USE OF DISCLAIMERS IN GIFT TAX, ESTATE TAX, GENERATION-SKIPPING TRANSFER TAX AND INCOME TAX POST-MORTEM PLANNING

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I. BACKGROUND

A. *Historical Development*

The concept of a disclaimer is that a beneficiary, heir, holder of a power or other recipient of a property interest may refuse to accept the transfer. The refusal is called a "disclaimer" under Internal Revenue Code (I.R.C.) § 2518 and California Probate Code section 260.[1]

Section 2-801 of the Uniform Probate Code (UPC) has provided for a refusal to accept a transfer since 1974. Such a refusal originally was called a "renunciation" under the UPC. Since 1990, UPC section 2-801 has called the refusal to accept a transfer a disclaimer; and the disclaimed property or interest passes as if the disclaiming person had predeceased the decedent.[2] Many states follow this pattern.

The federal law on disclaimers was clarified by the Tax Reform Act of 1976, which added I.R.C. § 2518.[3]

B. *Reasons for Doing Disclaimers*

1. *To save taxes*

a. To fully utilize the unused portion of a decedent's $600,000 unified credit exemption equivalent;
b. To qualify for (salvage) the marital deduction in an estate of the first spouse to die;
c. To pass property to a "qualified heir" and thus qualify for special use valuation under I.R.C. § 2032A;[4]

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1. *See* 26 U.S.C. § 2518 (1994); CAL. PROB. CODE §§ 260-334 (West 1991). (I.R.C. § 2046, in the chapter on estate tax, simply incorporates the disclaimer provisions of I.R.C. § 2518, which appears in the chapter on gift tax.)

2. *See* UNIF. PROBATE CODE § 2-801 (1993).

3. *See* 26 U.S.C. § 2518 (1994).

4. *See* 26 U.S.C. § 2032A (1994). *But see* Tech. Adv. Mem. 81-46-020 (July 3, 1981) (regarding pitfalls to be avoided); Estate of Thompson v. Commissioner, 864 F.2d 1128 (4th Cir. 1989); Estate of Clinard v. Commissioner, 86 T.C. 1180 (1986)(invalidating one of the requirements of Estate Tax Regulation section 20.2032A-8(a)(2)).

d. To decrease the amount of property passing to the surviving spouse (decrease marital) and thereby:

(i) avoid estate tax at the second death on future appreciation; and

(ii) avoid estate tax on "bracket creep" at the second death by removing value at the upper margin;

e. To qualify for, increase or accelerate an estate tax charitable deduction;

f. To fully utilize a decedent's $1,000,000 Generation-Skipping Transfer Tax (GST) exemption;

g. To qualify for a residential "rollover" under I.R.C. § 1034, or the "over 55" $125,000 exclusion for the survivor spouse (who must be owner);[5]

h. To qualify for six-month alternate valuation. Because an alternate valuation must reduce estate tax as well as the gross estate[6], even a modest disclaimer in a zero tax estate will suffice;

i. To avoid a gift tax on what is, in economic effect, the equivalent of a lifetime transfer by the disclaimant.

2. *Non-tax reasons*

a. To restructure a will or trust;

b. To pass assets to younger generations after post-death situation is known;

c. To avoid restrictions on holding S corporation stock if a trust is not a qualified subchapter S trust (QSST).[7] The 1996 Small Business Tax Act also allows a "small business trust" for tax years after 1996.[8]

d. To attempt to insulate against disclaimant's creditors. The problem is whether a disclaimer is a fraudulent conveyance. The authorities are split:

(i) *In re Atchison,* applying Illinois law, found that a disclaimer does not constitute a "transfer" for purposes of the Bankruptcy Code and denied the Bankruptcy Trustee's attempt to recover the disclaimed property;[9]

(ii) The U.S. Bankruptcy Court for the Western District of Texas, *In re Brajkovic,* vehemently disagreed with the Seventh Circuit's opinion in *Atchison,* found that the disclaimer was a transfer, and allowed the Trustee in Bankruptcy to recover it.[10] But the later opinion of the Fifth Circuit, also applying Texas law, specifically declined to follow the district court's

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5. *See* 26 U.S.C. § 1034 (1994).

6. *See* 26 U.S.C. § 2032(c) (1994).

7. *See* Priv. Ltr. Rul. 88-25-055 (Mar. 23, 1988).

8. The Small Business Job Protection Act of 1996, Pub. L. No. 104-188, § 1302(a), 1996 U.S.C.C.A.N. (110 Stat.) 1777 (to be codified at 26 U.S.C. § 1361(c)(2)(A)(v)).

9. Jones v. Atchison (*In re* Atchison), 925 F.2d 209, 212 (7th Cir. 1991).

10. Lowe v. Brajkovic (*In re* Brajkovic), 151 B.R. 402, 407-09, 411-12 (Bankr. W.D. Tex. 1993).

opinion in *Brajkovic,* and held that a disclaimer made before the disclaimant filed bankruptcy was *not* a transfer.[11]

(iii) In *Hoecher v. United Bank of Boulder* the Tenth Circuit reached the same conclusion as the Seventh and Fifth Circuits; that the disclaimer was not a "transfer;"[12]

(iv) *In re Watson,* held a disclaimer was an avoidable transfer made within 180 days of the filing of the bankruptcy petition.[13] *Query* whether this would be followed now in light of contrary results in three circuit courts.

(v) The North Dakota Supreme Court in *Nielsen v. Cass County Social Services Board*, held that a disclaimer related back to the date of death of the intestate decedent, and is treated as if the property never passed to the disclaimant.[14] It reversed the Social Services Board's holding that the disclaimant was ineligible for medical assistance until she incurred medical expenses greater than the amount of inheritance she disclaimed.[15]

(vi) Hence the case law generally seems to allow a disclaimer to escape revocation as a transfer in fraud of creditors. *NOTE,* however, that individual state rules may differ, and that under Treasury Regulation section 25.2518-1(c)(2) the fact a disclaimer may be *voidable* under state law does not disqualify it; but if the transfer is *wholly void* under state law, or is actually voided by creditors, it is not a qualified disclaimer.[16]

(vii) The beneficiary of a spendthrift trust can disclaim his interest. All of the Uniform Acts allow this, and in New York it has been allowed without such a statute.[17]

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11. Simpson v. Penner (*In re* Simpson), 36 F.3d 450, 452-53 (5th Cir. 1994).

12. Hoecher v. United Bank, 476 F.2d 838, 841 (10th Cir. 1973).

13. Geekie v. Watson (*In re* Watson), 65 B.R. 9, 12 (Bankr. C.D. Ill. 1986).

14. Nielsen v. Cass County Soc. Serv. Bd., 395 N.W.2d 157, 160 (N.D. 1986).

15. *See id. Nielsen* was superseded by statute. *See* Hinschberger v. Griggs County Soc. Servs., 499 N.W.2d 876 (N.D. 1990). The Nebraska court declined to follow it in *Hoesley v. State Dept. of Soc. Servs.*, 498 N.W.2d 571 (Neb. 1993). Hence the issue is far from settled.

16. *See* Treas. Reg. § 25.2518-1(c)(2) (1986).

17. *See* Estate of Gilbert, 592 N.Y.S. 2d 224 (Sur. Ct. 1992).

C. *Importance of When Interest Being Disclaimed Was Created*

1. *Before 1977*

If the interest disclaimed was *created* before 1977, Treasury Regulations section 25.2511-1(c)(2) provides that the transfer affected by a disclaimer is not a taxable gift if: (1) the disclaimer is valid under local law; (2) the disclaimer is "made within a reasonable time after knowledge of the existence of the transfer;" and (3) the property has not been accepted.[18]

In *United States v. Irvine,* the U.S. Supreme Court held that a disclaimer made in 1979 of a trust interest established in 1917 (long prior to the 1932 enactment of the gift tax) was not made "within a reasonable time after learning of the transfer."[19] The disclaimant had first learned of her trust interest in 1931.[20]

2. *After 1976*

Disclaimers of interests created after 1976 are governed by I.R.C. § 2518, enacted by the Tax Reform Act of 1976.[21] Section 2518 introduced the concept of a "qualified" disclaimer.[22] (See Part II below for elements.) Because most current situations will involve transfers created after the end of 1976, this outline will focus on the post-1976 criteria stated in § 2518 and the Regulations and Rulings thereunder.

3. *Husband-wife joint tenancies created between 1976 and 1982*
(See paragraph VII C *infra*)

4. *After 1981*
(See paragraph D 5 *infra* regarding disclaimers made after 1981.)

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18. Treas. Reg. § 25.2511-1(c)(2)(as amended 1994).

19. United States v. Irvine, 114 S. Ct. 1473, 1474 (1994).

20. *See id.* at 1474; see E. Bruce Jorgensen, Note, *Disclaimers of Interests Created Before Enactment of the Gift Tax:* United States v. Irvine, 48 TAX LAW. 553 (1995), for a critical analysis of *Irvine.*

21. *See* 26 U.S.C. § 2518 (1994).

22. *See* discussion *infra* Part II for elements.

D. *Local Law v. Federal Law*

1. *Does the disclaimer fulfill local law mandates?*

Most states now have disclaimer statutes. They don't necessarily parallel I.R.C. § 2518. To get the desired property law vesting as well as the desired effect, a disclaimer must comply with local law.

a. Private Letter Ruling (PLR) 79-37-011 held an attempted disclaimer by a Montana executor of a deceased legatee's interest in her deceased father's estate was not a valid disclaimer.[23] The deceased father (transferor decedent) was a resident of Iowa and under Iowa law the right of the deceased legatee (transferee decedent) to disclaim within the requirement period terminated upon the legatee's death within that time period.[24]

b. In *Lundgren v. Hoagland,* a trust beneficiary's assignment to creditors of his share of his father's estate was held not to constitute a renunciation (disclaimer) under local law because the assignment did not declare a renunciation or describe the property interest being renounced.[25]

2. *Who gets the interest disclaimed?*

a. In one case an adult daughter disclaimed an interest in her father's estate believing it would go to her mother.[26] The court held it passed to her own children.[27]

b. In another case a childless uncle disclaimed his share in his deceased brother's estate, believing it would benefit his five nieces and nephews equally.[28] The court held it passed one-third to one living child of his deceased brother.[29] The division was made "*per stirpes"* rather than in a per capita manner.[30] The same result would follow in states having a "right of representation" division of intestate shares.

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23. Priv. Ltr. Rul. 79-37-011 (May 31, 1979).

24. *See id.*

25. *See* Lundgren v. Hoagland, 711 P.2d 809 (Mont. 1985).

26. *See* Cory v. Bryant (*In re* Estate of Bryant), 196 Cal. Rptr. 856, 857 (Ct. App. 1983). *See, e.g.*, Ernst v. Shaw, 783 S.W.2d 400 (Ky. Ct. App. 1990); Webb v. Webb, 301 S.E.2d 570 (W.Va. 1983).

27. *See* Cory v. Bryant, 196 Cal. Rptr. at 862-63 (Ct. App. 1983).

28. *See* Welder v. Hitchcock, 617 S.W.2d 294, 296-97 (Tex. App. 1981).

29. *See id.* at 295-97, 299.

30. *See id.* at 295-97.

3. *Importance of local intestacy statutes; will provisions; risk of boomerang disclaimer*

The Uniform Probate Code (UPC) provides that an interest which is disclaimed passes by intestacy as if the disclaimant had predeceased the transferor or decedent. Many state statutes agree.[31] Practitioners in jurisdictions that do not have statutes like this may be limited in the use of disclaimers. Treasury Regulation section 25.2518-2(e)(5), Example 3, indicates that if the state does not have a provision treating the disclaimant as predeceasing the testator, a disclaimer will be effective only to the extent that the disclaimant does not have a right to receive the property *as an heir at law.*[32] In such states, a disclaimer of an intestate share may not be possible.

a. *Provisions of will or trust designating where disclaimed interest goes.*

If state law so provides, the disclaimed interest ordinarily will pass by intestacy. But if the transferor or decedent has designated in his will, trust or other instrument of transfer the person(s) to whom the disclaimed interest passes, that direction governs.[33]

b. *Boomerang disclaimers*

In Technical Advice Memoranda (TAM) 94-17-002 a daughter disclaimed an interest under her mother's will but failed to disclaim her intestate interest.[34] Believing the disclaimer was valid, the executor distributed the property to the disclaimant's children.[35] The Service ruled this a taxable gift because the property disclaimed had vested in the disclaimant daughter by intestate succession.[36]

4. *Federal law determines federal tax consequences.*

Although state law determines who is entitled to receive a disclaimed interest, federal law establishes whether a disclaimer is effective to avoid gift taxes. In *U.S. v. Irvine,* the Supreme Court held that "state law creates legal interests and

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31. *See* Cal. Prob. Code § 282 (West Supp. 1997).

32. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 3 (1986).

33. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 4-10 (1986); Priv. Ltr. Rul. 90-08-011 (Nov. 17, 1989).

34. Tech. Adv. Mem. 94-17-002 (April 29, 1994).

35. *See id.*

36. *See id.*

rights in property, [but] federal law determines whether and to what extent those interests will be taxed."[37]

5. *Post-1981 "putative" disclaimers*

In 1981, concerned it had given too much importance to local law, Congress added I.R.C. § 2518(c)(3), effective for post-1981 disclaimers.[38] If a post-1981 disclaimer fails to satisfy local law, this amendment allows a "written transfer" (sometimes called a "putative" disclaimer) to suffice for federal tax purposes *so long as* it meets the other requirements of § 2518 for a qualified disclaimer of the transferor's "entire interest in the property . . . to a person or persons who would have received the property had the transferor made a qualified disclaimer."[39]

E. *The Regulations Regarding Local Law*

The Internal Revenue Service Proposed Regulations of July 1980 required compliance with local law. The Final Regulations, issued August 7, 1986, do not require local law compliance for post-1981 disclaimers, and have de-emphasized local law as to *pre-1982* disclaimers (*i.e.*, prior to the addition of I.R.C. § 2518(c)(3)), saying that if such disclaimer "is not effective under . . . local law to divest ownership of the disclaimed property from the disclaimant and vest it in another, [it] is nevertheless treated as a qualified disclaimer under section 2518 if, under applicable local law, the disclaimed interest in [the] property is transferred . . . [by the attempted disclaimer] to another person without any direction on the part of the disclaimant."[40]

Because of these regulatory shifts, use caution as to pre-August 1986 IRS rulings, insofar as they deal with local law compliance.

