

Credit Shelter and Marital Trusts

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Key Takeaways

- High-net worth individuals and families often want to minimize or avoid estate taxes when transferring wealth. For married couples who want to structure how their wealth is transferred, a combination of credit shelter and marital trusts may be appropriate.
- Although these trusts are most appropriate for married couples with estates larger than the current lifetime gift and estate tax exemption amount (\$27.22 million in 2024), many more couples may benefit from these trusts starting in 2026 when the exemption amount is expected to be drastically reduced.
- In addition to estate tax minimization, these trusts may help achieve other estate planning goals, such as leaving assets to children from a prior marriage and protecting a vulnerable surviving spouse from financial fraud.
- By electing “portability,” surviving spouses can fully utilize their deceased spouse’s estate tax exemption by possibly creating and funding a credit shelter trust or transferring the deceased spouse’s unused exemption amount to themselves for later use.

Overview

Various trust structures are often used in estate planning to help high-net worth individuals and families minimize estate taxes and achieve broader wealth transfer goals. One strategy is to use credit shelter and marital trusts as a foundation to a high-net worth estate plan. Used together, these two trusts are sometimes referred to as an A/B trust. While credit shelter trusts can help reduce federal or state estate taxes upon the first spouse’s death, marital trusts can allow assets to move to a spouse tax-free, and in certain circumstances, can be used to ensure children from a previous marriage are not disinherited.

The federal lifetime estate tax exemption (\$27.22 million for married couples in 2024) is expected to be cut by half on January 1, 2026, when provisions of the Tax Cuts and Jobs Act of 2017 are [scheduled to sunset](#). As a result, credit shelter and marital trusts may become appropriate for more couples, particularly those with net worth between \$10 million and \$20 million, as they seek ways to reduce estate taxes. High-net worth individuals and families should consider speaking with their advisory team now to determine how best to prepare for the change in the lifetime exemption amount, given their personal circumstances.

Credit Shelter Trusts

A credit shelter trust (CST), also known as a bypass trust or a family trust (see more below), is an irrevocable trust that potentially allows an individual to transfer assets to their beneficiaries without incurring estate taxes. These trusts are often created at the death of the first spouse in their will or revocable trust.

Typically, the trust is funded with an amount equal to the amount of assets that an individual can pass to their beneficiaries without incurring estate taxes – usually an individual’s federal lifetime estate tax exemption (in 2024, \$13.61 million for individuals and \$27.22 million for married couples, less any gifts they made during their life that used part of their exemption). Thus, as the name implies, one of the primary purposes of a CST is to shelter the remaining estate tax exemption for use against the estate tax at the first spouse’s death.

In a CST, the assets typically are held in trust until the death of the surviving spouse, who, generally, is granted a limited power of appointment over the trust assets. A limited power of appointment allows the surviving spouse to make limited adjustments to the estate plan to accommodate changing circumstances and family finances. It also keeps the assets from being included in the surviving spouse’s estate since they are unable to name themselves, their estate, or creditors as beneficiaries.

While the provisions of a CST can vary, they typically allow for income distributions to the surviving spouse either through mandatory or discretionary distributions. The principal of the trust is usually not accessible to the surviving spouse unless the marital trust assets have been fully exhausted (see more below). And the level of access the surviving spouse has to the trust principal varies depending on the provisions of the trust as set by the grantor.

A CST can also be funded during one’s lifetime. This kind of trust is often called a family trust, as these trusts typically provide benefits for both the surviving spouse and children. Assets used to fund a family trust, including all future appreciation and income, are removed from the grantor’s taxable estate, typically resulting in a substantial estate tax reduction. Keep in mind that trusts are subject to condensed income tax brackets, which should be considered when using trusts in estate planning.

State estate taxes. Credit shelter trusts are also used for those who do not have a federal estate tax liability

A marital trust is often used instead of an outright transfer when the surviving spouse lacks the ability to manage his or her own finances or may be susceptible to frauds or scams.

but face state estate taxes because they live in states that impose an estate tax and where the exemption for state estate taxes is substantially lower than the federal exemption limit. The following states have their own state estate tax exemptions at or below the federal exemption limit: Connecticut, District of Columbia, Hawaii, Illinois, Maine, Maryland, Massachusetts, Minnesota, New York, Oregon, Rhode Island, Vermont, Washington. Residents of these states who have asset values near, at, or above the state estate tax exemption limit should consult their advisory team on whether CSTs are appropriate for their situation.

