Disclaimers: When the Usual Rules May Not Apply

by William D. Brewer
Hershner Hunter, LLP

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Disclaimers are useful tools, both for designing estate plans, and for making post mortem corrections to plans. Most of us know the basic rules of disclaimers, but sometimes these rules don't apply. Although the situation is not, as a Firesign Theatre album once proclaimed, that *Everything You Know Is Wrong*, there are instances where a valid disclaimer seems to violate well understood rules. A few of those instances are discussed below:

1. More than 9 months have passed since the decedent's death. Is it too late to use a disclaimer? Not necessarily.

The author was recently asked to assist a trustee after disclaimers had been used in an unsuccessful attempt to correct a generation-skipping problem. More than 15 months after the decedent's death the IRS auditor said the original disclaimers created a new and worse problem. The solution? New disclaimers.

The decedent had created a trust which left his entire estate to his grandchildren, all of whom were adults. However, the decedent's estate was large enough to trigger more than $700,000 in generation skipping transfer taxes. The trustee's advisors had suggested that the grandchildren and great grandchildren execute disclaimers, so that the decedent's only child would inherit enough of the estate (passing by intestacy as a result of the disclaimers) to eliminate the generation skipping transfer tax. The great grandchildren were minors, so their parents had executed the disclaimers on their behalf.

On audit, the IRS contended that the minors' disclaimers were invalid because the disclaimers could be revoked by them when they became adults, in violation of the requirement in IRC § 2518(b) that disclaimers be irrevocable. The IRS had previously made the same argument in Tech Advice Mem 7947008 (Aug. 16, 1979), applying Georgia law. If the IRS position applied here, the great grandchildren inherited the disclaimed property, and the generation skipping transfer tax had to be paid.

Since all the great grandchildren were still under age 21, we petitioned the court to appoint guardians ad litem for them. The guardians ad litem made new and irrevocable disclaimers. Although the new disclaimers were signed more than two years after the decedent's death, they were valid because they were made before the disclaimants reached age 21. IRC § 2518(b)(2)(B).

The use of guardians ad litem or other court appointed fiduciaries to make irrevocable disclaimers on behalf of minors has been approved in *Estate of Lassiter v. Commissioner*, TC Memo 2000-324. *See also Estate of Robert W. Goree, Jr. v. Commissioner*, TC Memo 1994-331 (1994), *nonacq* 1996-1 C.B. 1, 1996-2 C.B. 1. For a case in which "late" disclaimers by minor grandchildren might have cured poorly planned disclaimers, see *Estate of Holden v. Holden*, 539 SE2d 703 (SC 2000).

2. A guardian ad litem for a child has a duty to act in the child's best interest. Does that duty prevent the guardian ad litem from disclaiming property that would otherwise benefit the child? No.

As discussed above, having a guardian ad litem or other fiduciary make a disclaimer for a minor can insure that the disclaimer is irrevocable. In *Estate of Goree v. Commissioner*, TC Memo 1994-331 (1994), *nonacq* 1996-1 C.B. 1, 1996-2 C.B. 1, the decedent died intestate leaving his second wife and the children of both marriages as his only heirs. The IRS argued that the partial disclaimers by the wife as conservator for the children, and the acquiescence in the disclaimers by the guardian ad litem for the children, could not be in the children's best interest, and therefore were invalid as a matter of state law. The tax court held the disclaimers valid. It agreed with the probate court that the wife's ability to provide for and care for the children would be enhanced if the federal estate tax liability were minimized. *See also Estate of Lassiter v. Commissioner*, TC Memo 2000-324.

Of course, a guardian ad litem might not agree to a disclaimer, particularly if the party who would receive the disclaimed assets is not a direct ancestor of the minor whose disclaimer is sought. This was apparently the case in *Fleenor v. Williamson*, 171 Or App 599 (2000).

3. An adult has taken possession of property or accepted benefits from it. Is it too late to make a disclaimer? Maybe not.

An adult under Oregon law who is under 21 (*see* ORS 109.425) may take possession of property or accept benefits from it, and still disclaim the property within 9 months after reaching age 21, so long as he or she does not accept benefits after turning 21. For instance, if the proposed disclaimant is the beneficiary of a custodial account that terminates at age 18, the disclaimant can accept the custodial account's assets after reaching age 18 and still disclaim, so long as he or she accepts no benefits, such as dividends on stock, after reaching age 21. Treas Regs §§ 25.2518-2(d)(3) and 25.2518-2(d)(4) example 11.