II. ELEMENTS OF A "QUALIFIED DISCLAIMER" UNDER I.R.C. § 2518 (FOR POST-1976 INTERESTS)

A. *Federal Tax Requirements*

The essential elements under I.R.C. § 2518 and Treasury Regulation section 25.2518-2(a) are as follows:[41]

1. The disclaimer must be *irrevocable and unqualified*;
2. The disclaimer must be *in writing*;

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37. United States v. Irvine, 114 S. Ct. 1473, 1481 (1994).
38. *See* 26 U.S.C § 2518(c)(3) (1994).
39. *Id.*
40. Treas. Reg. § 25.2518-1(c)(1)(i) (1986).
41. *See* 26 U.S.C. § 2518 (1994); Treas. Reg. § 25.2518-(2)(a) (1986).

3. It must be made within *nine months* of the time that the interest is irrevocably transferred. In the case of an inheritance that would be nine months from the date of decedent's death. For minors under the age of twenty-one, I.R.C. § 2518 runs the nine months *from the later of*:[42]

   a. The day on which the transfer creating the interest in such person is made; or

   b. The day on which the disclaimant *attains age 21*. Cal. Probate Code § 279 is much more detailed, as to when the interest was created; and § 277 contemplates a disclaimer by a guardian, but § 295 approves any disclaimer which is valid under the I.R.C.

4. The disclaimer must be *delivered* within that nine month period by the transferor, his "legal representative," the holder of the legal title to the property, or the person in possession.[43] (Normally such delivery will be by an executor, administrator, or trustee.)

5. The disclaiming party *must not have accepted* the interest or property being disclaimed or any of its benefits before making the disclaimer.

6. The interest disclaimed must pass (as the result of the disclaimer) to either:

   i. the decedent's spouse; or

   ii. to a person other than the disclaimant.

The passage must be *without any direction* by the disclaimant. Precatory words concerning to whom the interest is to pass are ignored if they are really only precatory and are not operative in the transfer.[44] In *DePaoli v. Commissioner*, the court held that a settlement direction to pass the property to the decedent's wife was only precatory in effect, and did not disqualify the disclaimer, because the property would pass to her by intestacy.[45] This holding is a very charitable interpretation of the language of the settlement agreement in issue. The court also held that the disclaimant's illegitimate children were not intestate heirs.[46] This latter conclusion may not apply in states such as California which allow, in some circumstances, inheritance by a child born out of wedlock.[47]

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42. *See* 26 U.S.C. § 2518 (1994) (emphasis added).

43. *See* Treas. Reg. § 25.2518-2(c)(2)(1986). A timely mailing to such person is sufficient under Treasury Regulation section 25.2518-2(c)(2), and the Regulation extends time if the last day falls on a weekend or holiday. Use certified mail, return receipt, with the certificate stamped at the post office, to prove mailing date. Many state statutes also require a court filing.

44. *See* Treas. Reg. § 25.2518-2(e)(4), (a)(e)(5) & Ex. 8 (1986); *see also* Tech. Adv. Mem. 95-09-003 (Nov. 3, 1994) (holding that precatory language naming the taker of the disclaimed property did not disqualify the disclaimer under Illinois law).

45. *See* DePaoli v. Commissioner, 62 F.3d 1259, 1261-62 (10th Cir. 1995).

46. *See id.* at 1263-65.

47. See CAL. PROB. CODE §§ 6450-6455 (West Supp. 1997.); CAL FAMILY CODE §§ 7600-7730 (West 1994 & Supp. 1997).

B. *State Law Requirements*

Many state laws further require that the disclaimer (renunciation) instrument must:

1. *Identify the creator* of the interest;
2. *Describe the property* or interest renounced;
3. Be *signed* by the person renouncing; and
4. *Declare the disclaimer and the extent thereof*[48]; and
5. Be *filed* with the court if there is a probate, or with the general trial court or the trustee or fiduciary if there is no probate.[49] Any disclaimer should include those items anyway.

III. BARS TO DISCLAIMER

A. *State Law Statutory Bars; Creditor's Rights*

The practitioner should consult local law statutes, as some statutes contain bars which do not exist under federal tax law. A disclaimer may or may not be a fraudulent conveyance as to the disclaimant's creditors under state law. But if it is void as to creditors it cannot be a qualified disclaimer.[50]

B. Can Be No Consideration for Disclaimer

Under the IRS Final Regulations any acceptance of *consideration,* such as disclaiming an interest in property in exchange for a right to live in the family home for life, bars a qualified disclaimer.[51]

Triple whammy risks of settlement agreements

Proving lack of consideration may be a serious problem in the settlement of the contest of a will, trust or other inheritance dispute, as reciprocal promises are usually consideration. In *DePaoli v. Commissioner*, the decedent's will left everything to his son.[52] The surviving spouse asserted a probate dispute.[53] It was settled by an agreement under which everything went to the widow except a $600,000 exemption equivalent.[54] A marital deduction was claimed under the

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48. *See, e.g.,* CAL. PROB. CODE § 278 (West 1991 & Supp. 1997) (emphasis added).
49. *See* CAL. PROB. CODE § 280 (West 1991 & Supp. 1997) (emphasis added).
50. *See* Treas. Reg. § 25.2518-1(c)(2)(1986).
51. *See* Treas. Reg. § 25.2518-2(d)(2)(1986).
52. *See* DePaoli v. Commissioner, 66 T.C.M. (CCH) 1493, 1494 (1993).
53. *See id.*
54. *See id.*

settlement.[55] The Tax Court upheld IRS' imposition of an estate tax because the marital deduction did not qualify;[56] a gift tax against the son because his transfer was not a qualified disclaimer;[57] and a penalty for the son's failure to file a gift tax return.[58] The disclaimer was disqualified because the transfer did not pass without direction on the part of the disclaimant, but the same result would have followed based on the "no consideration" rule.[59]

This horrendous result was reversed on appeal by the Tenth Circuit, which held that the interest would pass to the wife by intestacy.[60] The Tax Court opinion nevertheless stands as a disaster warning. Two later Tax Court opinions "explain" *DePaoli*.[61]

C. *Acceptance of Benefits as a Bar*

1. A disqualifying benefit is deemed accepted if the disclaimant:
   - a. Receives a widow's or family allowance;[62]
   - b. Accepts dividends, interest or rents from the property;
   - c. Directs others to act respecting the property (*e.g.*, property .....man
   - d. Has used the property as security for a loan;[64] or
   - e. If income distributions already have been made to a trust beneficiary before he disclaims, the beneficiary must return the check to the trustee *uncashed*.[65]

2. Any exercise of a power of appointment is an acceptance.[66]

3. The Ninth Circuit in an unpublished opinion has held that a cut-back of a general power of appointment to a special power is an acceptance.[67] The Regulations agree with the Ninth Circuit.[68]

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55. *See id.*

56. *See id.* at 1495.

57. *See id.* at 1499.

58. *See id.* at 1499.

59. *See id.* at 1499.

60. *See* DePaoli v. Commissioner, 62 F.3d 1259, 1265-66 (10th Cir. 1995).

61. *See* Estate of Rapp, 1996 T.C.M. (RIA) ¶ 96,010 at 56; Estate of Nix, 1996 T.C.M. (RIA) ¶ 96,109 at 839; *see also* Priv. Ltr. Rul. 89-02-045 (Jan. 13, 1989) (upholding a settlement disclaimer, mainly because the dispute was bona fide and the settlement arms-length).

62. *See infra* Part IX(B)(6)(d).

63. *See* Treas. Reg. § 25.2518-2(d)(1) (1986).

64. *See* Treas. Reg. § 25.2518-2(d) (4) Ex. 5 (1986).

65. *See* Treas. Reg. § 25.2518-2(c)(5) Ex. 6 (1986) (emphasis added).

66. *See* Treas. Reg. § 25.2518-2(d)(1) (1986).

67. *See* Goudy v. United States, No. 86-4402, 1988 WL 69767, at *1, *4-5 (9th Cir. 1988), *rev'g* 86-2 U.S. Tax Cas. (CCH) ¶13,690, at 86,232 (D. Ore. 1986).

D. *Items That Do Not Constitute Acceptance of Benefits*

1. A joint tenant of residential property continuing to reside on the property.[69]
2. A surviving spouse continuing to live in the farm residence after he disclaims a one-half interest in the farm, if he pays reasonable rent for the other one-half interest.[70]
3. The fact a beneficiary has accepted [income] after age eighteen, the age of majority under local law, *so long as* he disclaims within nine months after attaining age twenty-one.[71]
4. Taking delivery of an instrument of title without more.[72]
5. Merely because local law vests title immediately upon the decedent's death;[73]
6. Accepting the income on a portion of a bequeathed brokerage account. If the disclaimant withdraws a portion of such an account and disclaims the rest, he is deemed to have accepted only a *pro rata* portion of the income, and his disclaimer of the balance of the account qualifies.[74]

The Service does *not* apply a formula to apportion the income to a spouse who receives income (like a family allowance) from the estate.[75]

7. A request for distribution from a trust is not an acceptance of benefits if the request is rescinded before the trustee has acted and the disclaimant in fact received no benefits.[76]
8. A surviving spouse's election to take against her husband's will, in order to force a statutory share, did not constitute an "acceptance" of that share and did not bar its later disclaimer.[77]
9. A tenant by the entireties is not considered to have accepted benefits by continuing to reside on one of the disclaimed properties in which he still held a fractional share.[78] Note that the result in this latter PLR seems inconsistent with the Service's treatment of other *tenancies by the entireties*. In PLR 94-27-003 the IRS

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68. *See* Treas. Reg. §§ 25.2518-2(d)(1) (1986), 25.2518-3(a)(1)(iii) (as amended in 1994), 25.2518-3(b) (as amended in 1994) & 25.2518-2(e)(1) (1986).

69. *See* Treas. Reg. § 25.2518-2(d) (1986).

70. *See* Priv. Ltr. Rul. 81-24-118 (Mar. 20, 1981).

71. *See* Treas. Reg. § 25.2518-2(d)(3), (d)(4) Ex. 11 (1986).

72. *See* Treas. Reg. § 25.2518-2(d)(1) (1986).

73. *See* Treas. Reg. § 25.2518-2(d)(1) (1986).

74. *See* Treas. Reg. § 25.2518-3(d) Ex. 17 (as amended in 1994).

75. *See infra* Part IV.A.

76. *See* Priv. Ltr. Rul. 92-10-014 (Dec. 11, 1991).

77. *See* Rev. Rul. 90-45, 1990-1 C.B. 176; *see also* Priv. Ltr. Rul. 94-40-027 (July 11, 1994) (permitting a disclaimer by the surviving spouse of the property share received on her partial election against her husband's will).

78. *See* Priv. Ltr. Rul. 91-06-016 (Nov. 8, 1990).

allowed disclaimer of a joint tenancy interest within nine months of decedent's death, but disallowed it for a tenancy by the entirety as to which the time ran from the date of *creation* of the tenancy, because a tenant by the entireties cannot unilaterally sever the tenancy whereas in most states a joint tenant can do so.[79]

10. A withdrawal by the surviving spouse of her one-half interest in a community property trust does not bar her from disclaiming her right to the income from the decedent's one-half interest.[80] PLR 95-07-017 allowed a surviving spouse to disclaim community property, even though she and her husband had entered into a binding community property agreement which apparently could not be unilaterally cancelled, under which all of the community property was to pass to the survivor.[81]

11. A surviving spouse was allowed to disclaim the decedent's one-half of a joint tenancy brokerage account (which by right of survivorship normally passes to the survivor joint tenant automatically upon death), because survivor had not made withdrawals from the account after decedent's death.[82]

E. *The Disclaimer Must Be Timely*

The nine month time limit is *strictly enforced:*

1. The granting of an extension of time to file the federal estate tax return does not extend the time to file a disclaimer.[83]

2. The nine month period runs from the date of death, even if probate of the will is long delayed.[84]

3. The nine month period for disclaiming an interest under a Grantor Retained Income Trust (GRIT) also runs from the settlor's death not the date the GRIT was created, where the settlor did not survive his retained term and did not exercise his general testamentary power of appointment.

4. The nine month period runs from the first spouse's death for property passing under Washington community property law.[85]

5. A seventeen-year-old's disclaimer delivered fifteen months after decedent's death was qualified because he had nine months after he turned twenty-one.[86]

6. In PLR 94-13-026 the Service approved a disclaimer made within nine months after the child attained age eighteen (state law age of majority).[87] Treasury Regulation section 25.2518-2(c)(1) clearly tolls the time for a disclaimer by a minor

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79. Priv. Ltr. Rul. 94-27-003 (Mar. 30, 1994); *see discussion infra* Part VII.B.

80. *See* Priv. Ltr. Rul. 94-24-023 (Mar. 15, 1994).

81. Priv. Ltr. Rul. 95-07-017 (Nov. 15, 1994).

82. *See* Priv. Ltr. Rul. 91-13-011 (Dec. 24, 1990).

83. *See* Fitzgerald v. United States, 73 A.F.T.R.2d (RIA) 2323, 2324 (W.D. La. 1993).

84. *See* Estate of Fleming v. Commissioner, 974 F.2d 894, 895-97 (7th Cir. 1992).

85. *See* Priv. Ltr. Rul. 95-07-017 (Nov. 15, 1994).

86. *See* Priv. Ltr. Rul. 92-23-051 (Mar. 11, 1992).

87. Priv. Ltr. Rul. 94-13-026 (Dec. 27, 1993).

until nine months after the minor's 21st birthday,[88] but the Service normally does not rule more expansively than the request, which here apparently used age eighteen.

7. Under I.R.C. § 2056(b)(8) a marital deduction can qualify for the surviving spouse's interest in a *charitable* trust *only* if the spouse is the sole non-charitable beneficiary.[89] In TAM 87-30-004 a decedent left a $9.7 million residue of his estate to a charitable remainder trust but named both his wife and an eighty-three year old brother as beneficiaries, the brother to take a unitrust interest only if he survived the wife.[90] This pattern was valid for a charitable deduction when the will was done, but not when the decedent died. It is unclear whether the brother attempted to disclaim, but the TAM is clear that he had not done so within the requisite nine months after the decedent's death, although the decedent's executor claimed that he could still do so under local law.[91] When the estate tax return was filed, the decedent's executor attempted to salvage the disaster by claiming a marital deduction for this trust under I.R.C. § 2056(b)(7).[92] The TAM ruled that no marital deduction could be claimed on these facts, and that the time for a disclaimer by the brother had expired.[93] Hence the $9.7 million trust did not qualify for either the marital deduction or the charitable deduction. Assuming a 55% rate, this subjected the trust in issue to an estate tax in excess of $5.3 million, which would have passed entirely free of estate tax if the elderly brother had timely disclaimed.

