixed percentage of the trust's overall value. See, IRC section 643(b).
- 6) If local law permits, consider giving an independent trustee the power to adjust between marital deduction trust income and principal in order to ensure that the surviving spouse receives a threshold level of income when equity values are "booming" and fixed income investment rates are "down."

- 7) Consider having IRA benefits paid to the QTIP marital deduction trust rather than outright to the surviving spouse. See, Revenue Ruling 2006-6, 2006-22 Internal Revenue Bulletin 939 (5/4/2006).
- 8) Consider permitting the surviving spouse to live rent free in the marital home if it is an asset of the marital deduction trust or the credit shelter trust.
- 9) Consider having the QTIP marital deduction trust stub income be paid to the estate of the surviving spouse rather than to the QTIP marital deduction trust remainder beneficiaries.
- 10) Consider having the QTIP marital deduction trust reimburse the surviving spouse's estate for the cost of valuing QTIP marital deduction property that is included in the surviving spouse's gross estate under IRC section 2044.
- 11) Consider granting the surviving spouse a testamentary limited power of appointment over the QTIP marital deduction trust. The class of appointees can be limited to the deceased spouse's descendants. This will permit the surviving spouse to maximize the utility of the reverse QTIP marital deduction trust election and the GST tax predeceased parent rule, due to unforeseen or changed circumstances occurring after the death of the first spouse. For example, the surviving spouse could appoint the reverse QTIP marital deduction trust property to a trust for the deceased spouse's grandchildren and more remote descendants who are skip persons, and the surviving spouse could appoint the non-GST-tax-exempt marital trust property to the deceased spouse's children and grandchildren who are non-skip persons (due to the predeceased parent rule).
- 12) Consider giving the surviving spouse an annual 5×5 right of withdrawal over the non-GST tax exempt QTIP marital deduction trust. See, IRC section 2514(e).
- 13) Consider having the surviving spouse not waive his or her right to recover estate taxes under IRC section 2207A attributable to QTIP property if the QTIP remainder beneficiaries are not the descendants of the surviving spouse.
- 14) Consider giving the surviving spouse a discretionary interest (income and/or principal) in the credit shelter trust using an independent trustee, i.e., a trustee who is not related or subordinate to either spouse. See, IRC section 672(c).
- 15) Consider giving the deceased spouse's children a discretionary interest in the income and/or principal of the credit shelter trust using an independent trustee. This technique is helpful if the surviving spouse is close in age to the grantor's children or if the surviving spouse is significantly younger than the deceased spouse, and the children will have to wait significantly longer to receive their inheritance but for their much younger step-parent.
- 16) Consider giving the trustee of the credit shelter trust the discretionary authority to pay the surviving spouse's funeral expenses if he or she dies impecunious.

Drafting Example: “Trustee Power to Pay Beneficiary’s Funeral and Burial Expenses. If, on the death of any current trust beneficiary, there shall be insufficient property in such beneficiary’s own probate estate or revocable living trust estate to pay his or her proper funeral and burial expenses (including the cost of transporting the remains and a suitable marker at his or her grave) and other satisfactory provisions have not been made (or are available) for the payment of such expenses, then Trustee may, in its sole discretion, pay all such charges out of the principal of the trust estate from which such beneficiary was entitled to receive distributions; provided however, no payment shall be made from the proceeds (or income therefrom) of life insurance owned by the trust that insures the life of such (now deceased) current trust beneficiary. Absent extraordinary circumstances, the maximum amount Trustee may pay hereunder (excluding the cost of transporting the remains) shall be fifteen thousand (\$15,000) dollars, adjusted for the cost-of-living. Trustee shall not pay funeral and burial expenses from tax favored retirement plan benefits. With regard to a disabled or handicapped beneficiary of a discretionary spendthrift trust or special needs trust, Trustee shall make no payments for funeral and burial expenses if Trustee shall determine in its sole, absolute and uncontrolled discretion that such payment is the obligation of any public or private agency.”

17) Instead of referring to the surviving spouse by his or her given name through the trust document, consider using the term “my Spouse” to refer to the named spouse but also state in the definition of “my Spouse” that the term does not include the named spouse if there is a divorce, legal separation, etc., and that any trusteeship, powers of appointment, durable powers of attorney, health care advocates, etc. are automatically canceled with respect to the named spouse if there is a divorce, legal separation, etc.

18) Coordinate each spouse’s estate plan with the terms and requirements of the prenuptial agreement, if any. Even in the absence of a prenuptial agreement, the spouses may want (and agree to) each spouse having a separate stand alone living trust (in addition to a married couple’s living trust for the benefit of one another and their descendants) to hold his or her premarital or separate property for the benefit of that spouse’s descendants (and not for the benefit of the surviving spouse) - a “poor man’s” form of postnuptial agreement.

Conclusion

In a second marriage situation where a spouse wants to provide for his or her surviving spouse, there are numerous ways to accomplish this objective while at the same time obtaining a marital estate tax deduction and assuring that the deceased spouse’s property will be distributed to whom he or she desire when the surviving spouse dies.

This article is excerpted and adapted from Chapter 12 of Sebastian V. Grassi, Jr, *A Practical Guide to Drafting Marital Deduction Trusts (with Sample Forms and Checklists)* published by ALI-ABA (800) 253-6397 (<http://www.ali-aba.org/aliaba/BK36.asp>)