Marital Trusts

A marital trust, also known as a spousal trust, is an irrevocable trust that allows an individual to transfer assets to their spouse without incurring estate taxes by utilizing the “unlimited marital deduction.” The unlimited marital deduction is a provision in the estate tax code that allows an individual to pass an unlimited amount of assets to their surviving spouse estate tax free, whether in trust or outright. A marital trust is often used instead of an outright transfer when the surviving spouse lacks the ability to manage his or her own finances or may be susceptible to frauds or scams. By having the assets owned in trust, you provide another layer of security to prevent a loved one from being taken advantage.

The assets of the marital trust become part of the surviving spouse’s estate, which is why it is common practice for the credit shelter/marital trust documents to require that all the assets of the marital trust be spent before access to the credit shelter trust is granted. This forces the marital trust, which is not necessarily shielded from estate taxes (depending on the surviving spouse’s remaining estate tax exemption),

to be used for the maintenance and support of the surviving spouse while safeguarding the assets of the credit shelter trust, which are generally shielded from estate taxes at the second spouse's passing.

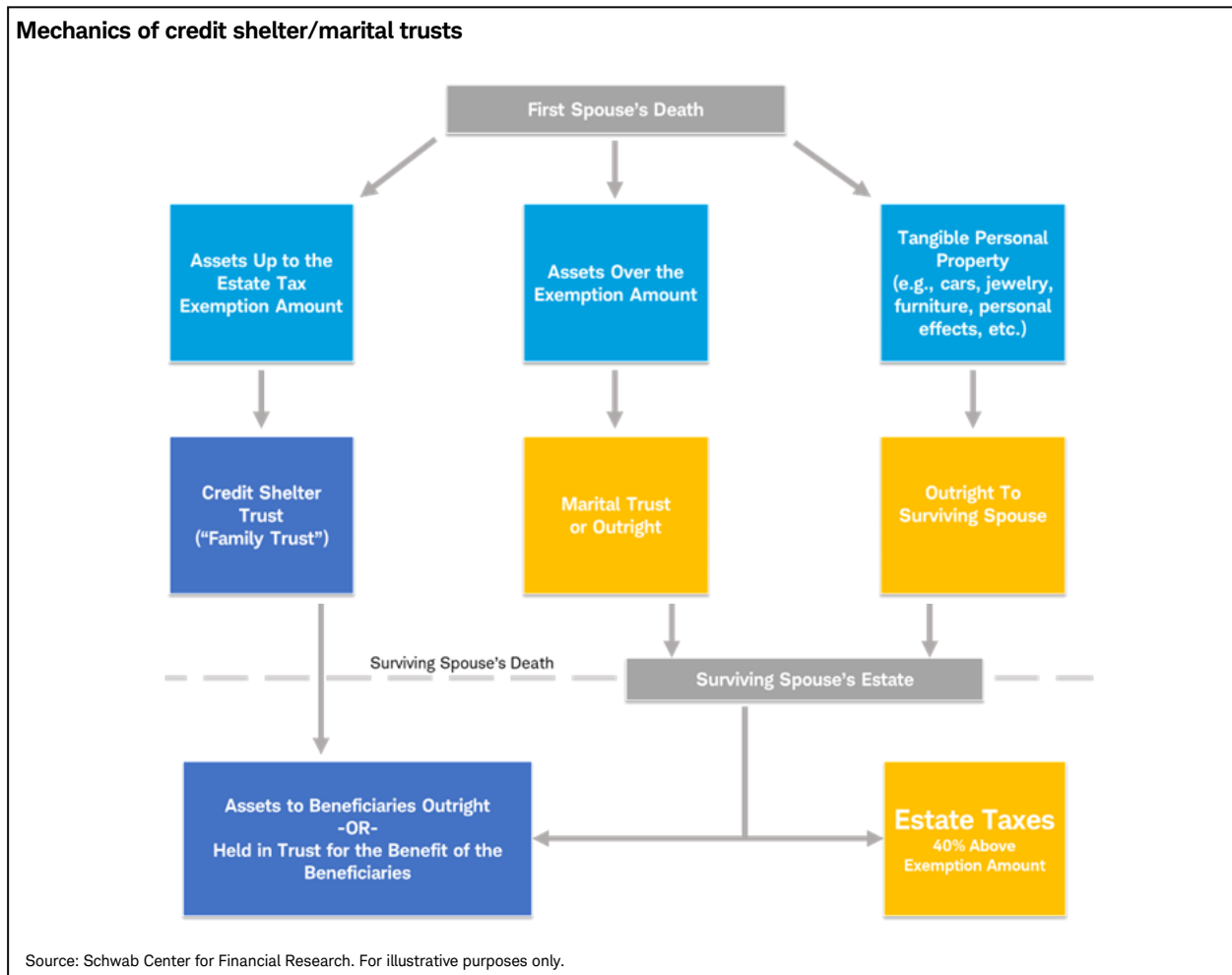
In the case of blended families, where a spouse wants to ensure that upon the second-to-die spouse's death, assets transfer to children from a prior marriage, a qualified terminable interest property (QTIP) trust may be preferable. These trusts are a variation of the standard marital trust in that they both qualify for the unlimited marital deduction for estate taxes, but unlike a standard marital trust that typically gives the surviving spouse the ability to appoint who receives the trust assets after they die, a QTIP allows the creator of the trust (the deceased spouse/grantor) to irrevocably determine who the final beneficiaries of the trust are, once the surviving spouse dies. This helps ensure that legacy planning for the children from a prior marriage is accomplished per the wishes of the first-to-die spouse.