IV. THE IMPORTANCE OF EARLY ACTION; LIABILITY RISKS FOR TAX ADVISORS

The possibility of disclaimers should be considered *immediately* upon a decedent's death because:

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88. Treas. Reg. § 25.2518-2(c)(1) (1986).
89. *See* 26 U.S.C. § 2056(b)(8) (1994).
90. Tech. Adv. Mem. 87-30-004 (Apr. 15, 1987).
91. *See id.*
92. *See id.*
93. *See id.*

A. *Widow's or Family Allowance May Bar a Disclaimer*

A widow's allowance, family's allowance, income distribution from a trust, or other early action *may preclude a later disclaimer.*[94] Similarly in PLR 84-05-003, a disclaimer by a widow was disallowed because her expenses were paid by the estate (presumably via a widow's or family allowance) for nine months after decedent's death, even though she had repaid the estate shortly after the disclaimer.[95]

B. *Risk of Suit Against a Lawyer or CPA Who Fails to Advise of Availability of Disclaimer*

An attorney or accountant can be sued for failure to advise an heir or beneficiary of the tax benefits of disclaiming an inheritance.

In California, a suit against a lawyer for negligent failure to advise of the possibility of a disclaimer was settled just prior to trial.[96] The husband, age eighty-three, died and the wife, age eighty-seven, died eight and one-half months later. The combined estate was $1.2 million.[97] The lawyer had filed a petition to set aside (confirm) that most of the husband's estate passed to the wife.[98] The children claimed the lawyer should have waited until after expiration of the nine month period to file the spousal set-aside petition.[99] The failure to make a disclaimer resulted in a $250,000 increase in estate tax.[100] Terms of the settlement are not known.

A family lawyer and CPA were sued in *Linck v. Barokas & Martin.*[101] The defendants there had been in the process of preparing an estate plan for a mutual client with an estate of about $ 3 million when he died.[102] The entire estate passed to the widow.[103] If she had disclaimed any of the inheritance, the disclaimed property would have passed to the couple's three children in equal shares.[104] No disclaimer was made and three years later the wife and children sued the lawyer and CPA for $ 1 million.[105] They alleged negligence in failing to advise the wife to disclaim part of the $ 3 million, because such a disclaimer would have avoided the disclaimed

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94. *See* Treas. Reg. § 25.2518-3(d) Ex. 18 (as amended in 1994).

95. Priv. Ltr. Rul. 84-05-003 (Oct. 11, 1983). *But see supra* Part III.D.4. explaining an opposite result on a rather similar situation involving a brokerage account. *See infra* Part IX.B.6.d. for a way to hedge this risk.

96. *See IRC §: Disclamiers,* RECENT DEVS. IN EST. PLAN. AND ADMIN. (Continuing Education of the Bar, Cal.) Jan./Feb. 1991, at 97-98 (on file with the *Drake Journal of Agricultural Law*).

97. *See id.* at 97.

98. *See id.*

99. *See id.* at 98.

100. *See id.*

101. Linck v. Barokas & Martin, 667 P.2d 171 (Alaska 1983).

102. *See id.* at 172.

103. *See id.*

104. *See id.* 173-74.

105. *See id.*

property being subject to a second transfer tax when the property was passed to the children by the wife.[106] The tax there was paid on the first death because the decedent died in 1978, before the 1981 enactment of the unlimited marital deduction in ERTA. The trial court sustained a demurrer and dismissed the case, but the Supreme Court of Alaska reversed, saying the complaint stated a cause of action.[107] The case was thereafter settled.

See also *Bucquet v. Livingston,* where the drafting lawyer was held liable to a decedent's beneficiaries for: (a) his malpractice in drafting a testamentary by-pass trust for the surviving spouse with a general power of appointment which pulled the trust back into her estate, and (b) in his capacity as the attorney handling probate of the decedent's will, for failure to advise the surviving spouse to disclaim her power of appointment.[108]

A recent Florida case also upheld a cause of action against both the attorney for the estate and the accountant who prepared the federal estate tax return, neither of whom ever advised the surviving spouse that a disclaimer could have reduced the overall taxes due as the result of the deaths of both spouses.[109] The damages alleged were $320,000.[110]

C. *Professional Liability Risk Even in Small Estate*

The *Linck* and *Bucquet* cases can be a hazard in even a small estate, particularly if the property is passing to someone who has a short life expectancy or who already has a substantial estate, and who would prefer to shift it to the next generation.

V. TYPES OF INTERESTS THAT MAY BE DISCLAIMED

Assuming all the other elements of a *qualified* disclaimer are fulfilled,[111] a wide range of interests may be disclaimed.

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106. *See id.*
107. *See id.*
108. Bucquet v. Livingston, 129 Cal. Rptr. 514, 518-21 (Ct. App. 1976).
109. *See* Kinney v. Shinholser, 663 So. 2d 643, 645-47 (Fla. Dist. Ct. App. 1995).
110. *See id.* at 645.
111. *See supra* Part II.A.

A. *In General*

One may disclaim the *specific interest* in property, an *undivided portion* of any separate interest, an *income interest* (subject to the segregation rule noted below for trusts), a *remainder interest* or an undivided portion of either interest.[112]

One may disclaim property that is *severable,* such as accepting some shares of stock and making a disclaimer of remaining shares in same corporation.[113] The following are specific examples:

B. *A Testamentary Bequest*

1. Note that because under the law of most states the disclaimant is deemed to have predeceased the testator, the disclaimed interest will pass, however the will or trust specifies for that eventuality.[114]
2. If there is no residuary clause in the will, property passes to decedent's heirs at law, assuming local law so provides.[115]
3. One may disclaim a dollar amount out of a residuary estate, or a fractional share of the residuary estate, so long as the disclaimant receives no income on the disclaimed share.[116]

C. *Intestate Share*

One may disclaim an *intestate share.*[117] This only works if the state's local law treats the disclaimant as predeceasing the testator. If a disclaimant other than the surviving spouse also qualifies as an heir of law, the disclaimer must cover his rights in both capacities.[118] One should *always* include a disclaimer of any intestate right as to the disclaimed property. A horrible boomerang occurred when the beneficiary disclaimed under the will but failed to disclaim her intestate right.[119]

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112. *See* Treas. Reg. § 25.2518-3(a) (as amended in 1994).

113. *See* Treas. Reg. § 25.2518-3(a)(1)(ii) (as amended in 1994); Priv. Ltr. Rul. 87-02-023 (Oct. 10, 1986).

114. *See* Treas. Reg. § 25.2518-3(d) Exs. 1, 2, 3, 4 (as amended in 1994); Treas. Reg. 25.2518-2(e)(5) Exs. 9, 10 (1986).

115. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 2 (1986). *See, e.g.,* CAL. PROB. CODE § 282(a) (West 1991 & Supp. 1997).

116. *See* Treas. Reg. § 25.2518-3(d) Ex. 19 (as amended in 1994); *see infra* Part VI regarding trusts.

117. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 2 (1986).

118. *See* Treas. Reg. § 25.2518-2(e)(3) (1986).

119. *See* Tech. Adv. Mem. 94-17-002 (Apr. 29, 1994).

D. *Pecuniary Amount; Need for Segregation*

A recipient can disclaim a *specific pecuniary (dollar) amount* out of either a pecuniary or non-pecuniary bequest or gift; but watch out for acceptance of benefits by receipt of income prior to the disclaimer.[120] If only a *portion* of a pecuniary bequest is being disclaimed, the disclaimed amount and the income attributable to it must be segregated from the remaining portion of the bequest.[121] In Priv. Ltr. Rul. 95-13-011, the Service ruled that on funding the assets, the assets must be valued either as of the date of the disclaimer *or,* on a basis that is "fairly representative" of post-death appreciation and depreciation.[122]

E. Severable Specific Property Interest

One may disclaim a specific interest in severable property. Treasury Regulation section 25.2518-3(a) defines severable property as "property which can be divided into separate parts each of which, after severance, maintains a complete and independent existence."[123] Examples of disclaimable items include specified paintings and jewelry; 300 identified acres out of a 500 acre parcel; an undivided portion of the income from a farm; the disclaimant's entire interest in the income from a trust while retaining his entire interest in corpus, or vice versa.[124] However, the Examples also contain limits on disclaiming some partial rights while retaining others.

1. *Corporate stock.*[125] One may also disclaim some shares and retain others (presumably identical shares) in the same corporation because they are severable.[126] In *Brown v. Momar,* the decedent's stock was subject to a shareholder's agreement requiring his estate to offer the stock back to the corporation at book value.[127] However, the agreement allowed each shareholder to transfer stock to his issue.[128] Decedent's will gave the stock to his wife, but she disclaimed so then it passed to her and to the decedent's sons, who thus took the stock and avoided a bargain price sale

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120. *See* Treas. Reg. § 25.2518-3(c), (d), Ex. 16 &17 (as amended in 1994).

121. *See* Treas. Reg. § 25.2518-3(c) (as amended in 1994); *see also* Priv. Ltr. Rul. 82-08-069 (allowing disclaimer of a part of a joint bank account balance); Priv. Ltr. Rul. 81-13-061 (allowing disclaimer by a son of all his interest in his parents' residuary estate except the amount needed to pay a debt owed by him to the estate).

122. Priv. Ltr. Rul. 95-13-001 (Dec. 29, 1994); Rev. Proc. 64-19 (1964).

123. Treas. Reg. § 25.2518-3(a) (as amended in 1994).

124. *See* Treas. Reg. § 25.2518-3(d) (as amended in 1994).

125. *See* Treas. Reg. § 25.2518-2(d)(4) Ex. 6 (1986).

126. *See* Treas. Reg. § 25.2518-3(a)(1)(ii) (as amended in 1994); Priv. Ltr. Rul. 87-02-023 (Oct. 10, 1986).

127. Brown v. Momar, Inc., 411 S.E.2d 718, 720-22 (Ga. Ct. App. 1991).

128. *See id.* at 720.

to the corporation.[129] The court upheld the disclaimer's effect, notwithstanding the shareholders' agreement.[130]

2. *Real estate.* Segregable real estate may be disclaimed.[131] But if a farm is bequeathed and the beneficiary asks the executor to sell the farm and distribute the proceeds, the beneficiary cannot disclaim a portion of the proceeds of sale of the farm.[132] And the beneficiary of an outright devise of real estate cannot carve out and retain an income interest while disclaiming the remainder. The same restrictions apply to securities.[133]

3. *UTMA.* Stock received under the Uniform Transfers to Minors Act (formerly the Uniform Gifts to Minors Act) may be disclaimed within nine months after the minor attains age twenty-one.[134] Note, however, the Service's restrictive position on disclaimers by minors in Part VIII.6. *infra*.

4. *Caveat: UTMA minor cannot accept income after age 21.* If the Custodian holds UTMA property until the minor is age 25 (as the Act now allows), the minor cannot disclaim if he has accepted any dividends or income after attaining age 21.[135] Note, however, under Part VIII.F. *infra,* the Service's attacks on disclaimers by minors of interests which the minors hold directly, even when a court approves the disclaimer.

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129. *See id.*

130. *See id.* at 721-22. *But see infra* Part V.E.2. regarding prohibition of carving out an income interest.

131. *See* Treas. Reg. § 25.2518-3(d) Ex. 3 (as amended in 1994); Treas. Reg. § 25.2518-2(e)(5) Ex. 10 (1986).

132. *See* Treas. Reg. § 25.2518-2(d)(4) Ex. 4 (1986).

133. *See* Treas. Reg. § 25.2518-3(b), (d) Ex. 2 (as amended in 1994).

134. *See* Treas. Reg. § 25.2518-2(d)(4) Ex. 11 (1986).

135. *See* Treas. Reg. § 25.2518-2(d)(3), (d)(4) Ex. 11 (1986).

F. *Life Insurance*

One commentator has suggested that a surviving spouse should be able to disclaim life insurance (*i.e.*, the cash value of the policy) on the disclaimant's own life, if that policy were owned by the decedent and would otherwise pass to the disclaiming surviving spouse under the decedent's will or trust.[136] The suggestion seems logical but no specific authority for it could be located. However, in PLR 89-51-041 the IRS ruled that the beneficiaries of an irrevocable insurance trust could disclaim the property which apparently was at least partly funded by life insurance proceeds.[137]

G. *Qualified Retirement Plan Benefits and IRAs*

One may disclaim the following retirement plan benefits:

1. A money purchase pension plan.[138]
2. A profit sharing plan.[139]
3. Such a disclaimer by the beneficiary of a qualified retirement plan may be made despite the alienation provisions of ERISA.[140]
4. A surviving spouse may disclaim an interest in an Individual Retirement Account (IRA).[141] A disclaimer may be used to remove IRA benefits from a bypass trust and cause them to pass to the surviving spouse by intestate succession.[142]
5. In PLR 95-37-005 the deceased husband had begun to draw income from his IRA.[143] On his death the IRA benefit was to pass to a residuary trust of which the surviving spouse was the beneficiary and trustee, and over which she held a power of appointment.[144] She was allowed to disclaim her interest in the IRA and her power of appointment.[145] She also made a partial Qualified Perminable Interest Property (QTIP) election for the IRA and split the residuary trust in order to maximize the

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136. Malcolm A. Moore, *The Ever-Expanding Use of Disclaimers in Estate Planning: An Update,* 24 INST. ON EST. PLAN. ¶ 1700, ¶ 1705, at 17-11 (1990).

137. Priv. Ltr. Rul. 89-51-041 (Sept. 26, 1989).

138. *See* Priv. Ltr. Rul. 90-16-026 (Jan. 18, 1990).

139. *See* Priv. Ltr. Rul. 88-38-075 (July 1, 1988).

140. *See* Gen. Couns. Mem. 39,858 (Sept. 9, 1991); Young v. Dep't of Admin., 524 So. 2d 1071 (Fla. Dist. Ct. App. 1988).

141. *See* Priv. Ltr. Rul. 90-37-048 (June 20, 1990).

142. *See* Priv. Ltr. Rul. 96-15-043 (Jan. 17, 1996).

