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**Dennis M. Sandoval,**  
A PROFESSIONAL LAW  
CORPORATION

*Protecting and Preserving  
Wealth for Future  
Generations*

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*Mr. Sandoval is the only  
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# California and Federal Tax Planning and Representation Newsletter

## *Disclaimer Proves Fatal to Estate Plan*

Mr. Katz executed a will in 1991 that called for the creation of a “pecuniary credit shelter trust” equal to the amount of the “aggregate federal estate tax exemption equivalent.” The will language further provided that the credit shelter trust “shall not be reduced on account of any disclaimer by my wife.” Finally, another provision in the will stated that “notwithstanding any otherwise conflicting provision in this will, if my wife disclaims any interest in any portion of the property otherwise passing outright to her under this Article of my will, such portion shall be added to the [credit shelter] trust.” The purpose of the credit shelter trust created under Mr. Katz’s will was to place an amount equal to the amount that can pass free of estate tax into trust so that it would eventually pass to his children without being subject to estate taxes in his wife’s estate.

The effect of a qualified disclaimer is to treat the disposition of the asset disclaimed as if the disclaimant had predeceased, thereby causing the assets to be distributed to the contingent beneficiary under the will, trust, retirement plan, life insurance or other document controlling the disposition of the asset. Where this is no controlling document, the asset would be distributed to the next person of priority under the intestacy laws of the state. Internal Revenue Code section 2518 provides that a qualified must” (1) identify the property being disclaimed, (2) be in writing, (3) be signed by the disclaimant, (4) be an irrevocable and unqualified refusal to accept the interest in the property, (5) be made within nine months after date of death of the owner of the property, (6) be made prior to the disclaimant’s acceptance of the disclaimed interest or any of its benefits, and (7) the disclaimed interest must pass without any direction on the part of the disclaimant.

Upon Mr. Katz’s death in 1998, the amount that could be passed free of estate tax was \$625,000. Apparently Mrs. Katz felt he had no need to access any of the funds being transferred to the credit shelter trust under her husband’s will, so she disclaimed her interest in the credit shelter trust. This means that the assets allocated to the credit shelter trust would pass immediately to Mr. Katz’s children under the terms of the credit shelter trust.

In addition to disclaiming her interest in the credit shelter trust, Mrs. Katz also disclaimed her interest in a designated number of shares of five different securities owned by her husband. At trial, her lawyer explained that Mrs. Katz's disclaimer of these securities was for the purpose of directing what assets she was disclaiming in association with the funding of the credit shelter trust.

The IRS argued that Mrs. Katz disclaimed both her interest in the \$625,000 allocated to the credit shelter trust as well as her interest in the five securities – therefore an estate tax was due of the value of the securities disclaimed since the value of all assets disclaimed was in excess of the amount that could be passed free of estate tax. The estate argued that Mrs. Katz only intended to disclaim \$625,000 worth of assets.

The Tax Court in *Estate of David Katz v. Commissioner*, T.C. Memo 2004-166, held that the language of the will was clear – the credit shelter trust was to be funded with \$625,000 and any disclaimer by Mrs. Katz was not to reduce this amount, instead any amount disclaimed was to be added to the credit shelter trust. Therefore, the Tax Court held for the IRS.

In this case, the executor of Mr. Katz's will could have allocated the designated securities to the credit shelter trust without an additional disclaimer by Mrs. Katz and the estate tax imposed by the IRS could have been avoided. This is a perfect example of why it is so critically important to hire a specialist in estate planning to assist your clients with their estate and trust administrations. Here, a simple mistake by Mrs. Katz cost her children hundreds of thousands of dollars in estate taxes that would have ultimately been avoided but for the errant disclaimer.

## ***Can We Be of Assistance to You?***

Dennis M. Sandoval, A Professional Law Corporation, specializes in estate planning (including probate administration and trust / will contests), asset protection planning, elder law (including qualifying for Medi-Cal coverage, conservatorships, and creation of Special Needs Trusts for disabled beneficiaries) and tax controversy work (including federal and state tax audits, appeals and litigation). All of your referrals will be handled promptly and professionally.

***Mr. Sandoval is available to speak to your group or organization. Call (951) 787-7711 to schedule him to speak on any topic relating to estate planning, elder law, asset protection or taxes.***

### Upcoming Seminars / Classes for Professionals

|   |                   |             |  |
|---|-------------------|-------------|--|
| The Mechanics of Drafting First Party and Third Party Special Needs Trusts in California  | 6/18/2005         | 9 am - noon | UNEX<br>3 hrs. Attorney CLE  |
| Basics of Conservatorships in California  | 5/26/2005         | Noon - 1 pm | Kaiser Hospital<br>Riverside, California                                       |
| Maintaining and Maximizing Government Benefits for Special Needs Beneficiaries: The Basics of Administering a Special Needs Trust | 6/18/2005         | 1 pm - 4 pm | UNEX<br>3 hrs. Attorney CLE  |
| Retirement Plan Distribution Rules: A Magical Mystery Tour; Federal Estate Tax Repeal Update and recent Tax Developments          | 9/29 - 10/2/2005  | TBD         | National Academy of Elder Law Attorneys<br>Sheraton New Orleans<br>New Orleans |
| Topics to be Determined   | 10/6 - 10/10/2005 | TBD         | American Academy of Estate Planning Attorneys<br>Catamaran Hotel<br>San Diego  |