

**THE LAW OFFICE OF  
JAMES A. HYATT**  
13220 Executive Park Terrace  
Germantown, Maryland 20874  
Telephone (301) 540-3300  
Fax (301) 540-3309  
jhyatt@estateplanningmatters.com

## **WHY YOUR LIVING TRUST MAY BE OBSOLETE**

Over the last twenty years, Living Trusts have become the most popular form of estate planning. Living Trusts are very effective tools in facilitating most people's estate planning objectives - providing for the management of property in the event of a disability and passing their estates in the most economical fashion. But as we tell our clients, there are many reasons why you should review and sometimes update your Living Trust.

Family dynamics change (for example, births, marriages, divorces, deaths) and sometimes folks change their minds about how they want to leave their property, or about the people they want to handle the administration of their estate or trusts, or who is to be the guardian for their children.

But perhaps the biggest threat to achieving a client's objectives comes from unforeseen changes in the laws (tax and otherwise) that apply to estates and trusts.

When lawyers prepare legal documents we draft them so as to accommodate the laws as they exist at the time. If laws change after documents are signed, those changes may cause significant problems without the client knowing it. Provisions in the documents that were perfect for the laws in effect one year may cause serious problems if those laws change. In those circumstances, the legal documents must be modified to accommodate the changes and bring about the best results.

In the past two years we have seen three law changes that significantly affect virtually all revocable trusts. Accordingly, if you have not reviewed your living trust in the last couple years, there could be serious problems lurking in your estate plan.

This article will briefly explain those three law changes. The first two are linked, so we will deal with them together.

**First**, the federal estate tax exemption amount has increased to \$5 million per person (with an inflation index that has already increased the amount to \$5,430,000). Additionally, a new element of the tax law known as "portability" now makes it much easier for a married couple to utilize both of their exemptions without complex "credit shelter" planning. Under the prior law, such credit shelter trusts (also known as A-B trusts or Bypass trusts) were a critical element of virtually all living trusts for married couples. It is primarily these provisions that are no longer appropriate for most, if not all, married couples because they are no longer necessary to avoid federal estate tax unless the couple's estate exceeds \$11 million.

**Second**, Maryland has also reduced the burden of its own estate tax law. The amount exempt from the Maryland estate tax has been increased to \$1.5 million in 2015 and will increase to \$2 million in 2016, \$3 million in 2017, \$4 million in 2018, and in 2019 will thereafter be

linked to the federal exemption amount. Thus, the Maryland estate tax presents much less a problem and will soon render the credit shelter trust unnecessary.

The bottom line effect of the federal and Maryland estate tax law changes is that the “tax driven” language traditionally used for the past thirty-plus years in most living trusts for married couples is no longer suitable for a couple of reasons. First, the changes in the tax laws now allow many clients to greatly simplify their planning by eliminating the “credit shelter” provisions. This will eliminate the need to maintain two trusts after one spouse dies, and make the surviving spouse’s life much less complicated. Secondly, the existence of the “old” language may actually result in more taxes being incurred by the children at the death of the surviving spouse. This unintended effect is a result of a loss of the “basis step-up” as it applies to the capital gains tax.

Space limitations don’t allow a full and complete explanation of why it is critically important that married couples with Living Trusts take a fresh look at how the tax provisions of the documents are structured. In most cases those provisions are geared towards tax concepts that no longer apply and therefore are obsolete and will bring about a negative result.

It should be noted that there are non-tax reasons why married couples will want to maintain separate trusts with provisions that will keep the first-to-die spouse’s assets in a continuing trust. These non-tax reasons include protection from a second marriage, creditor protection and asset protection in the event of dementia, Alzheimer’s, etc. But in those cases where what I call “Family Wealth Preservation” is desired, a type of “marital trust” rather than a credit shelter trust will usually achieve far greater tax results.

**Third**, the new Maryland Trust Act, implemented this year, significantly revamped Maryland law. For one thing, the Act creates some new duties and responsibilities on the part of Trustees, including notice requirements to future beneficiaries. Additionally, the new Trust Act allows clients to include special provisions that can override the statutory provisions, thus providing greater flexibility that can make it easier for your heirs. In other words, due to some of the aspects of the new Act, some of the “boilerplate” provisions of the trusts drafted before the Act went into effect should be re-examined.

The “maintenance” of any estate plan is always essential – just like oil changes are essential for your car. But with the recent law changes we have seen in the past two years, it is even more important that planning is kept current.

If you have a Living Trust, and would like to see if it continues to suit your needs, please feel free to give my office a call.



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[www.estateplanningmatters.com](http://www.estateplanningmatters.com)