To qualify as a QTIP, the trust must only benefit the surviving spouse during their lifetime, the surviving

spouse must be a U.S. citizen, and all the income the trust generates must be paid to the surviving spouse, at least annually (the trust principal is distributed at the trustee's discretion, depending on the trust provisions).

Portability

For married couples, portability allows the deceased spouse's unused exemption (DSUE) amount to transfer to the surviving spouse. This helps alleviate any unused exemption amount at the first spouse's passing, and provides for greater, real-time flexibility in the estate planning process. For example, if you died today while married and had no prior taxable gifts, you would have \$13.61 million in unused exemption to transfer to your surviving spouse that he or she could use to shelter estate and gift taxes during their life or at death. Being able to elect portability and transfer unused exemption amounts between married couples has diminished the use of credit shelter trusts when estate tax minimization is the *only* estate planning goal.



Note: To transfer the DSUE amount to the surviving spouse, a proper portability election must be made on Form 706 (estate tax return), within five years of the decedent's date of death.

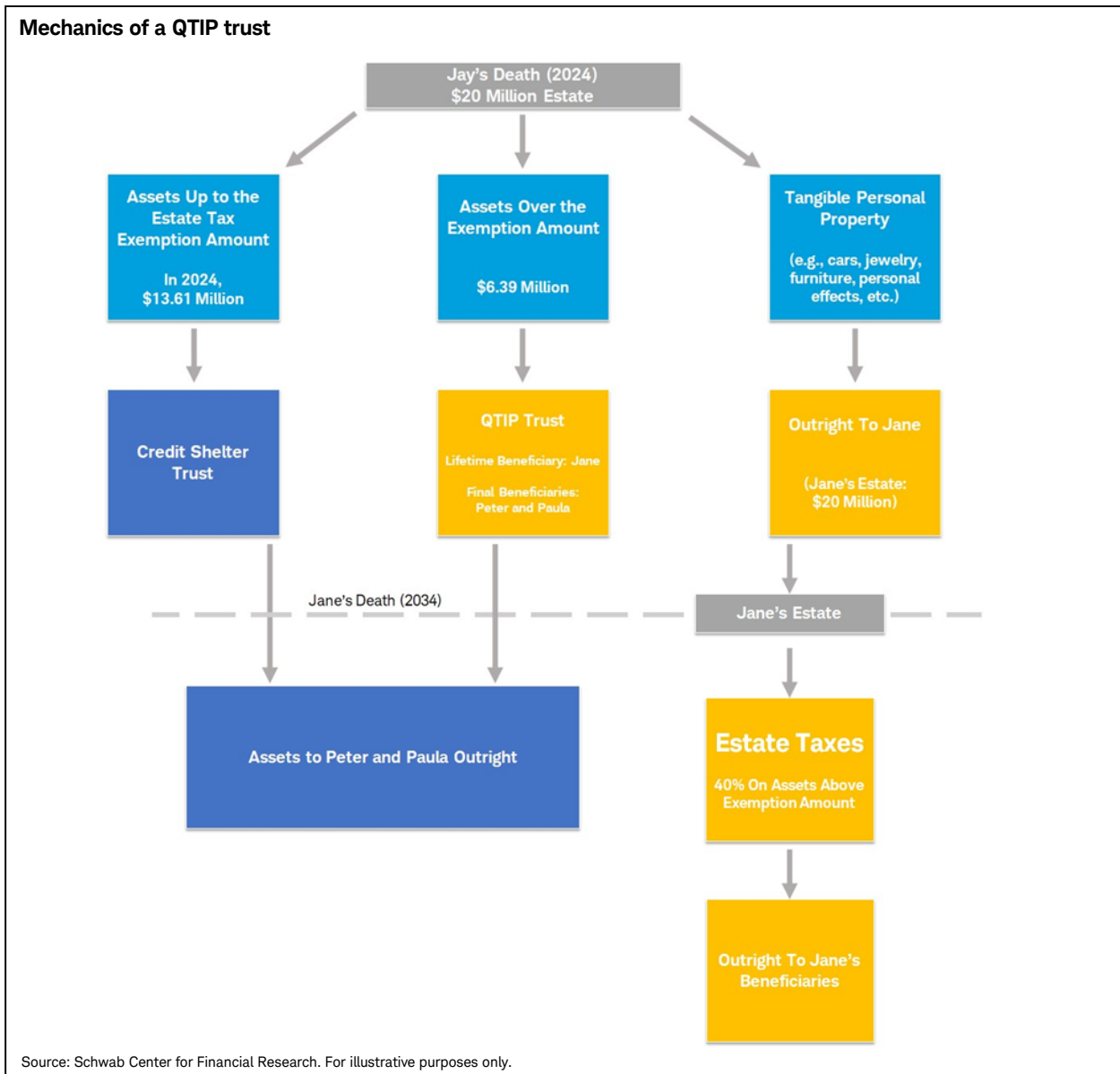
Example: QTIP trust

Jay and Jane are married with a combined net worth of \$40 million. Jay was previously married and has two children, Peter and Paula, from that marriage. Jane was not married prior to marrying Jay.

Jay wants to ensure that their assets are used to take care of Jane for her life and that, upon Jane's death, all remaining assets pass to Peter and Paula, his children from his first marriage. To that end, Jay created a credit shelter and QTIP trust as a part of his estate plan.

In 2024, Jay passes away. Upon his death, Jay's trustee funds the credit shelter trust with an amount of assets equal to Jay's remaining unused exemption amount. Since Jay had no prior taxable gifts, his exemption amount is equal to the full 2024 estate tax exemption amount, \$13.61 million. All assets above that amount fund the QTIP trust, which utilizes the unlimited marital deduction to ensure that no estate taxes are due upon Jay's death.