143. Priv. Ltr. Rul. 95-37-005 (June 13, 1995).

144. *See id.*

145. *See id.*

decedent's GST tax exemption.[146] Under the convoluted facts she wound up with all of the income from the IRA.[147] The disclaimer there was well done.

6. In PLR 96-15-043 decedent had funded a bypass credit shelter trust with two IRAs.[148] The widow was to receive the income and held a power of appointment.[149] In default of exercise of the power the remainder would go to her issue.[150] However, the trust did not satisfy the Minimum Distribution Rules under I.R.C. § 401 and the Proposed Regulations.[151] So the widow, children and grandchildren all disclaimed their interest in the trust.[152] The IRAs thus passed to the widow by intestacy, and she thus qualified to "roll over" her husband's two IRAs into her own IRA, thereby deferring the income tax.[153]

7. In PLR 94-37-042 the personal representative was not allowed to roll over the decedent's qualified plan to his widow, because the decedent had acquired an interest in the plan during his lifetime and had control over it.[154] Note that the law of retirement benefits is *extremely complex.* Care should be taken to check beneficiary designations and other aspects of a qualified plan or IRA, as they are also subject to a variety of potential penalty taxes.[155] The 1996 Tax Act has liberalized some of the rules previously applicable to distributions from retirement plans, although the effective dates of the respective amendments vary.

H. *Powers of Appointment*

One may disclaim powers of appointment.

1. The disclaimer may cover any interest that passes by either the *exercise or lapse of a general power*.[156]

2. In PLR 86-07-013 the IRS ruled with respect to a *special power* that:[157]

a. The time for disclaimers by contingent beneficiaries of a special power of appointment held by the surviving spouse over a QTIP marital trust began to run from the date of decedent's death;[158] and

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146. *See id.*

147. *See id.*

148. Priv. Ltr. Rul. 96-15-043 (Jan. 17, 1996).

149. *See id.*

150. *See id.*

151. *See id.*

152. *See id.*

153. *See id.*

154. Priv. Ltr. Rul. 94-37-042 (June 22, 1994).

155. *See, e.g.*, Louis A. Mezzullo, *Planning for Distributions from Qualified Retirement Plans and IRAs*, 46 MAJOR TAX PLAN. ¶1200, at 12-1 (1994).

156. *See* Treas. Reg. § 25.2518-2(c)(3); *see also* Treas. Reg. § 25.2528-3(d), Ex. 21 (as amended in 1994) (allowing disclaimer of a power of appointment as to one-half of the property subject to the power).

157. Priv. Ltr. Rul. 86-07-013 (Nov. 14, 1985).

b. That the time for disclaiming contingent beneficial interest in a residuary trust to be funded *after the death* of the surviving spouse with property from the QTIP, if she failed to exercise the special power, also ran from the date of the decedents' death.[159]

3. The time to disclaim property that passes by lapse of a pre-1942 general power of appointment runs from the *date of lapse*, not the powerholder's date of death.[160]

4. The Regulation also allows a person to make a qualified disclaimer of an interest in property even if he thereafter holds a fiduciary power to distribute to designated beneficiaries, but *only* if the power to distribute is subject to an *ascertainable standard*.[161]

5. *Caveat:* The Regulation says that if a disclaiming party holds other powers (such as a trustee who holds both the power of appointment and a power to invade corpus), he would have to disclaim both the power of invasion and the power of appointment.[162]

Any exercise of a power of appointment is an acceptance precluding disclaimer. See *supra* Part III.C.2.

See, however, PLR 90-28-005, discussed in part X *infra* relating to the GST tax, in which the survivor spouse was permitted to disclaim a general power of appointment with respect to one half of a trust.[163] A QTIP election was made for the disclaimed share and a reverse QTIP election was made as to a portion of the disclaimed share.[164] The attorney there also split the trust in a court proceeding to utilize the unused portion of the decedent's GST exemption.[165]

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158. *See id.*

159. *See id.*

160. *See* Priv. Ltr. Rul. 94-45-014 (Aug. 10, 1994); Priv. Ltr. Rul. 93-18-020 (Feb. 4, 1993).

161. *See* Treas. Reg. § 25.2518-2(e)(5) Exs. 11 & 12 (1986).

162. *See* Treas. Reg. § 25.2518-3(d) Ex. 9 (as amended in 1994).

163. Priv. Ltr. Rul. 90-28-005 (July 13, 1990).

164. *See id.*

165. *See id.*

I. *Partnership Interest*

In PLR 91-23-003, a surviving *limited* partner who also was decedent's executor voted, after decedent's death, the decedent's interest and her own interest to make herself general partner.[166] Her attempted disclaimer of her own interest failed because the voting was deemed an acceptance of benefits, and her disclaimer caused a taxable gift.[167] The disclaimer of a partnership interest, however, presumably would have qualified but for her benefit acceptance.[168]

J. *Disclaimer After Election Against the Will*

In Revenue Ruling 90-45, the Service ruled that a surviving spouse could disclaim, even though the survivor had elected, prior to the disclaimer, to take an intestate share in decedent's estate against the will.[169] The interest must be disclaimed within nine months of the decedent's death.[170]

K. *Special Use Valuation*

McDonald v. Commissioner, one of the leading joint tenancy disclaimer cases, disqualified a special use valuation election under § 2032A regarding North Dakota farm land.[171] The court said the § 2032A agreement should have been signed by the children and grandchildren who actually took the land by reason of the disclaimer, and not by the surviving spouse who had disclaimed any interest in that particular land.[172] (As noted *infra*, the IRS ultimately acquiesced in this decision, thus changing the joint tenancy disclaimer rules, but its Action on Decision 1990-06 presumably means the Service also approved the result under § 2032A.)[173]

In PLR 94-07-015, a special use valuation was used in valuing a ranch for computing the amount of the marital deduction trust.[174] A charity was the remainder beneficiary of the trust for a specific dollar amount, after the surviving spouse's death.[175] Because a charity cannot be a qualified heir under § 2032A(e)(1), the survivor saved the special use value election by disclaiming his interest in a life insurance policy, which passed to family members who were the other remainder

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166. Priv. Ltr. Rul. 91-23-003 (Feb. 14, 1991).

167. *See id.*

168. *See* Priv. Ltr. Rul. 90-26-003 (June 29, 1990).

169. Rev. Rul. 90-45, 1990-1 C.B. 175.

170. *See id.*

171. McDonald v. Commissioner, 853 F.2d 1494 (8th Cir. 1988).

172. *See id.* at 1497-98.

173. *See* McDonald v. Commissioner, 853 F.2d 1494 (8th Cir. 1988), *action on decision,* 1990-06 (Feb. 7, 1989).

174. Priv. Ltr. Rul. 94-07-015 (Feb. 18, 1994).

175. *See id.*

beneficiaries.[176] That enabled the trustee to borrow on the policy to satisfy the pecuniary bequest to the charity, thus eliminating it as a beneficiary of the ranch land.[177]

VI. TRUSTS; SPECIAL PROBLEMS

A. *Disclaimers in Trusts Involve Special Timing Factors*

1. *Interests created before 1977 must be disclaimed within "reasonable time."* I.R.C. § 2518 applies only to interests created after December 31, 1976.[178] If there are two taxable transfers, such as a completed gift of a remainder interest in an *irrevocable* trust, with the settlor retaining a life estate, and that earlier transfer precedes December 31, 1976, § 2518 does not apply to that creation.[179] The time for disclaiming that earlier irrevocable gift, therefore, is *not* nine months from creation of the trust but rather "a reasonable time after learning of the existence of the transfer."[180]

Jewett v. Commissioner invalidated a disclaimer of a remainder made *before* death of the intervening life tenant but more than thirty-three years after creation of the interest.[181] The latter was held not a "reasonable time."[182] The *Jewett* court disapproved *Keinath v. Commissioner*,[183] which had held that a disclaimer executed shortly after expiration of the intervening life estate, but nineteen years after the remainder being disclaimed was created, was within a "reasonable time."[184]

The rationale of *Jewett* was recently applied in *United States v. Irvine*, which invalidated an attempted disclaimer by a trust beneficiary which was made some forty-seven years after the beneficiary learned of its existence.[185] In *Irvine,* a trust was created in 1917, the beneficiary learned of the trust in 1931, and the gift tax was enacted in 1932.[186]

PLR 86-01-017 upheld a partial disclaimer made in 1985, within nine months of the time the disclaimant learned of his interest, even though the trusts had been created several years earlier (prior to 1977).[187]

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176. *See id.*
177. *See id.*
178. *See* Treas. Reg. § 25.2518-l(a)(1) (1986).
179. *See* Treas. Reg. § 25.2518-2(c)(5) Ex. 10 (1986).
180. *See* Treas. Reg. § 25.2511-1(c)(2) (1986).
181. Jewett v. Commissioner, 455 U.S. 305 (1982).
182. *See id.*
183. Keinath v. Commissioner, 480 F.2d 57 (8th Cir. 1973).
184. *See Jewett*, 455 U.S. at 309.
185. United States v. Irvine, 511 U.S. 224 (1994).
186. *See id.*
187. Priv. Ltr. Rul. 86-01-017 (Oct. 11, 1985).

2. *Disclaimer by a fiduciary* In Revenue Ruling 90-110, an attempted disclaimer by a trustee of a power to invade corpus for the benefit of a party other than the surviving spouse (which disclaimer was made to try to qualify the trust for QTIP treatment) was invalidated.[188] A disclaimer cannot properly be made by a fiduciary without either (a) the beneficiary's consent, or (b) an express grant of authority in the governing instrument.[189] Including a power to disclaim in wills and trusts, hence, is very important. This attempt also was not saved by I.R.C. § 2518(c)(3), because such a transfer would be defective as a violation of the beneficiary's rights. In PLR 95-21-032, the IRS stated, "generally, a disclaimer of a trustee is not effective for purposes of [I.R.C. § 2518]."[190]

If a disclaimant is both a beneficiary and a fiduciary (executor or trustee), a disclaimer of the beneficial interest by that person is not effective if that person retains a *wholly discretionary* power to allocate the affected interest among a designated class.[191] But the fiduciary may harvest a crop or maintain a home belonging to the estate without violating this restriction.[192]

3. *Disclaimer by a trustee.* PLR 95-21-032 upheld a disclaimer by a trustee to invade principal for his own benefit, because he was also disclaiming all rights to income and principal of the trust, thus terminating all of his interests in the trust.[193]

4. *Disclaimer of a portion; required segregation.* If an income beneficiary wishes to disclaim income from only a portion of the specific property in the trust, the disclaimer must require that the disclaimed specific property be segregated from the rest of the trust and to pass to someone other than the disclaimant or his spouse.[194]

5. *Segregation required if disclaiming income and remainder interest in portion of trust assets*. The same segregation rule applies if the beneficiary is disclaiming an income interest and a remainder interest in specific trust assets, but retaining interests in other trust assets.[195] In this latter instance, however, both the specific property disclaimed and the income therefrom must be segregated.

6. *Fractional share of a trust interest.* In an unusually liberal PLR, the IRS allowed a disclaimer of a fractional share of a trust interest (with the numerator tied to the settlor's unified credit) even though the disclaimant had already received

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188. *See* Rev. Rul. 90-110, 1990-2 C.B. 209.
189. *See id.*
190. Priv. Ltr. Rul. 95-21-032 (Feb. 28, 1995) (citing Rev. Rul. 90-110, 1990-2 C.B. 209).
191. *See* Treas. Reg. § 25.2518-2(d)(2) (1986).
192. *See id.*
193. Priv. Ltr. Rul. 95-21-032 (Feb 28, 1995).
194. *See* Treas. Reg. § 25.2518-3(a)(2) (as amended in 1994).
195. *See id*.

"modest distributions."[196] They were not deemed an acceptance because the distributions were less than the income disclaimant was entitled to under the non-disclaimed part.[197]

7. *Undivided portion.* A beneficiary may disclaim an *undivided portion* of an interest in a trust but must comply with Treasury Regulation section 25.2518-3(b) concerning disclaimers of undivided portions.[198]

8. *Return of uncashed check.* A trust income beneficiary who wishes to disclaim after he has received income distributions by check must return the checks *uncashed* with the disclaimer.[199]

9. *No disclaimer for term of years.* A beneficiary *may not* disclaim an income interest for a certain number of years.[200]

10. *Segregate any disclaimed specific trust asset.* If an interest in a specific trust property is disclaimed, that disclaimed property and the income therefrom must be segregated from the rest of the trust.[201]

11. *Cannot disclaim a "slice" of merged interests.* If the transferor has by two separate transfers given a beneficiary a life interest and a remainder interest in the same property so that the interests are *merged* under local law, the beneficiary cannot disclaim those separate interests. The beneficiary may disclaim the entire merged interest or an undivided portion of the merged interest.[202]

12. *Disclaimer of power to change corporate trustee.* In an early PLR, the IRS ruled that a surviving spouse who had under the trust the power to remove the corporate trustee every two years, and replace it with another independent corporate trustee, could disclaim that power, so long as the disclaimer satisfied the provisions of the local (California) disclaimer statute.[203] At that time (1981) this PLR seemed a bit inconsistent with the then-extant proposed Regulations. Because the final Regulations treat income and principal interests as independent and separately

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196. *See* Priv. Ltr. Rul. 90-36-028 (June 12, 1990).

197. *See id.*

198. *See* Treas. Reg. § 25.2518-3(a)(2) (as amended in 1994).

199. *See* Treas. Reg. § 25.2518-2(c)(5) Ex. 6 (1986).

200. *See* Treas. Reg. § 25.2518-3(a)(1)(i) (as amended in 1994).

201. *See* Treas. Reg. § 25.2518-3(a)(2) (as amended in 1994); Priv. Ltr. Rul. 88-31-032 (Aug. 5, 1988).

202. *See* Treas. Reg. § 25.2518-3(d) Ex. 12 (as amended in 1994).

203. *See* Priv. Ltr. Rul. 81-22-075 (Mar. 6, 1981).

disclaimable[204] and allow disclaimers of a general power of appointment over corpus,[205] this PLR seems more consistent with the IRS' current policy.

