I.R.C. Section 2518 and the Law of Disclaimers An Update

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Abstract

The Tax Reform Act of 1976 introduced Code section 2518, which attempted to create definite standards for a disclaimer to be valid for federal tax purposes.

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The Tax Reform Act of 19761 introduced Code section 2518,2 which attempted to create definite standards for a disclaimer to be valid for federal tax purposes. In 1978, Congress amended section 2518 to liberalize one of the many requirements which must be satisfied for a disclaimer to be qualified,3 and in 1981, Congress again amended section 2518 to remove the requirement that the disclaimer be valid under state law.4 This article will endeavor to discuss the post-1978 evolution of section 2518 beginning with a critical analysis of the Internal Revenue Service’s (“IRS”) interpretation of that Section as incorporated in the proposed regulations promulgated under section 2518. In addition, the most significant of the numerous private letter rulings issued by the IRS interpreting section 2518 will be discussed including a review of the effect of the 1981 amendment. In conclusion, suggestions for clarifying aspects of the law of disclaimers will be put forth with the hope that the stated purpose of the law will be achieved.5

I. Disclaimers as an Estate Planning Tool
A disclaimer is the refusal to accept the ownership of property or

The major importance of disclaimers is the flexibility they provide for estate planning. Disclaimers can be used to correct errors in an estate plan after it would ordinarily be too late (for example, after the testator's death), adjust the estate plan to account for changed circumstances, avoid the creditors of a beneficiary and allow post mortem estate planning. The following example will demonstrate the use of disclaimers as a method of achieving tax savings; assume each of the following disclaimers are qualified.

A disclaimer may be used to save gift tax. X devises Whiteacre to B. B has no need for Whiteacre and would prefer it to pass to his son C. If B accepts Whiteacre and transfers it to C for less than adequate and full consideration, B has made a taxable gift to C. However, if B disclaims Whiteacre it passes to C and no gift tax will be imposed on B. There is no gift from B to C because B will be treated as never having owned Whiteacre.

A disclaimer may be used to save estate tax. X devises Whiteacre to B who is terminally ill. B would prefer to give Whiteacre to his son C in a manner that will not have any tax ramifications. If B accepts Whiteacre and then dies, Whiteacre will be included in B's gross estate. If B disclaims Whiteacre, it will pass to C and there will be no

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7. I.R.C. § 2518(a) (1976); WAYS AND MEANS COMM. REPORT, supra note 6, at 65.


9. I.R.C. § 2518(a); WAYS AND MEANS COMM. REPORT, supra note 6, at 65.

10. “(a) General Rule-For purposes of this subtitle, if a person makes a qualified disclaimer with respect to any interest in property, this subtitle shall apply with respect to such interest as if the interest had never been transferred by such person.” I.R.C. § 2518(a); WAYS AND MEANS COMM. REPORT, supra note 6, at 65.

11. I.R.C. § 2518(a); WAYS AND MEANS COMM. REPORT, supra note 6, at 65. For purposes of estate tax, I.R.C. § 2046 (1976) says 2518 applies.

inclusion in B's gross estate because B will again be treated as never having owned Whiteacre.\textsuperscript{13}

A disclaimer may be used to prevent an overfunding or an underfunding of a marital bequest for purposes of achieving the optimal marital deduction.\textsuperscript{14} If an amount greater than the optimal marital deduction\textsuperscript{15} passes to the surviving spouse, the excess will be taxed in the estate of the surviving spouse.\textsuperscript{16} If the surviving spouse disclaims the excess\textsuperscript{17} over the optimal marital deduction, the disclaimed property will not be included in the surviving spouse's gross estate.\textsuperscript{18} If an amount less than the optimal marital deduction is provided for the surviving spouse, a disclaimer by another can increase the property passing to the spouse and allow use of the full marital deduction.\textsuperscript{19} In much the same way, a disclaimer by one heir can be used to increase an estate's charitable deduction.\textsuperscript{20} Thus, a disclaimer can be an important post mortem estate planning tool.