Jane lives an additional 10 years, during which the QTIP trust makes quarterly distributions of the net income of the trust to help maintain and support her. Upon Jane's death, the assets remaining in the both the credit shelter and QTIP trusts are distributed outright to Peter and Paula.



Example: Portability

What if Jay was never married prior to Jane, and Peter and Paula are the offspring of Jay and Jane? Instead of funding a credit shelter trust upon Jay's death, if Jay's estate planning documents allow for it, Jay's executor could timely elect portability on the estate tax return and "port" over Jay's \$13.61 million dollar exemption to Jane, for her to use in addition with the exemption she has available to her at the time of her death, which in 2034 is estimated to be about \$10.5 million.¹ In this scenario, the credit shelter trust is not funded, Jay's entire estate passes outright to Jane utilizing the unlimited marital exemption, and Jane's estate has \$24.11 million of exemption to utilize against the estate tax.

Bottom line

Credit shelter and marital trusts make up the foundational documents for a married couple's estate plan where estate taxes need to be minimized and other goals need to be met. Using trusts in estate planning involves the interplay of laws, taxes, and, most importantly, the goals of the individual or family. Therefore, consult with a wealth advisor and estate planning attorney before implementing any strategies.

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Endnote

1. Assuming the estate tax exemption amount reverts in 2026, under the sunset provisions of the Tax Cuts and Jobs Act of 2017 and 5% inflation.

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As Director of Estate, Trust, and High-Net-Worth Tax for the Schwab Center for Financial Research, Austin provides analysis and insights on topics including complex estate, gift, and trust planning, advanced charitable strategies, business succession, and executive compensation.

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