But examples involving adults over 21 also allow some degree of acceptance. For instance, in Priv. Ltr. Rule 199932042 (May 19, 1999) husband and wife had a joint brokerage account. After his wife's death, husband deposited income from the joint account into his bank account (which had been joint, but became his sole account after his wife's death). He also authorized the brokerage to transfer the investment securities in the joint brokerage account into a new brokerage account opened in his sole name. Despite these acts, the IRS allowed husband to make a qualified disclaimer of his wife's interest in the brokerage account. Critical to this result were husband's acts shortly after those described above. On the same day he became personal representative, he opened a new brokerage account in the name of the wife's estate and

transferred one half of each security in the original (joint) brokerage account into it. He also deposited into an estate bank account one half of the joint brokerage account earnings he had previously deposited into his bank account.

The quick damage control helped. The IRS concluded that husband's acts in depositing the brokerage income and transferring the brokerage assets into accounts in his name did not constitute acceptance, given that husband never did anything further with either the securities or the funds he deposited into the bank account.

Finally, some things that look very much like taking possession or accepting benefits of property may not prevent a disclaimer. A disclaimant may continue to live in a home owned with the decedent as joint tenants or tenants by the entirety, receive an instrument of title to property, or become vested in title under ORS 114.215, and still disclaim the property. Treas Reg § 25.2518-2(d)(1), Priv. Ltr. Rule 8124118 (March 20, 1981). Likewise, acting as a fiduciary with respect to property does not necessarily cause a loss of the ability to disclaim that property. Treas Reg § 25.2518-2(d)(2). Note that a fiduciary who is also a disclaiming beneficiary may have discretionary powers which should also be disclaimed if those powers are not limited by an ascertainable standard. Treas Regs '§§ 25.2518-2(e)(1) and 25.2518-2(e)(5) examples 11 and 12.

4. The disclaimant cannot accept consideration for making a disclaimer. Can this rule prevent elaborate, prearranged plans of disclaimer to achieve desired results? Perhaps not.

There are numerous instances of successful prearranged disclaimer plans by heirs and devisees which cause the disclaimed property to pass to a surviving spouse and qualify for the marital deduction. *See* for instance, *Estate of Lassiter v. Commissioner*, TC Memo 2000-324, and Priv. Ltr. Rule 9509003 (Nov 3,1994), in which the IRS found that "although the five disclaimants have acted in concert in making the disclaimers in order to reduce the estate tax liability of the Decedent's estate, such action does not constitute the acceptance of any consideration in return for the making of a disclaimer within the meaning of [Treas Reg] § 25.2518-2(d)(1)."

In *Monroe v. Commissioner*, 124 F3d 699 (5th Cir 1997), the Fifth Circuit approved disclaimers by 29 devisees of Louise Monroe, some of whom were unrelated to her, made at the request of her husband's nephew. The disclaimers caused the disclaimed property to pass to the decedent's husband free of estate tax. Shortly thereafter, the husband made generous gifts to each of the disclaimants, in many cases equal to the amount disclaimed.

The Tax Court had found that the disclaimers were not qualified because they were the result of an implied promise by the husband to make gifts to the devisees if they disclaimed. However, the Court of Appeals for the Fifth Circuit reversed, stating that the very purpose of disclaimers is "to facilitate post-mortem estate tax planning and to increase family wealth on the 'expectation' that there will thus remain more wealth to pass on to the disclaimants in the future."

5. The testator's intent is the "pole star" for interpreting a will. Does that mean that a disclaimer which is contrary to the testator's apparent intent must be rejected? No.

The essence of a disclaimer is that it alters the estate plan, sometimes radically so. For instance, in *Palmer v. White*, 100 Or App 36 (1989) the decedent created a trust designed to delay her daughter from receiving her inheritance for 10 years. The daughter disclaimed, which caused the mother's estate to pass immediately to the daughter through intestacy, completely defeating the mother's plan. Note that this was a nonqualified disclaimer for tax purposes.

See also Estate of Lassiter v. Commissioner, TC Memo 2000-324, in which the decedent's estate plan, written before the unlimited marital deduction, created a trust that failed to qualify for the marital deduction. The surviving spouse and the descendants, through an elaborate disclaimer plan, essentially rewrote the trust, so it could qualify for the marital deduction.

Conclusion: As can be seen from the examples above, there are interesting twists in the disclaimer laws. Estate planners should be aware of the possibility that even if the facts do not fit the classic example for a disclaimer, a disclaimer may still be possible.

If you have questions, please contact any member of The Estate and Business Planning Practice Group:

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