A disclaimer will prevent the imposition of a generation skipping

\textsuperscript{13} Brown v. Rautzahn, 63 F.2d 914 (6th Cir. 1933), \textit{cert. denied}, 290 U.S. 641 (1933); I.R.C. § 2518(a); \textit{Ways and Means Comm. Report}, \textit{supra} note 6, at 65.

\textsuperscript{14} I.R.C. §§ 2518(a), 2056 (1954) (amended by 1981 ERTA); \textit{Ways and Means Comm. Report}, \textit{supra} note 6, at 65. In the following discussion it is assumed that achieving the optimal marital deduction is desired. The optimal marital deduction is not necessarily the maximum deduction allowable, for example, where a decedent's adjusted gross estate is less than $425,000. For the law prior to § 2518 see generally I.R.C. § 2056(d) (1954) (amended by 1981 ERTA) and Treas. Reg. § 20.2056(d)-1 (1958).

\textsuperscript{15} ERTA 1981 amended § 2056 to provide for an unlimited marital deduction.

\textsuperscript{16} It will be included in the estate of the surviving spouse as an I.R.C. § 2033 inclusion because the spouse owned the property at death. If the marital bequest were limited to the optimal amount, the excess would escape estate tax entirely.

\textsuperscript{17} The issue of partial disclaimers will be discussed later in this article as part of an analysis of the Tax Reform Act of 1976. \textit{See} text accompanying notes 58-104.

\textsuperscript{18} I.R.C. § 2518(a); \textit{Ways and Means Comm. Report}, \textit{supra} note 6, at 65. This possibility of a surviving spouse disclaiming an interest in a marital trust and taking a portion of the disclaimed interest under a non-marital trust will be discussed later in this article. For purposes of this example assume the property passes to the issue of the surviving spouse.

\textsuperscript{19} I.R.C. § 2518(a).

\textsuperscript{20} \textit{Id.} For an excellent discussion and example of disclaimers with respect to charitable deductions, see Newman & Kalter, \textit{The Need For Disclaimer Legislation—An Analysis of The Background and Current Law}, 28 Tax. L. 571, 577 (1975).
tax.\textsuperscript{21} X devises to his son B a life estate in Whiteacre with remainder to B's son C. Assuming that the value of the property at B's death is greater than $250,000, a generation skipping tax will be imposed at that time.\textsuperscript{22} If B disclaims his life estate, no generation skipping tax will be imposed because B will be treated as never having owned a life estate in Whiteacre.\textsuperscript{28}

A disclaimer may shift the income tax consequences of a trust.\textsuperscript{24} X devises to B, a wealthy individual with a large income, the power to designate who shall be the recipient of an income interest in the trust res. The power excludes designation of the grantor's spouse.\textsuperscript{25} If B disclaims his power he will not be taxed on the income.\textsuperscript{26} Assuming B disclaims and the income is payable to B's son C, an individual with very little income, income tax will be saved as a result of the graduated tax rates.

II. Legislative History

The confusion and uncertainty surrounding the common law of disclaimers has generated considerable discussion of ways to clarify the law.\textsuperscript{27} Many commentators and Congress suggested that the law of disclaimers be federalized and specific disclaimer requirements be imposed.\textsuperscript{28} The widespread dissatisfaction with the pre-1977 state of the