In *Estate of Wall v. Commissioner*, the Tax Court held the grantor's retained power to discharge the trustee of some irrevocable trusts and to replace it with a new corporate trustee did not cause the trust assets to be included in the grantor's estate.[206] As a result the Service revoked old Revenue Ruling 79-353 in Revenue Ruling 95-58.[207]

VII. JOINT TENANCIES AND TENANCIES BY THE ENTIRETIES

A. *The* McDonald *Case - Joint Tenancies in Real Estate*

Prior to 1990, the IRS had asserted that the nine-month time for disclaiming an interest in joint tenancy ran from the date of *creation* of the interest. Because many joint tenancies long predated the death of the first joint tenant to die, this disqualified a large number of joint tenancy transactions. In *McDonald v. Commissioner*, the court held that a survivorship interest in a joint tenancy that is subject to unilateral partition by either tenant is "created" by the death of the first cotenant to die, and not on the date the tenancy was originally established.[208] In a major reversal of its prior litigating position, the Service, in its Action on Decision (AOD) 1990-06 acquiesced in *McDonald*, but limited the acquiescence to situations in which a joint tenant has a unilateral right to sever under state law.[209] This AOD effectively disavowed the provision of regulation section 25.2518-2(c)(4)(i), which says that a joint tenant cannot disclaim a joint interest attributable to consideration provided by that tenant.[210] *McDonald* involved North Dakota farm land.[211] *Kennedy v. Commissioner,* which reached the same result, albeit on a power of appointment analogy, involved Illinois farm land.[212]

Occupancy by the survivor spouse of a joint tenancy residence and making mortgage payments, both after decedent's death, is not an acceptance of benefits precluding disclaimer.[213]

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204. *See* Treas. Reg. § 25.2518-3(a)(1) (as amended in 1994).

205. *See* Treas. Reg. § 25.2518-3(d) Ex. 21 (as amended in 1994).

206. *See* Estate of Wall v. Commissioner, 101 T.C. 300 (1993).

207. Rev. Rul. 95-58, 1995-2 C.B. 191.

208. McDonald v. Commissioner, 853 F.2d 1494 (8th Cir. 1988), *action on decision,* 1990-06 (Feb. 7, 1989).

209. *See id.*

210. *See* Treas. Reg. § 25.2518-2(c)(4)(i) (1986).

211. *See McDonald*, 853 F.2d at 1494.

212. Kennedy v. Commissioner, 804 F.2d 1332 (7th Cir. 1986).

213. *See* Priv. Ltr. Rul. 91-35-043 (June 3, 1991).

B. *Joint Tenancies in Personal Property*

1. *Mutual funds and financial accounts*

In *Dancy v. Commissioner*, the parties had held various financial accounts in joint tenancy.[214] Following *McDonald* and *Kennedy,* the court held there was no principled difference between joint tenancy property that could be partitioned and a bank account from which either could withdraw.[215] TAM 94-27-003 allowed a surviving spouse to disclaim interests jointly held with the deceased spouse in mutual funds and bank accounts.[216]

2. *Joint tenancy brokerage accounts*

PLR 91-13-011 allowed a disclaimer by the surviving spouse's right to receive the decedent's half of a joint tenancy brokerage account.[217] This was done to fund an otherwise inadequately funded bypass trust intended to utilize the decedent's unified credit.

PLR 90-44-062 also approved disclaiming an interest in a survivorship brokerage account.[218]

In PLR 92-14-022, the IRS stated that a surviving spouse's transfer of assets from a joint brokerage account held with the deceased spouse to an account in the survivor's sole name did not constitute an acceptance of benefits (which would have precluded disclaimer), even though the survivor had withdrawn cash, because the withdrawals never reduced the account below the date of death balance of the decedent's one-half of the account.[219] An acceptance did occur, however, from the survivor's sale of securities from the account made after decedent's death.[220]

Disclaimers of joint tenancy interests in personal property are now allowed in California. *Propst v. Stillman* expressly validated unilateral severance of joint tenancy personalty.[221]

C. *Spousal Joint Tenancies Created Between 1976 and 1982*

The 1976 Tax Reform Act established a special category of husband-wife joint tenancies created (or if they preexisted were severed and re-created) after

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214. Dancy v. Commissioner, 872 F.2d 84 (4th Cir. 1989).

215. *See id.*

216. *See* Tech. Adv. Mem. 94-27-003 (July 8, 1994); *see also* Priv. Ltr. Rul. 93-36-011 (June 8, 1993) (allowing disclaimer of jointly owned certificates of deposit (CDs)).

217. Priv. Ltr. Rul. 91-13-011 (Dec. 24, 1990).

218. Priv. Ltr. Rul. 90-44-062 (Aug. 7, 1990).

219. *See* Priv. Ltr. Rul. 92-14-022 (Jan. 6, 1992).

220. *See id.*

221. Propst v. Stillman, 788 P.2d 628 (Cal. 1990).

December 31, 1976.[222] Former I.R.C. § 2515 and § 2515A, adopted in 1978 but effective for joint interests created after December 31, 1976, were repealed as to joint interests created after December 31, 1981.[223]

As to spousal joint tenancies created during this 1977-1982 window, the Regulations allow the survivor to disclaim within nine months after the death of the first spouse.[224]

In *Gallenstein v. United States*, a spousal joint tenancy was created before 1977 but the decedent died after 1981.[225] The court held that the contribution rule of I.R.C. § 2040(a) applied, rather than the automatic qualified joint interest rule of § 2040(b).[226] The rationale was that the effective date provisions of 1981 ERTA did not repeal the effective date of the 1976 Act amendments. Under *Gallenstein,* therefore, up to 100% of the property may be included in the estate of the first spouse to die (depending on how much he or she contributed to the tenancy), but the surviving spouse can disclaim the portion so included.

D. *Non-Spousal Joint Tenancies*

PLR 94-11-014 permitted a daughter to disclaim the joint interest in stock she had held with her mother because local (Ohio) law allowed unilateral partition during lifetime.[227]

E. *Accounts That Are Really Community Property*

PLR 90-42-042 allowed the surviving spouse to disclaim $590,000 out of an "investment savings account" even though the account was *entirely in the survivor's name.*[228] This was allowed because the money in the account had actually been community property up to the time of the decedent's death.[229] The survivor had not made any withdrawals since the deceased spouse's death.[230]

F. Tenancy by the Entirety Problems

The limitation of AOD 1990-06 is emphasized in PLR 92-08-003, where the IRS declined to follow *McDonald* and ruled that an attempted disclaimer by the surviving tenant in a tenancy by the entirety was not qualified because under local

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222. *See* 26 U.S.C. § 2040 (1994) (as amended by the 1976 Tax Reform Act).
223. *See* 26 U.S.C. §§ 2515, 2515A (1994).
224. *See* Treas. Reg. § 25.2518-2(c)(4)(ii) (1986).
225. Gallenstein v. United States, 975 F.2d 286 (6th Cir. 1992).
226. *See id.*
227. Priv. Ltr. Rul. 94-11-014 (Dec. 15, 1993).
228. Priv. Ltr. Rul. 90-42-042 (July 23, 1990).
229. *See id.*
230. *See id.*

(Arkansas) law a tenancy by the entirety could not be severed unilaterally but rather required voluntary action by *both* co-tenants.[231]

A similar result occurred in TAM 94-27-003, where the Service rejected as untimely an attempted disclaimer of a tenancy by the entirety because under local (Maryland) law there was no right of lifetime partition.[232] The IRS, therefore, ruled the time for disclaimer ran from creation of tenancy by the entirety.[233]

Because Pennsylvania law treats spousal joint tenancies as tenancies by the entirety, IRS ruled that jointly owned bonds could not be timely disclaimed by the survivor spouse.[234] But the same TAM allowed disclaimer of joint tenancy bank accounts and CDs because Pennsylvania law treated these latter accounts as owned pro-rata to contribution, and thus effectively subject to partition.[235]

Curiously, in PLR 91-35-044 the Service approved disclaimer of a one-half interest in a tenancy by the entirety residence which passed to the disclaimant by intestacy.[236] The disclaimer was allowed although it was made within nine months of decedent's date of death, not from creation of the tenancy by the entirety.[237] The issue of timeliness was not discussed, and may have been forgotten or lost in consideration of several other issues being ruled upon.

In PLR 90-12-053, dealing with a Virginia tenancy by the entirety, the surviving spouse sought to disclaim, but the IRS did not discuss whether Virginia law allows a tenancy by the entirety to be unilaterally severed.[238]

In TAM 94-27-003, the IRS reiterated its position that on a tenancy by the entirety the nine-month time limit for a disclaimer runs from the date of creation of the tenancy, not from the first death.[239]

VIII. WHO MAY SIGN A DISCLAIMER

A. *Attorney*

In *Estate of Allen*, the wife died first.[240] The husband died a few months later, and was the sole beneficiary under his predeceased wife's will.[241] The daughter-executor decided her father's estate should disclaim its interest in her

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231. *See* Priv. Ltr. Rul. 92-08-003 (Oct. 28, 1991).
232. Tech. Adv. Mem. 94-27-003 (Mar. 30, 1994).
233. *See id.*
234. *See* Tech. Adv. Mem. 95-29-001 (March 22, 1995).
235. *See id.*
236. Priv. Ltr. Rul. 91-35-044 (June 3, 1991).
237. *See id.*
238. Priv. Ltr. Rul. 90-12-053 (Dec. 27, 1989).
239. Tech. Adv. Mem. 94-27-003 (Mar. 30, 1994).
240. Estate of Allen, 1989 T.C.M. (RIA) ¶89,111, at 540, 541.
241. *See id.*

mother's estate.[242] Just before the deadline for filing the disclaimer, the executor went to Sun Valley on a vacation and was stuck there by bad weather.[243] She telephoned her Oregon lawyer and authorized him to sign and file the disclaimer on her behalf, which he did.[244] The Tax Court upheld that disclaimer because Oregon law allowed an oral agency in such circumstances.[245] Treasury Regulation section 25.2518-2(b)(1) only requires the disclaimer to be signed by the disclaimant or his "legal representative."[246]

B. *Executor*

In *Estate of Allen,* the Tax Court acknowledged that the executor was qualified to disclaim.[247]

1. In PLR 79-37-011, the Service apparently did not challenge the fact that the Montana executor could disclaim, but rather denied the disclaimer on the ground that the legatee for whom the executor was acting had an interest in an Iowa estate, and Iowa law did not allow a disclaimer after the legatee's death.[248]
2. In California, an executor or administrator is authorized by statute to disclaim.[249]
3. One commentator suggests that if the entire estate passes by an inter vivos trust, one should have an executor or administrator appointed to have a fiduciary who is clearly the decedent's "legal representative" disclaim.[250]

C. *Guardian*

PLR 83-26-110 upheld a disclaimer by a guardian on behalf of her minor daughter.[251]

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242. *See id.*
243. *See id.*
244. *See id.*
245. *See id.* at 543-44.
246. Treas. Reg. § 25.2518-2(b)(1) (1986)
247. Estate of Allen, 1989 T.C.M. (RIA) ¶89,111, at 540.
248. Priv. Ltr. Rul. 79-37-011 (May 31, 1979).
249. *See* CAL. PROB. CODE §§ 58(a), 277(b) (West 1991).
250. *See* Harold Weinstock, *The Marital Deduction: A Planning Update*, 41 MAJOR TAX PLAN. ¶1800, at 18-12 (1989).
251. *See* Priv. Ltr. Rul. 83-26-110 (Mar. 30, 1983); *see also* Tech. Adv. Mem. 90-03-007 (Jan. 19, 1990) (allowing disclaimer by a guardian ad litem for minor, unborn and unascertainable beneficiaries). *But see* Part VIII.F. *infra* regarding disclaimers by minors and Part VI.A.2. *supra* regarding disclaimers by fiduciaries.

D. *Trustee*

In *Cleaveland v. United States*, the court upheld a disclaimer by a trustee.[252] *Cleaveland* is a liberal result. The district court there allowed a trustee to qualify a trust as a QTIP by disclaiming the trustee's power to use both principal and income for the children's education.[253] The trustee's disclaimer was held to terminate the children's rights because they received notice but did not object.[254]

One should not rely on *Cleaveland* because in Revenue Ruling 90-110, the Service invalidated a trustee's attempt to qualify a trust for a QTIP election by trying to disclaim a power to invade corpus for a party other than the surviving spouse.[255] A disclaimer cannot be made by a fiduciary without the beneficiaries' consent or an express grant of authority in the governing instrument.

E. *Holder of Power of Attorney*

Disclaimer was upheld when made by holder of a durable power of attorney.[256] Consistent with Service's recent position on gifts made under a power of attorney for an incompetent, the power of attorney should expressly authorize a disclaimer.

F. *Problems on Disclaimers for Minors*

The Service has taken a negative position regarding disclaimers by minors in some circumstances. In *Estate of Goree*, a father died in an accident leaving a $2.5 million estate.[257] Decedent was intestate so under governing state law (Alabama) much of his estate would pass to his three minor children.[258] The children's mother had herself appointed conservator of the minors, and then obtained a court order authorizing her to disclaim on the children's behalf all but $200,000.[259] The disclaimed interest then passed to her, qualified for the marital deduction, and reduced the estate tax materially.[260] Both the decedent's father and the guardian ad litem supported the petition.[261] There was evidence the disclaimers allowed the

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252. Cleaveland v. United States, 62 A.F.T.R.2d (RIA) 5992 (C.D. Ill. 1988); *accord* Treas. Reg. § 25.2518-2(d)(2) (1986); Treas. Reg. § 25.2518-3(d) Ex. 9 (as amended in 1994). *But see* Part VI.A.2. *supra.*

253. *See id.* at 5994.

254. *See id.*

255. *See* Rev. Rul 90-110, 1990-2 C.B.

256. *See* Priv. Ltr. Rul. 90-15-017 (Jan. 10, 1990)

257. Estate of Goree, 68 T.C.M. (CCH) 123, 124 (1994).

258. *See id.* at 124-26.

259. *See id.* at 125.

260. *Id.*

261. *See id.* at 127-28.

mother to better care for the children, and that they could expect to inherit from her later.[262] The IRS disallowed the marital deduction but the Tax Court upheld the estate, finding that the decree authorizing the disclaimer was not "plainly and palpably erroneous" (the test under Alabama law).[263] The Tax Court refused to make its own determination on the propriety of the state court decree authorizing the disclaimer.[264] The Service has not given up; it announced non-acquiescence.[265]

It appears New York would allow disclaimers by a minor when the interest would pass to the widow.[266] But a New Jersey court refused to allow a disclaimer for a minor, saying it would not "affirmatively intercede to aid a plan when the sole purpose is the evasion of taxes."[267] The court there failed to distinguish between avoidance and evasion.

