



QTIP TRUSTS: ESTATE PLANNING AND REMARRIAGE

Estate planning for couples often should consider the possibility of remarriage, either through divorce or death. One valuable tool for this contingency is called a qualified terminable interest property trust—QTIP for short.

Here's a common situation where a QTIP might be appropriate. Jane and John are married, with one child. John has another child from a previous marriage. If John dies first, his property would pass to Jane free of estate tax under the unlimited marital deduction. But John has a concern. As much as he loves and trusts Jane, he's concerned that when she dies she may pass all of the property she inherited from him, along with her own property (minus any estate taxes), to the couple's child, leaving the child from John's previous marriage without anything. Or consider a scenario in which Sam marries a woman 20 years younger. The younger spouse might remarry following Sam's death, and ultimately Sam's assets, passed to his wife at his death, could end up in the hands of her husband or children from the second marriage.

That's where a QTIP can come in. Let's break down this mouthful of a phrase. A qualified terminable interest property trust is "qualified" because assets placed in the trust qualify for the unlimited marital deduction as long as the trust meets two major requirements. First, all income generated by the assets held in the trust must be paid out at least annually to the surviving spouse for the life of the spouse. Second, no one can have the power to appoint any trust property to benefit anyone other than the surviving spouse during his or her lifetime. If these requirements are not met, then the property passed into the QTIP won't qualify for the marital deduction and would face potential estate taxes.

"Terminable interest" means the surviving spouse cannot control the property in the QTIP and their interest in the property ends at their death.

In our example, John could use other trust arrangements, such as a credit shelter trust, which would kick off income to Jane during her lifetime, yet ensure that John's property eventually goes to his child from a previous marriage (as well as his child with Jane, if he chooses). However, a credit shelter trust won't shelter from estate taxes property that exceeds the exemption amount

(\$650,000 in 1999), while a QTIP is able to make use of the marital deduction and postpone all estate taxes until the surviving spouse dies.

In some situations, it may be beneficial to use a combination of trusts. A credit shelter trust would receive property up to the amount of the deceased spouse's estate tax exemption (\$650,000 in 1999), then the remainder of the property, or a portion of the remainder, could go into the QTIP. The trust also can be written in such a way that it is able to hold on to the assets for a while in the event the beneficiaries are still young at the time of the surviving spouse's death.

Qualified terminable interest property trusts are generally irrevocable, meaning they cannot be revoked once property is placed in the trust. A QTIP can be set up so that the surviving spouse has access to some of the principal, though that's not a requirement.

Funding a QTIP trust with assets from retirement accounts, such as an IRA or a qualified plan, is a trickier problem. Some observers suggest that these accounts should never be used to fund a QTIP. Others say they can, but you have to be sure that all income generated by the accounts are paid into the QTIP. Otherwise, retirement money put into the QTIP would be disqualified for the marital deduction and potentially be subject to estate taxes.

While QTIPs are most commonly used by couples with children from current or previous marriages, they can work for childless couples. For example, each partner might want to ensure that some of their estate goes to their side of the family, such as siblings or nephews.

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