

Date: April 1, 2014

NOTICE TO CLIENTS WITH "A/B" TAX PLANNING TRUSTS

I hope you are doing well and ready to enjoy a long overdue spring! Looking at your file, you established what we call A/B trusts for each of you to maximize potential estate tax savings. In the meantime, there have been substantial changes in federal estate tax laws that may make your A/B trusts obsolete depending on the value of your combined estates.

The changes are relatively complicated to explain, but in simplified terms, if your combined estates are worth less than double the current applicable unified credit amount it makes sense for you to seriously consider updating your trusts sooner rather than later.

So, what is the applicable unified credit amount? It is the amount a person can leave to anyone without incurring a federal estate tax. That amount as of this year is \$5,340,000, which amount will increase each year to the extent of the increase in the consumer price index. In addition, federal law now provides that if the first to die of a married couple does not use up his or her applicable unified credit amount, as long as his or surviving spouse does not get remarried, and a federal estate tax return is filed for the spouse who dies first, the estate of the second spouse to die can add the unused portion of applicable unified credit amount of the first to die to the applicable unified credit amount available to the estate of the second to die. This is called making the first to dies' unused applicable unified credit amount "portable."

The effect of these changes is that in 2014 a married couple can shelter combined estates worth \$10,680,000 without the necessity of each of them having the A/B trusts you now have; but rather having a single trust for both of you; or making changes to your A/B trusts that would allow the assets of the first spouse to die transfer directly to the surviving spouse so that the combined assets will be taxable in the surviving spouse's estate, if that is desirable under the tax laws applicable as the time of the survivor's death.

The advantage of having all of your assets taxable in the surviving spouse's estate is that all of the assets in his or her estate will get a step-up in income tax basis to their fair market value at the time of his or her death. This means that if the heirs of the estate of the survivor sell capital assets they inherit from the survivor, their capital gains will only be the amount by which those assets have increased in value, if any, since the death of the survivor; rather than how much they have increased in value from when they were originally purchased or inherited by the survivor. This is valuable for two reasons. First, it eliminates large capital gains on assets in the survivor's trust which were purchased or inherited by him or her long ago for much less than they are worth at the time of his or her subsequent death. Second, in your current plan on the death of the first to die, although the assets held in his or her family trust (which will likely contain all of his or her assets, if his or her estate is worth less than \$5,340,000) will be stepped up at that time, they will not get a stepped up basis at the time of the death of the survivor of the two of you. So, making your combined assets taxable at the death of the

survivor of you also eliminates taxation of capital gains on the assets of the first to die, which occur between the death of the first to die and the death of the survivor.

In short, where our goal in the past was the avoidance of estate taxes when the applicable unified credit amount was as low as \$600,000 and the marginal estate tax rate was up to 55% (it's now 40%), under current law the goal has changed to the avoidance of capital gains taxes; provided your total combined estates is below \$10,680.00 (adjusted for inflation).

Accordingly, I strongly recommend that you consider contacting me to go over your current estate plan, and specifically your trusts, to determine if it needs updating to accomplish your goals and to take advantage of the changes in the applicable laws.

I look forward to hearing from you soon.

Sincerely,

Michael L. Wood