

# Altshuler and Spiro

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## DISCLAIMER TRUST

### I. Basics of Disclaimer Trust

- A. Assets are held in a trust which, at the death of the first spouse to die the Surviving Spouse can revoke and amend. See Probate Code § 267(b)(3)
- B. Trust needs to state that if within nine (9) months [Treasury Regulation 25.2518-2(c)(5) & Probate Code § 279] of the first spouse to die's death, the Surviving Spouse disclaims all or any fraction of the assets or of selected assets, such property will be held under a Bypass/Exemption/Credit-Shelter Trust. See Probate Code § 282.
  - i. The gift tax rules will apply as if the disclaimed interest had never been transferred to the person making the disclaimer.
    - a. The disclaimed property will not be treated as part of the estate of the person making the disclaimer for estate tax purposes (Treasury Regulation 20.2046-1) or for generation skipping transfer tax purposes. (Internal Revenue Code § 2654(c)).
  - ii. Where Surviving Spouse intended to disclaim into a Bypass Trust but never did so, no disclaimer was made. The Court indicated that a key element of a valid disclaimer is the identification of assets being disclaimed. Estate of Chamberlin TC Memo 1991-181, Aff'd 87AFTR2d ¶ 2001-987 (9<sup>th</sup> Circuit, 2001).
  - iii. In Private Letter Ruling 8412078, the Surviving Spouse was allowed to disclaim a fraction of an outright bequest which then fell into a Bypass Trust.
  - iv. The written Disclaimer must have been delivered to the Trustee. Treasury Regulation 25.2518-2(b)(2).
  - v. For assets in a revocable trust which pass to a trust that the Surviving spouse can revoke or amend, the nine (9) months begin running at the first spouse to die's death. Treasury Regulation 25.2518-2(c)(5). Examples (1)-(4) and (6)

- vi. In addition to a fractional disclaimer, a pecuniary (or dollar amount) disclaimer is allowed. Treasury Regulation 28.2518-3(c).
- vii. A formula disclaimer based on finally determined estate tax values of the disclaimed assets does not violate public policy. The Proctor case, where gift was to be returned if it turned out that gift tax was payable, was distinguished. Christiansen, 130 TC No. 1.

## II. Goal of the Disclaimer Trust

- A. To defer the decision on whether or not to create and fund the trust that protects the amount that the first spouse to die can pass on without estate taxes until the first spouse to die's death.
- B. To allow the Surviving Spouse, at the first spouse to die's death, to look at the size of the estate, the size of the Survivor's own exemption equivalent and the Survivor's own life expectancy in determining:
  - i. Whether or not to disclaim
  - ii. Whether or not to protect the first spouse to die's exemption
  - iii. Whether or not to restrict the Surviving Spouse
    - a. Irrevocable Trust
    - b. Limitations on what the Surviving Spouse can do
    - c. Duties to the remainder beneficiaries
    - d. 1041 annual Income Tax return requirement
- C. To take advantage of the special rule only available to Surviving Spouses, which allows the Surviving Spouse (if desired) the right to benefit from the disclaimed property: income plus right to invade principal under an ascertainable standard. Internal Revenue Code § 2518(b)(4) and Treasury Regulation 25.2518-2(a)(5).
- D. A power of attorney specifically authorizing an attorney-in-fact to disclaim on behalf of the Surviving Spouse may be executed. See Probate Code § 4264.
  - i. This covers the situation in which the Surviving Spouse is incapacitated at the death of the first spouse to die.

## III. Problems of the Disclaimer Trust

- A. Surviving Spouse fails to act within the nine (9) months and inadvertently loses the ability to protect the first spouse to die's exemption equivalent.
- B. Surviving Spouse cannot be given even a limited power of appointment over the Trust which receives the Disclaimed assets. Reg 25.2518-2(e)(5) Example 5

- C. Surviving Spouse loses the ability to disclaim if he or she accepts benefits of the property during the nine (9) month period and before making the Disclaimer.
- i. Examples of acceptance of benefits include acceptance by Surviving Spouse of dividends, interest or rents from property to be disclaimed. See Private Letter Ruling 8817061. But Surviving Spouse's residing in residence prior to disclaimer was not considered to be an acceptance of benefits. Private Letter Ruling 9135044 and Treasury Regulation 25.2518-2(d)(l)
  - ii. Surviving Spouse's paying expenses of residence prior to disclaimer was not considered to be an acceptance of benefits. Private Letter Ruling 9135043
  - iii. Sale of an asset within the trust prior to the disclaimer was not considered an acceptance. TAM 9509003.
    - a. But removal of the asset from the Trust and transfer of it out to the Surviving Spouse would be an acceptance by the Spouse.
  - iv. The Surviving Spouse by acting as Trustee is not deemed to have accepted benefits unless the Trustee has the power to direct payment of the disclaimed interests. Treasury Regulation 25.2518-2(d)(2).
    - a. If Surviving Spouse has testamentary or intervivos special power of appointment over Bypass Trust, Disclaimer will not be qualified. Treasury Regulation 25.2518.2(e) Example 5
    - b. If Surviving Spouse as Trustee can invade Bypass Trust for his or her health, education, support and maintenance, Disclaimer will be qualified. Treasury Regulation 25.2518-2(e) Example 6.
    - c. If Surviving Spouse has 5 & 5 power over Bypass Trust, Disclaimer will be qualified. Treasury Regulation 25.2518-2(e) Example 7.