G. *Disclaimers by a Fiduciary*

See Part VI.A.2 *supra*.

IX. DISCLAIMERS TO CURE DRAFTING ERRORS, OR TO INCREASE, SAVE, OR DECREASE A MARITAL OR CHARITABLE DEDUCTION OR BYPASS

A. *Salvaging the Marital Deduction for pre-ERTA (before Sept. 12, 1981) and Other Non-Qualifying Wills and Trusts*

1. *Unlimited marital deduction*

The Economic Recovery Tax Act of 1981 (ERTA) created the unlimited marital deduction for estates of decedents dying after 1981.[268] Before that the maximum estate tax marital deduction was limited to the *greater* of $250,000 or 50% of the value of the adjusted gross estate.[269]

2. *Pre-ERTA documents may not qualify for unlimited marital deduction*

At the time ERTA was adopted, it was believed that if a pre-September 13, 1981 instrument used a pre-ERTA formula clause or referred to the "maximum

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262. *See id.* at 127.

263. *Id.*

264. *See id.* at 128.

265. *See* Estate of Goree v. Commissioner, 68 T.C.M. (CCH) 123 (1994), *action on decision*, 1996-001 (Mar. 4, 1996).

266. *See In re* Kramer, 421 N.Y.S.2d 975 (Sur. Ct. 1979).

267. *In re* Estate of Horowitz, 531 A.2d 1364, 1366 (N.J. Super. Ct. Law Div. 1987).

268. *See* Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, 1981 U.S.C.C.A.N. (95 Stat. 172) 105, 227-29.

269. *See id.*

marital deduction," the pre-ERTA law would limit the amount deductible unless a codicil or amendment executed after September 13, 1981 referred either to an unlimited marital deduction or the state involved enacted a statute that construed the words "maximum marital deduction" to mean the new unlimited marital deduction.[270] California adopted a statute stating that a reference to a "maximum allowable marital deduction," referred to in a pre-ERTA instrument, passes to the recipient only an amount equal to that allowed under the federal law which pre-dated ERTA.[271]

3. *1990* Levitt *case*

The Tax Court's decision in *Estate of Levitt v. Commissioner* offers hope in a state that does not have a statute like California's.[272] In *Levitt,* a 1975 revocable inter vivos trust provided that the marital trust was to receive the maximum marital deduction amount reduced by the value of other property qualifying for the marital deduction that passed outside of the trust.[273] A majority concluded the trustor's intent was to minimize federal estate taxes, not to limit the amount of property passing to the surviving spouse.[274] The court concluded the ERTA transition rules did not prohibit the estate from claiming the unlimited marital deduction.[275] *Levitt* has been followed in *Estate of Lucas.*[276]

4. For an excellent discussion of the problems of qualifying early wills for the marital deduction, see Edna R.S. Alvarez, *Saving the Marital Deduction for Pre-ERTA Wills*.[277]

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[270]. *See* Ronald D. Aucutt, *Marital Deduction Changes*, 1981 A.L.I.-A.B.A. STUDY OUTLINE ON THE ECONOMIC RECOVERY TAX ACT 333, 344-45.

[271]. *See* CAL. PROB. CODE § 21523 (West 1991).

[272]. *See* Estate of Levitt, 95 T.C. 3168 (1990).

[273]. *See id.* at 3171.

[274]. *See id.* at 3174.

[275]. *See id.* at 3175.

[276]. *See* Estate of Lucas, 61 T.C.M. (CCH) 1703 (1991); Priv. Ltr. Rul. 91-14-004 (Dec. 11, 1990), 92-06-006 (Oct. 24, 1991). In a somewhat different context the Ninth Circuit in *Estate of Ellingson v. Commissioner*, 964 F.2d 959 (9th Cir. 1992), allowed a QTIP qualification under an ambiguously drafted trust, based on the instrument that stated an express *intention* to so qualify.

[277]. *See* Edna R. S. Alvarez, *Saving the Marital Deduction for Pre-ERTA Wills,* TENTH ANN. U.S.C. PROB. AND TR. CONF. (University of Southern California Law Center), Nov. 16, 1984, at 4-1 (on file with the *Drake Journal of Agricultural Law*).

B. *Other Disclaimers Affecting the Marital Deduction*

1. *Saving noncomplying gifts of use of residence*

A gift of the use of a residence to a surviving spouse for "as long as she wishes to use it" does not (at least by itself) qualify for the marital deduction.[278] In TAM 91-40-004, the decedent had left his residence to his wife so long as she continued to use it and did not remarry.[279] Disclaimers of a life estate by the sons did not qualify because they retained the remainder interest in the same property.[280] The Service ruled that under the I.R.C. and the Regulations one cannot disclaim some interest in a property while retaining others in the same property when the interests were not separately created.[281] But see Part IX.B.4 & 5 *infra.*

There should be no objection, however, to language like that involved in these above PLRs if the residence is an asset of an otherwise qualifying marital trust in which the survivor spouse is entitled to all of the income in all events and has the power to direct the trustee to make the property productive. Many marital trusts contain discretionary residential use provisions. The problem is that a conditional occupancy right cannot simply stand alone. Even an ordinary life estate does not qualify for the marital deduction, if it does not meet the QTIP provisions of I.R.C. § 2056(b)(7).[282]

2. *Disclaimer to eliminate remarriage restriction*

In PLR 84-02-121 the spouse's interest in the testamentary trust was to terminate upon the earlier of the death *or the remarriage* of the surviving spouse, and to then pass to the children and the issue of any deceased child.[283] The spouse, children, and grandchildren all executed qualified disclaimers disclaiming *all* interests in the testamentary trust.[284] The will provided that if all these parties predeceased testator the property passed under the laws of descent.[285] The Service held the disclaimers effective to pass the entire property to the surviving spouse free of trust and this disclaimed interest qualified for the marital deduction.[286]

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278. *See, e.g.,* Tech. Adv. Mem. 93-01-005 (Sept. 30, 1992) (stating that a disclaimer by the remaindermen sufficed under Connecticut law to vest the house in the survivor and qualify for the marital deduction).

279. Tech. Adv. Mem. 91-40-004 (June 24, 1991).

280. *See id.*

281. *See id.*

282. *See* Estate of Bennett, 100 T.C. 42, 55-56 (1993).

283. Priv. Ltr. Rul. 84-02-121 (Oct. 14, 1983).

284. *See id.*

285. *See id.*

286. *See id.*; Priv. Ltr. Rul. 83-01-040 (Sept. 30, 1982).

3. *Disclaimers to create intestacy*

Several PLRs have approved marital deductions involving disclaimers that produced an outright intestate interest in the surviving spouse.[287] Be sure state law passes the interest where the client wants it to go before using such intestacy-producing disclaimers.

4. *Cannot disclaim after accepting income*

The holder of a trust income interest cannot disclaim that interest if the holder has accepted income, prior to making the disclaimer.[288]

5. *Disclaimers to increase marital deduction*

a. *Children's disclaimers of income.* If the children (or other beneficiary) have an interest in both principal and income in a trust in which they wish to relinquish only the income interest to the surviving spouse, such a disclaimer would be permitted under the Regulations.[289] The same result applies if only an interest in corpus is disclaimed.[290]

b. *Disclaiming life interest while retaining remainder interest.* Several Private Letter Rulings have upheld disclaimers of lifetime interests, although the disclaimant retains after-death interests (i.e., after the death of the surviving spouse).[291]

6. *Disclaimers to decrease the marital deduction*

a. *Spouse can disclaim interests in less than all trusts.* If the surviving spouse has an income interest in both the marital and non-marital trusts, the survivor may disclaim his or her interest in the marital trust without disclaiming his or her interest in the non-marital trust, and still have a valid disclaimer.[292]

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[287]. *See* Priv. Ltr. Rul. 84-09-089 (Nov. 30, 1983), 85-10-023 (Dec. 7, 1984), 84-02-121 (Oct. 14, 1983), 86-50-047 (Sept. 16, 1986), 87-29-008 (Apr. 8, 1986), 87-08-069 (Nov. 17, 1986).

[288]. *See* Treas. Reg. §§ 25.2518-2(d)(4) Ex. 1, 25.2518-2(c)(5) Ex. 6 (1986). *But see* Priv. Let. Rul. 92-14-022 (July 6, 1992) regarding disclaimer of segregable income.

[289]. *See* Treas. Reg. § 25.2518-3(d) Ex. 8 (as amended in 1994).

[290]. *See* Treas. Reg. § 25.2518-3(a)(1)(i) (as amended in 1994). *But see* Tech. Adv. Mem. 93-01-005 (Sept. 30, 1992) in Part IX.B.1. *supra.*

[291]. Priv. Ltr. Rul. 83-37-069 (June 15, 1983), 86-38-016 (June 19, 1986), 87-06-066 (Nov. 14, 1986), 89-06-036 (Nov. 14, 1988), 88-24-006 (March 10, 1988), 88-17-031 (Apr. 29, 1988), 88-15-038 (Jan. 21, 1988), 88-07-026 (Nov. 20, 1987), 87-04-023 (Oct. 24, 1986). *But see* Tech. Adv. Mem. 93-01-005 (Sept. 30, 1992).

[292]. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 6 (1986).

b. *Formula disclaimer.* *Estate of McInnes* upheld a formula disclaimer by the surviving widow of an amount necessary to reduce the husband's taxable estate to $500,000.[293]

"Circuitous" Formula Clause; Oil & Gas. In *Estate of Nix*, decedent's will gave his spouse various assets, including a pecuniary gift of an amount that produced the lowest federal estate tax.[294] The widow disclaimed various specific assets including certain oil and gas royalties and working interests.[295] At date of death the estate value was more than $1,594,000 but on the estate return the personal representative claimed a zero tax, asserting that the formula gift took into consideration the spouse's disclaimer and under the formula thus caused additional property to pass to the spouse so there was still no tax.[296] The Service disagreed and the Tax Court upheld a $191,000 deficiency.[297] The Service argued the formula was "circuitous."[298] The Service often does this when a disclaimer is used to create a taxable estate, because in such cases the survivor spouse often has a short life expectancy. One defense to this Service position is to specify in any formula clause used that the formula amount be determined without regard to any disclaimers.

c. *Percentage interest* . Similarly, a surviving spouse may disclaim a percentage interest in a marital trust.[299] If the will so provides, the disclaimed interest may pass to the non-marital trust, so long as it does so without any direction by the surviving spouse.[300]

d. *Receiving widow's allowance may bar disclaimer.* A surviving spouse cannot disclaim an interest if the spouse previously had the expenses paid by the estate (presumably by family or widow's allowance) even if the spouse repaid those prior receipts after the disclaimer.[301] The survivor should still be able to disclaim, however, particular properties out of a marital trust if it can be demonstrated that none of the spouse's family allowance was paid out of the income from the properties being disclaimed.[302]

e. *Remainder disclaimer; required segregation of disclaimed specific asset or trust portion.* A remainderman also may disclaim his or her interest

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293. Estate of McInnes v. Commissioner, 64 T.C.M. (CCH) 840 (1992).
294. Estate of Nix v. Commissioner, 71 T.C.M. (CCH) 2347 (1996).
295. *See id.* at 2348.
296. *See id.*
297. *See id.* at 2347.
298. *See id.* at 2350.
299. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 4 (1986). Priv. Ltr. Rul. 94-35-014 (June 2, 1994).
300. *See* Treas. Reg. § 25.2518-2(e)(5) Ex. 4 (1986).
301. *See* Priv. Ltr. Rul. 84-05-003 (Oct. 11, 1983).
302. *See* Priv. Ltr. Rul. 92-14-022 (Jan. 6, 1992) (regarding non-acceptance of benefits from joint tenancy brokerage account); Treas. Reg § 25.2518-3(d) Ex. 17 (as amended in 1994).

in a marital trust, or an undivided portion thereof, or in specific assets, without making a taxable gift.[303] Note, however, the requirement under Part VI.A.3 & 8. *supra* of segregating trust property, following a disclaimer of an interest in specific trust assets.

f. *Surviving spouse can disclaim specific gift though she takes residuary income.* A surviving spouse may disclaim a bequest to the spouse even though the disclaimed property will thereby fall into the residuary trust of which the spouse is an income beneficiary.

7. *Some deficiencies not salvable; state law restrictions*

In *Estate of Bennett*, decedent had established two trusts, neither of which fulfilled marital deduction criteria.[304] The trust instrument was devoid of any provision stating an intention to qualify the trust in issue for the marital deduction.[305] Local (Kansas) law restricted a court from "correcting a mistake" unless it appeared on the face of the instrument and complied with the decedent's apparent intentions.[306] The trustees did a court approved reformation and several beneficiaries signed disclaimers.[307] The Tax Court recognized that proper reformation *could* be retroactive, and that the Regulations expressly contemplate disclaimers in favor of the surviving spouse.[308] But the Tax Court held it was not bound by the local state court judgment, and that: (a) under Kansas state law the decedent's intent governed and the estate had no power to rewrite the unambiguous trust; (b) that the trustees' attempted disclaimers "would amount to renunciation of their trusteeships;" and (c) that certain of the beneficiary disclaimers were invalid under Kansas law because they were not filed with the court and because they did not effect transfers under local law.[309]

8. *Limitations on fiduciary disclaimers*

A valid disclaimer by a fiduciary requires consent of a beneficiary or an express authorization in a governing instrument.[310]

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303. *See* Priv. Ltr. Rul. 78-49-009 (Sept. 5, 1978).

304. Estate of Bennett, 100 T.C. 42, 64 (1993).

305. *See id.* at 63.

306. *See id.* at 61.

307. *See id.* at 50.

308. *See id.* at 61.

309. *Id.* at 66

310. Rev. Rul. 90-110, 1990-2 C.B. 209. *But see* Cleaveland v. United States, 62 A.F.T.R.2d (RIA) 148 (C.D. Ill. 1988); Treas. Reg. §§ 25.2518-2(d) (1986), 25.2518-3(d) Ex. 9 (as amended in 1994).

9. *Example of correction of drafting error regarding marital deduction*

A large number of PLRs are sought to correct drafting errors.[311] In PLR 83-37-069, a will was drafted after the 1981 ERTA but gave the trustee powers of invasion for decedent's daughter's benefit instead of limiting the benefit to the widow.[312] The daughter disclaimed,[313] saving the drafting lawyer from a malpractice claim.