\begin{itemize}
\item[21.] I.R.C. § 2518(a); Ways and Means Comm. Report, supra note 6, at 65. See § 2614(c) (1976); S. Rep. No. 94-1236, 94th Cong., 2d Sess. 607 (1976).
\item[22.] See generally I.R.C. §§ 2601-2614.
\item[23.] I.R.C. § 2518(a); Ways and Means Comm. Report, supra note 6, at 35. I.R.C. § 2614(c) refers to § 2518 for the effect of a qualified disclaimer.
\item[24.] I.R.C. § 2518(a); Ways and Means Comm. Report, supra note 6, at 65.
\item[26.] I.R.C. § 2518(c)(2) (1976) treats a power with respect to property as an interest in such property. I.R.C. § 2518(a) will treat B as never having the power if he disclaims it. In Gallagher v. Smith, 223 F.2d 218 (10th Cir. 1954), rev'd 119 F. Supp. 360 (D.C. Pa. 1953) a widow disclaimed a portion of her interest in a trust. The court held she was only taxable on the income of the portion she retained.
law brought about the enactment of section 2518. A disclaimer of an interest in property created after 1976 will be effective for federal tax purposes only if it is a "qualified" disclaimer. Section 2518 delineates the requirements a disclaimer must satisfy to be considered qualified. Section 2518, as initially adopted, required that the disclaimed property must pass to a person other than the disclaimant and that the disclaimer be valid under local law.

In 1978, Congress recognized that the requirement that the disclaimed property pass to someone other than the disclaimant would create an undesirable situation where the disclaimant was a surviving spouse and the property passed to a non-marital or marital trust as a result of the disclaimer. Congress therefore amended section 2518 to make it possible for property to pass to a decedent's spouse as a result of a disclaimer even if the surviving spouse was the disclaimant.

In 1981, Congress, recognizing the local law still played an important role in determining whether a disclaimer was qualified, amended section 2518 in an attempt to make it independent of state law. Congress felt that state law was not an adequate basis upon which to measure the effectiveness of a disclaimer because local disclaimer laws were not uniform. This caused identical refusals to accept property to be treated differently for Federal estate and gift tax purposes.

III. Proposed Regulations and Private Rulings

The IRS published proposed regulations for section 2518 on July 6, at 66.

29. Newman & Kalter, Disclaimers of Future Interests, 49 NOTRE DAME LAW. 827, 837 (1974); Committee on Estate and Gift Taxes, Tax Section Recommendations No. 1974-2, 27 TAX LAW. 818 (1974); (1974). The dissatisfaction stemmed from the fact that prior to § 2518, disclaimers were handled under many different code sections and in many different regulations and were dependent upon local law. See Treas. Regs. §§ 25.2511-1(c) (1972), 20.2041-3(d)(6) (1958), 20.2056(d)-1(a)(1958).


At this time, the date final regulations will be issued and the form those regulations will take is entirely speculative. In addition to the proposed regulations, the IRS has attempted to interpret the law as it relates to specific taxpayer questions by issuing numerous private letter rulings. This portion of the article will analyze several important provisions of the proposed regulations and several significant private letter rulings with respect to section 2518.

**A. Reliance Upon State Law**

The intent of Congress in enacting section 2518 was to create a federal standard for disclaimers, thus ending reliance upon state law in determining the federal tax consequences of a disclaimer. Therefore, most practitioners hoped that section 2518 would provide a uniform set of rules for determining the federal tax consequences of a disclaimer. However, prior to the amendment of section 2518 contained in the Economic Recovery Tax Act of 1981, section 2518(b)(4)(A) and (B) required that the disclaimed interest must pass to a person other than the disclaimant or the spouse of the decedent (the decedent being the testamentary transferor). The pre-1982 absence of a federal rule or regulation determining who will receive the disclaimed property prevented section 2518 from acting as a safe harbor because the courts were forced to look to local law in making the determination as to whether a disclaimer was disqualified. Consequently, if local law did not recognize the disclaimer, section 2518(b)(4) could not be satisfied. Therefore,

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33. On November 23, 1981, a final version of the regulations were delivered to the Commissioner for final approval.
35. "If the requirements of the provision are satisfied, a refusal to accept property is to be given applicable effect for federal, estate and gift tax purposes even if the local law does not technically characterize the refusal as a 'disclaimer'. . . ." WAYS AND MEANS COMM. REPORT, supra note 6, at 67. See also, Frimmer, supra note 5.
37. There are no federal rules or regulations which deal with who the recipient of the property will be after the property has been disclaimed. Therefore, local law must be consulted.
prior to 1982, the only way to be certain a disclaimer would be qualified is to satisfy both state and federal requirements.