In TAM 92-47-002, disclaimers by the children of discretionary payments of principal and income qualified the trust for a QTIP marital deduction.[314]

10. *Funding bypass trust*

Examples of PLRs that allowed disclaimers to adequately fund a decedent's bypass trust, and thus fully utilize his unified credit (exemption equivalent) include the following:

a. PLR 91-13-011,[315] which involved a disclaimer of joint tenancy brokerage account to fund bypass; and

b. PLR 90-36-028,[316] which involved a disclaimer of fractional share tied to settlor's unified credit.

11. *Qualifying bypass for marital deduction*

Ordinarily the bypass trust is preserved intact because it is not included in the surviving spouse's estate. There may, however, be a need in exceptional cases. See the following:

a. Bypass in a pre-ERTA will revised to qualify for marital deduction.[317]

b. Disclaimer by family of a right to income from bypass trust was allowed to qualify for QTIP.[318]

c. Disclaimers by children of discretionary income rights and principal distributions qualified for marital deduction.[319]

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311. *See*, *e.g.*, Priv. Ltr. Rul. 83-37-069 (June 15, 1983).
312. *See id.*
313. *See id.*
314. Tech. Adv. Mem. 92-47-002 (Nov. 20, 1992).
315. Priv. Ltr. Rul. 91-13-011 (Dec. 24, 1990).
316. Priv. Ltr. Rul. 90-36-028 (June 12, 1990).
317. *See* Priv. Ltr. Rul. 89-35-024 (Sept. 1, 1989).
318. *See* Priv. Ltr. Rul. 87-04-023 (Oct. 24, 1986).
319. *See* Tech. Adv. Mem. 92-47-002 (Nov. 20, 1992).

12. *Disclaimer of 5 and 5 power while keeping income interest*

In PLR 79-28-054,[320] the Service relied on changes made by the Revenue Act of 1978 to rule on a proposed disclaimer. PLR 84-35-056 also allowed a surviving spouse to disclaim her 5 and 5 power ($5,000 or 5% of corpus per year) while retaining her income interest in the trust and her co-trustee fiduciary powers.[321]

13. *Disclaimer permitted after election against will*

In Rev. Rul. 90-45, the Service ruled that a surviving spouse could still make a qualified disclaimer after the spouse had elected to take an intestate share of the estate against the deceased spouse's will, as long as the surviving spouse's disclaimer was timely.[322]

14. *Guardian ad litem*

If disclaimers are needed from beneficiaries who are minors, unborn, or unascertainable, consider seeking the appointment of a guardian ad litem for such purposes. The Service ruled favorably on disclaimers that included those by a guardian ad litem in TAM 90-03-007.[323] The disclaimers there saved a QTIP marital deduction by relinquishing the rights of non-spousal beneficiaries to receive income.[324] See Part IX.B.15.c. *infra* regarding disclaimers by a fiduciary.

15. *Caveats*

a. If the disclaimer is of a specific trust asset, or is of a pecuniary amount from a bequest, be sure the discla
b. Be sure the disclaimant has not accepted any benefits (such as a widow's or family allowance). (See Part IX.B.6.d. *supra*).
c. See Part VI.A.2. *supra* regarding limitations on disclaimers by a fiduciary (express authorization required).
d. Be sure the other elements of a *qualified* disclaimer (see Part II.A. *supra*) are fulfilled.

Estate of Fleming illustrates the time trap.[325] In *Fleming,* the disclaimer by an executor was held untimely because it was filed within nine months of the date the

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320. Priv. Ltr. Rul. 79-28-054 (Apr. 16, 1979).
321. Priv. Ltr. Rul. 84-35-056 (May 29, 1984).
322. Rev. Rul. 90-45, 1990-1 C.B. 176.
323. Tech. Adv. Mem. 90-03-007 (Jan. 19, 1990).
324. *See id.*
325. Estate of Fleming, 58 T.C.M. (CCH) 1034 (1989).

decedent's will was admitted to probate, rather than nine months after his date of death, which was the date the interest transferred.[326]

C. *State Court Actions To Reform A Trust May Be Risky*; Nicholson *case*; *State Court Reformation Not Binding on IRS*

Using disclaimers to qualify an otherwise ineligible trust for the marital deduction seems safer than attempting to modify or reform the trust in state court. In *Estate of Nicholson v. Commissioner,* the decedent and his wife had created a pre-ERTA trust that gave the surviving spouse only so much of the net income as was necessary to maintain her standard of living, thus not meeting the requirement that the surviving spouse receive all of the income.[327] The trustees brought suit in Texas state court to reform the trust, and obtained an order modifying the trust so as to require the trustee to pay all income to the surviving spouse.[328] The IRS was not a party to the suit.[329] On the basis of the reformation order the executor treated the surviving spouse's interest as a QTIP, which election the Service denied and assessed a deficiency.[330] The Tax Court upheld the Service, for what appears to be three separate reasons as follows: (a) Texas law did not allow a court to consider statutes enacted after the trust became effective;[331] (b) the trust was not ambiguous because it gave the widow only enough income to maintain her customary living standard and the rest to the remaindermen;[332] (c) it refused to uphold a state court modification made after the IRS "ha[d] acquired rights to tax revenues . . . ."[333]

In *Estate of Ellingson v. Commissioner*, the court cited *Nicholson* favorably regarding reformation, but nevertheless reversed the Tax Court and upheld a rather poorly drafted trust as qualifying for a QTIP marital deduction, largely because the settlor's intent to so qualify was expressly stated in the trust.[334]

In *Commissioner v. Estate of Bosch*, the Supreme Court held it would not give finality in a tax controversy to a state court's decision on an underlying state law issue, unless the decision was by the state's highest court.[335] The IRS often accords little weight to routine decisions of a state probate or trial court.[336]

The Service's position on reformation seems ambiguous, however, because:

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326. *See id.* at 1036-37.
327. Estate of Nicholson v. Commissioner, 94 T.C. 666 (1990).
328. *Id.*
329. *Id.*
330. *Id.*
331. *Id.*
332. *See id.* at 674-78.
333. *See id.* at 680.
334. Estate of Ellingson v. Commissioner, 964 F.2d 959, 963 (9th Cir. 1992).
335. Commissioner v. Estate of Bosch, 387 U.S. 456, 465 (1967).
336. *See*, *e.g.*, Rev. Rul. 73-322, 1973-2 C.B. 44.

a. In PLR 89-02-045, (a sixteen-page dissertation), the Service upheld as non-taxable a trust reformation in settlement of a dispute.[337] The key point was the fact the dispute was bona fide and the settlement was at arms-length.

b. In PLR 90-17-015 the Service upheld Qualified Domestic Trust qualification under I.R.C. § 2056A for the benefit of a non-citizen surviving spouse under a trust that had been reformed by the local probate court's order entered before the due date for the decedent's estate tax return.[338]

c. See PLR 90-07-016, discussed under Part XI *infra*, which involved a reverse QTIP, the IRS required the still-living testator to modify his will.[339] It is hard to know if the IRS would have permitted this change by a post-death reformation, because this taxpayer was still living.

X. DISCLAIMERS AFFECTING CHARITABLE DEDUCTION

A. *Failed Disclaimers*

A worst case scenario is TAM 87-30-004, discussed *supra* at Part III.E.7, where a non-charitable secondary income beneficiary of a charitable remainder trust failed to disclaim in time, thus causing an estate tax exceeding $5.3 million.[340]

B. *Successful Charitable Disclaimers*

1. In PLR 93-17-039, decedent's children disclaimed favor of several foundations, each child's disclaimer passing to a particular foundation.[341] As originally structured, each foundation's bylaws allowed the child to participate in the foundation's distribution decisions.[342] To cleanse what would be a violation of the I.R.C. § 2518(b)(4) requirement that the disclaimed property "pass without direction" by the disclaimant, the Service allowed each foundation to amend its bylaws to segregate the disclaimed assets and have them administered by trustees independent of the disclaimant.[343]

2. PLR 95-50-026 allowed the husband-wife creators of an irrevocable charitable remainder unitrust funded with their community property, to disclaim to the charitable remainder University a portion of their retained unitrust (income)

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337. Priv. Ltr. Rul. 89-02-045 (Jan. 13, 1989).
338. Priv. Ltr. Rul. 90-17-015 (Apr. 27, 1990).
339. Priv. Ltr. Rul. 90-07-016 (Feb. 16, 1990).
340. Tech. Adv. Mem. 87-30-004 (Apr. 15, 1987).
341. Priv. Ltr. Rul. 93-17-039 (Feb. 2, 1993).
342. *See id.*
343. *See id*

interest.[344] Among other points, the Service ruled the donors qualified for income tax and gift tax charitable deductions.[345]

3. PLR 95-32-026 allowed a charitable deduction for a charitable remainder unitrust, following disclaimers by the non-charitable remainder beneficiaries.[346]

4. In companion PLR 95-32-027, the disclaimant had the right to recommend who was to receive grants from the charitable fund.[347] The Service ruled a disclaimer by the donor did not violate the rule that the property "pass without direction," because the donor could only recommend grant recipients and the charity made the final decision.[348]

5. Since 1964, to qualify for a charitable deduction, a split-interest charitable remainder trust must be an annuity trust or a unitrust.[349] Examples of disclaimers (sometimes coupled with reformations) to qualify old trusts for charitable deduction include PLRs 90-04-011, 85-50-018, and 78-21-045.[350]

C. *Related Ninety Day time Limit on Reformation of Charitable Trusts*

Although not a disclaimer issue, if an attorney is considering disclaimers in a charitable trust but wishes also to consider a state court reformation, he should be aware of the strict ninety day limit for such reformations under I.R.C. § 2055(e)(C)(iii). In addition, PLR 95-49-016 concluded that a charitable remainder interest was not reformable under § 2055(e)(3).[351]

XI. DISCLAIMERS AFFECTING THE GENERATION SKIPPING TRANSFER TAX AND COMBINED DISCLAIMERS

A. *GST Tax Background*

The Generation Skipping Transfer Tax (GST Tax) as originally enacted in 1976 was *substantially* revised in 1986.[352] Despite superficial similarities, the 1986

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344. Priv. Ltr. Rul. 95-50-026 (Dec. 15, 1995).

345. *See id.*

346. Priv. Ltr. Rul. 95-32-026 (May 12, 1995).

347. Priv. Ltr. Rul. 95-32-027 (May 12, 1995).

348. *See id.*

349. *See* 26 U.S.C. § 664(d)(1)(2) (1994).

350. Priv. Ltr. Rul. 90-04-011 (Jan. 26, 1990), 85-50-018 (Sept. 12, 1985), 78-21-045 (Feb. 23, 1978).

351. Priv. Ltr. Rul. 95-49-016 (Dec. 8, 1995).

352. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2717; Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1879.

GST Tax contained in Chapter 13 is different than its predecessor.[353] One should *not* rely on GST Tax rulings or cases based on the pre-1986 revision. The revised Act generally applies to dispositions made after October 22, 1986. A complete summary of the present GST Tax is beyond the scope of this paper, but these are some of the most important points:

1. The old $250,000 "grandchild exclusion" under the 1976 Act was abolished.

2. *$1,000,000 GST Exemption*. Each individual now has a $1,000,000 GST exemption, under I.R.C. § 2631.[354] Allocations made of that exemption are irrevocable. The $1,000,000 exemption is not transferrable, not even between spouses. Note that this exemption does not track with the $600,000 per transferor exemption equivalent under the estate tax. If a married couple wishes to use their combined $1.2 million estate tax exemption equivalent, and also to use up while alive their respective $1,000,000 GST Tax exemptions, the $800,000 difference between the two ($400,000 per transferor) will be subject to a gift tax.

3. All transfers subject to the GST Tax which exceed the $1,000,000 per transferor exemption, are at the highest estate tax rate. Usually this is a flat 55% rate, but the rate increases by 5% for estates exceeding $10,000,000.[355]

4. The so-called "Gallo" exemption, which previously allowed an additional $2,000,000 per grandchild exemption, is no longer available, as such disclaimers had to be made before the end of 1989.[356]

5. If spouses make a "gift splitting" election under I.R.C. § 2513 for gift tax purposes on a lifetime gift, the split is also recognized for GST Tax purposes.[357] But one cannot split the $1,000,000 GST Tax exemption.

6. "Direct skips," "taxable distributions," and "taxable terminations" are still subject to the GST Tax, but with some modifications over the 1976 Act.

7. Multi-generational trusts that are *not* "grandfathered" (*see infra*) are subject to repeated taxation at successive generations below the transferor.

8. Trusts that were irrevocable before September 25, 1985 *and* are not includable in the grantor's estate under § 2038 (regarding certain retained powers),

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353. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2717; Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1879.

354. *See* 26 U.S.C. § 2631(a) (1994).

355. *See* 26 U.S.C. § 2641(a)(1) (1994). *See, e.g.* 26 U.S.C. § 2001(c)(1)(2) (1994).

356. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2731.

357. *See* 26 U.S.C. § 2652(a)(2) (1994).

are "grandfathered" and are exempt from the current GST Tax. An extension of a "grandfathered" trust is also grandfathered if done under a non-general power of appointment that's part of the original trust. But any modification done after the September 25, 1985 cutoff date destroys grandfathered status.[358]

9. Under the "predeceased child rule," the GST Tax does not apply to a transfer to a younger generation (typically a grandchild) whose parent predeceased the transfer. But a state statute treating a disclaimant as having predeceased a decedent is not effective to qualify under the "predeceased child rule."[359]

10. *New Final GST Regulations*. The Service operated under Proposed and Temporary Regulations for a long time. New Final Regulations were issued on December 27, 1995.[360] These Final Regulations differ from the predecessor Temporary Regulations, thus care must be taken with authorities that rely on the earlier versions.[361] The Final Regulations now mandate the payment of interest on death-time transfers from the date prescribed by local law (such as the one-year delay under California law).

B. *Reverse QTIP Election for GST Tax Purposes*

I.R.C. § 2652(a)(3) allows the transferor of QTIP property to elect irrevocably to treat such property for GST Tax purposes as if the QTIP election had not been made (*i.e.*, the "reverse" QTIP election).[362] In some situations this election is necessary to avoid losing the benefit of some or all of the transferor's $1 million GST Tax exemption. This election is not available for a general power of appointment marital trust, but there may be instances in which disclaimers may be used to convert all or some of a general power of appointment trust into a QTIP trust, thereby qualifying for the I.R.C. § 2652(a)(3) election.

In PLR 90-07-016, involving division of QTIP trusts to reflect a reverse QTIP election, the Service required the still surviving testator to add a provision to his will calling for division of the marital residue in compliance with Revenue

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358. *See* Edward C. Halbach, *Understanding and Working with the Generation-Skipping Transfer Tax*, GENERATION-SKIPPING PLANNING, (Continuing Education of the Bar, Cal.) June/July 1996, at 3.

359. *See* Treas. Reg. § 26.2612-1(a)(2) (1995).

360. *See* Treas. Reg. § 26.2611-1 (1995).

361. *See* Treas. Reg. § 26.2654-1(a)(1)(ii)(A) (1995) (referencing the "appropriate interest" requirement under the valuation rules); *Generation Skipping Transfer Tax*, 18 EST. PLAN. & CAL. PROB. REP. (Continuing Education of the Bar, Cal.) Aug. 1996, at 14-15 (on file with the *DRAKE JOURNAL OF AGRICULTURAL LAW*); Jeffery A. Dennis-Starthmeyer, *The Not-So-Final GST Regulations: Good, Bad, and Ugly!*, 17 EST. PLAN. & CAL. PROB. REP. (Continuing Education of the Bar, Cal.) Feb. 1996, at 104 (on file with the *Drake Journal of Agricultural Law*).

362. *See* Treas. Reg §§ 26.2652-1(a)(6) Ex. 6, 26.2652-2(d) Ex. 1 (1995).

Procedure 64-19.[363] Revenue Procedure 64-19 requires that when assets used to satisfy a pecuniary marital gift are valued at federal estate tax values, rather than the date of distribution values, the assets distributed to the marital deduction must be collectively "fairly representative" of post-death appreciation and depreciation of all the assets then available in the estate to satisfy the pecuniary gift.[364]

A reverse QTIP election generally is not effective unless it is made with respect to all of the property in the subject QTIP trust. But since the 1988 amendment to the statute, a QTIP trust can be split into two separate trust, allowing for separate elections to be made with respect to all of the property in one of split trusts.[365] For a convoluted disclaimer involving a reverse QTIP with respect to multiple trusts, see PLR 93-29-025.[366]

In PLR 90-28-005, the survivor spouse was permitted to disclaim a general power of appointment with respect to one half of a trust.[367] A QTIP election was made for the disclaimed share and a reverse QTIP election was made as to a portion of the disclaimed share.[368] The attorney there also split the trust in a court proceeding in order to utilize the unused portion of the decedent's GST Tax exemption.[369]

C. *Disclaimers Designed to Fully Utilize the Deceased Spouse's $1,000,000 GST Tax Exemption*

In a recent estate handled by the author's office, the decedent had established a $450,000 trust for his grandchildren, and had left the residue (after carving out a QTIP and various other trusts) to his surviving spouse. The residuary clause provided that if the spouse failed to survive the testator, the residue would go to decedent's son. If he failed to survive the testator, the residue was to be divided into four equal shares between the decedent's daughter-in-law and his three grandchildren.

The surviving spouse elected to disclaim an additional $550,000, which, when added to the original $450,000 trust for the grandchildren, would fully utilize the decedent's $1,000,000 GST Tax exemption. The family agreed that the son and daughter-in-law would also disclaim, so that neither of them would have any interest in the $550,000 interest disclaimed by the surviving spouse, and it would then pass

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363. Priv. Ltr. Rul. 90-07-016 (Feb. 16, 1990).

364. *See id.*

365. *See* Priv. Ltr. Rul. 91-33-016 (Aug. 16, 1991).

366. Priv. Ltr. Rul. 93-29-025 (July 23, 1993).

367. Priv. Ltr. Rul. 90-28-005 (July 13, 1990).

368. *See id.*

369. *See id.* See Edna R.S. Alvarez, *Post-Mortem Reconstruction of the Marital Deduction—QTIPS, Disclaimers and Other Tools*, 44 MAJOR TAX PLAN. ¶1200, at 12-1 (1992), for further examples discussing the earlier version of the Regulation.

pursuant to other provisions of the decedent's will to the grandchildren's trust. A unpublished PLR approved this.

PLR 92-03-028 upheld the use of pecuniary formula disclaimers to reduce residuary gifts to grandchildren to a total of $1 million.[370] There were additional disclaimers by the testator's great-grandchildren.[371] These caused the balance of the residue of the estate to go to the testator's daughter, thus eliminating any GST Tax in the estate.[372] This ruling provides guidance, as follows:

(i) The disclaimers there, using primarily a formula under which only the maximum amount that could pass free of the GST Tax would pass to the grandchildren, were held to constitute qualified disclaimers of a specific pecuniary amount, so long as they were delivered to the executrix within nine months after the decedent's death.[373]

(ii) This PLR also approved the executrix's allocating decedent's $1 million GST Tax in equal shares to the shares held for each grandchild.[374] The Service agreed that the disclaimed property would all pass under governing state law to the decedent's daughter, who was a non-skip person.[375]

D. *Broad Definition of a Trust for GST Purposes*

For GST purposes a trust includes many arrangements that clearly are not trusts under state law. Treasury Regulation section 26.2652-1(b)(1)[376] defines a "trust" very broadly as follows:

> A trust includes any arrangement (other than an estate) that has substantially the same effect as a trust. Thus, for example, arrangements involving life estates and remainders, estates for years, and insurance and annuity contracts are trusts. Generally, a transfer as to which the identity of the transferee is contingent upon the occurrence of an event is a transfer in trust; however, a transfer of property included in the transferor's gross estate, as to which the identity of the transferee is contingent upon an event that must occur within 6 months of the transferor's death, is not considered a transfer in trust solely by reason of the existence of the contingency.

Thus disclaimers should be considered in any situation with GST Tax exposure if any of the above categories of interests are present.

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370. Priv. Ltr. Rul. 92-03-028 (Jan. 17, 1992).

371. *See id.*

372. *See id.*

373. *See id.*

374. *See id.*

375. *See id.; see also* Priv. Ltr. Rul. 95-13-011 (Dec. 29, 1994) (stating that GST Tax disclaimer which produced a zero inclusion ration, thus preserving decendent's $1,000,000 GST exeption).

376. *See* Treas. Regs. § 26.2652-1(b)(1) (1995).

E. Dividing a Trust Into GST-Exempt and Non-Exempt Parts; Great Care for Grandfathered Trusts

1. *Division*

If the size of a trust exceeds $1 million and the transferor has not already used his or her $1 million exemption, consideration should be given to splitting the trust into exempt and non-exempt parts. The two parts can be mirror images of each other. In California this is accomplished by a Court petition under the Probate Code. Many states have similar statutes. If a particular state has no enabling statute, counsel could request the court to entertain such a petition under the court's historic equity jurisdiction over trusts. If a charitable trust is involved, the *cy pres* doctrine may help.

PLR 90-28-005 includes an example of a division of a trust for tax purposes.[377] PLR 91-26-020 allowed division of a trust on a fractional basis.[378]

In PLR 90-20-017, in passing on a request to divide a GST Tax trust, the Service stated:

> The mere partitioning of a trust that does not otherwise change the quality, value, or timing of any of the powers, beneficial interests, rights, or expectancies originally provided for under the terms of the trust will not prevent the resulting trust interest from being treated as a trust in existence on the date of the original trust instrument for purposes of Chapter 13 of the Code.[379]

2. *Disclaimer in connection with division*

Whenever a trust involves provisions or powers that suggest a need for disclaimers for other reasons, such as estate tax QTIP qualification, one should consider a concurrent division of the trust if its original size is larger than the decedent's unused $1 million GST Tax exemption.

3. *Time limit on division; funding the severed trust*

The Regulations on the QTIP marital deduction trust (generally effective March 1, 1994), require that divisions into separate trusts to effect a partial QTIP election must be accomplished before estate administration is completed.[380] The

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377. Priv. Ltr. Rul. 90-28-005 (July 13, 1990).

378. Priv. Ltr. Rul. 91-26-020 (June 28, 1991).

379. Priv. Ltr. Rul. 90-20-017 (May 18, 1990); *see* Priv. Ltr. Rul. 89-51-068 (Dec. 22, 1989); Priv. Ltr. Rul. 89-27-026 (July 7, 1989).

380. Treas. Reg. § 20.2056(b)-7 (1994).

severed trusts must be funded at full market value on the division date.[381] The trust, however, does not have to contain a pro rata share of each asset.[382]

F. *Use Great Care on GST Tax Grandfathered Trusts*

Great care is essential when dealing with any disclaimers relating to a trust which is otherwise grandfathered from the GST Tax. Before utilizing a disclaimer with respect to any trust that was otherwise "grandfathered" for GST Tax purposes, a Private Letter Ruling should be obtained.

XII. DISCLAIMERS FOR INCOME TAX PURPOSES

A. *Transfer to Lower Tax Bracket*

The beneficiary of a will or trust who has adequate income, or who is in a higher bracket, may wish to disclaim the right to the income to the next generation, assuming the will or trust does not specify that it goes elsewhere if the disclaimant fails to survive the decedent. Such a disclaimer of an income interest is permitted under Treasury Regulation section 25.2518-3(a)(1).[383]

B. *Avoid DNI*

A less obvious application is a disclaimer by a beneficiary to avoid the *estate's* distributable net income (DNI) being deemed distributed to the beneficiary, because the will or trust allows the gift to be funded in property or cash.

1. The basic income tax problem, if the income estate is substantial, is that all DNI will be deemed distributed (up to the amount of the distribution) to any beneficiary who receives distribution of a pecuniary gift which is not a specific gift, even though the distribution is all principal for state trust law purposes and fiduciary accounting purposes.

2. To constitute a "specific" gift (which does not carry out DNI upon any distribution), the gift or bequest must be of a *specific sum of money* or *specific property*. Further, the amount of the money or the identity of the specific property must be ascertainable under the terms of the will or trust as of the date of death.[384]

3. Thus a gift that is in a stated dollar amount, or is a piece of specifically described property, does not carry out DNI upon distribution.

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381. *See* Treas. Reg. § 20.2056 (b)-7 (b)(2)(ii)(B) (1994).
382. *See id.*
383. *See* Treas. Reg. § 25.2518-3(a)(1) (June 10, 1994).
384. *See* 26 U.S.C. § 663(a) (1994); Treas. Reg. § 1.663(a)-1(b)(1) (1960).

4. If, however, the will or trust makes a gift of cash *or property* having a value of $50,000, the gift is not a "specific" gift within the meaning of I.R.C. § 663(a) and the Regulations.

5. Such a cash or property gift leaves the executor or trustee with discretion as to how to fund.

6. In such circumstances it may be possible for the executor or trustee and the beneficiary to disclaim any right to fund the gift with any property other than cash. Such a disclaimer, if successful, would qualify the bequest as a "specific" gift that would not carry out DNI. The result is that if a distribution is then made to such a beneficiary in a form which would be principal for state law purposes, *no* DNI is deemed to be carried out with it. Consequently, the DNI is taxed to the estate or trust itself (if there are no other distributions that carry out DNI), or is deemed passed out to any other beneficiary to whom "non-specific" property is distributed during the current year. The author's office has utilized such a disclaimer, but it has not been tested upon audit, so no representation is made as to effectiveness of such disclaimer. Note, however, the current 39.6% tax rate on trust and estate income of more than $7,900.

7. Although no specific authority has been found for this precise sort of disclaimer (to avoid taxability to beneficiary of income which is deemed distributed to an estate beneficiary upon his or her receiving a principal distribution), it appears to be within the spirit of the final Regulations, Letter Rulings, and case law, as follows:

a. a trustee who has a power to invade corpus for a designated beneficiary (and who does not have any other power such as the power to appoint property in the corpus) may disclaim that power to invade,[385] and

b. *Cleaveland v. Untied States* allowed a trustee to disclaim its power to divert trust funds for the college education of decedent's children.[386] The children did not join in the disclaimer because of the then-extant Proposed Regulations.[387] The court analogized the invasion power being disclaimed to a power of appointment; [388]

c. In PLR 90-17-015, the Service allowed a trust to be reformed to meet the Qualified Domestic Trust requirements of I.R.C. § 2056A; [389]

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385. *See* Treas. Reg. § 25.2518-3(d) Ex. 9 (as amended in 1994).

386. Cleaveland v. United States, 62 A.F.T.R.2d 5992, 5993 (Dist. Ct. Ill. 1988).

387. *See id.*

388. *Id.* at 5994.

389. Priv. Ltr. Rul. 90-17-015 (Jan. 25, 1990).

d. The Regulations allow a person to make a qualified disclaimer of a beneficial interest in property even if after such disclaimer the disclaimant (like the trustee in the example) has the fiduciary power to distribute to designated beneficiaries, subject to an ascertainable standard;[390]

e. Such a disclaimer logically should not run afoul of the prohibition against a disclaimer of a "partial interest"[391] because only the funding method is affected, not the amount of the gift; and

f. In PLR 89-02-045 the Service upheld the reformation and partition of a trust in settlement of a dispute regarding various aspects of the trust and its administration.[392] New trustees were appointed, investment authority was clarified, principal allocations and charges were established, and beneficial interests were redefined, all pursuant to an arm's length settlement agreement.[393]

XIII. GET A RULING

Much of the authority on disclaimers is in the form of PLRs, but they cannot even be cited to a court as precedent. A Private Letter Ruling should be sought on any proposed disclaimer that involves a significant economic impact. Because ruling requests require substantial turn around time, they should be sought early. Note that an extension of time to file the estate tax return does not extend the time to disclaim.

XIV. SLIGHTLY IMPROVED AUTHORITY STATUS OF PLRS, TAMS, AND GCMS

Private Letter Rulings are of course not authority that binds the Service as to anyone except the taxpayer to whom the PLR was issued. Private rulings, however, may provide authority to avoid a penalty. Private Letter Rulings, Technical Advice Memoranda, Actions On Decisions, and General Counsel Memoranda issued since 1984 may be treated as authority for avoidance of the penalty for substantial understatement of income tax imposed by § 6662, provided they have been released to the public.[394]

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390. *See* Treas. Reg. § 25.2518-2(e)(1)(ii) (1986).
391. *See* Treas. Reg. § 25.2518-3(a)(1)(i) (as amended in 1994).
392. Priv. Ltr. Rul. 89-02-045 (Oct. 21, 1988).
393. *See id.*
394. I.R.S. Notice 90-20, 1990-10 C.B. 328.