The proposed regulations specifically provide that a disclaimer, to be qualified, must be valid under state law. Moreover, in a number of private letter rulings, the IRS has ruled that a disclaimer not valid under state law cannot be a qualified disclaimer under section 2518. Recognizing that the purpose and intent of section 2518—to create a uniform federal standard for disclaimers—was being thwarted by the IRS, Congress, as part of the Economic Recovery Tax Act of 1981, added a new section 2518(c)(3) to the Code. Section 2518(c)(3) provides that:

(3) Certain Transfers Treated as Disclaimers. For purposes of Subsection (a), a written transfer of the transferor's entire interest in the property—
   (A) which meets requirements similar to the requirements of paragraphs (2) and (3) of Subsection (b), and
   (B) which is to a person or persons who would have received the property had the transferor made a qualified disclaimer (with in the meaning of Subsection (b)), shall be treated as a qualified disclaimer.

Thus, notwithstanding the fact that a disclaimer is not valid under local law, the recipient of property could, if the requirements of section 2518(c)(3) are satisfied, transfer property to another free of transfer tax.

The application of section 2518(c)(3) in many situations is unclear. Section 2518(c)(3) makes no attempt to define requirements which are "similar to" those contained in sections 2518(b)(2) and (3).

38. Prop. Reg. § 25.2518-1(c)(1), 45 Fed. Reg. 48,922 (1980) (to be codified at 26 C.F.R. § 25.2518). The regulation provides: "If a disclaimer is not effective under applicable local law to divest ownership of the disclaimed property in the disclaimant and to vest it in another, the disclaimer is not a qualified disclaimer under Section 2518."


40. ERTA 1981 § 426(a) (which added § 2518(c)(3)).

Consequently, a disclaimant will have no reliable method of determining whether he has complied with the requirements of subsection (c)(3). For example, is a disclaimer ten months after the date on which the interest was created qualified because a ten-month requirement is “similar to” the nine-month requirement? Is a disclaimer which occurs one day after a disclaimant has accepted the benefits of property qualified because the short period for which the benefits were accepted is “similar to” the requirement that none of the benefits be accepted? Conversely, is the “similar to” requirement to be interpreted more stringently than the normal requirements of section 2518(b)?

Another significant defect in section 2518(c)(3) is the requirement for a written transfer of the “entire interest” in property. 42 Although unclear, that requirement seems to prohibit the disclaimer of an undivided portion of an interest. This can be illustrated by the following example. X dies intestate with Blackacre, his only asset, passing to B. State law prohibits the disclaimer of an intestate share. B disclaims an undivided ½ interest in Blackacre. If state law recognized the disclaimer of an intestate share, B’s disclaimer would be qualified insofar as it would be the disclaimer of an undivided portion of an interest. 43 It appears doubtful that Congress intended to limit the interest which may be disclaimed to the “entire interest” in property in situations where the disclaimer is not valid under state law. Therefore, section 2518(c)(3) should be interpreted in such a manner as to allow the disclaimer of an undivided portion of an interest in property. 44

42. Id.

43. See Prop. Reg. § 25.2518-3(b) and the text accompanying notes 54-58 infra.

44. Due to the recent passage of § 2518 (c)(3), there is no indication at this time as to how the IRS will interpret the “entire interest” requirement.

The legislative history of § 2518(c)(3) provides:

Under the Committee Bill, for purposes of the estate and gift tax, a refusal to accept any property interest that is not effective to pass title under local law will be considered to pass the property without any direction on the part of the disclaimant if the refusal otherwise satisfies the Federal requirements and the disclaimant timely transfers the property interest to the person who would have received the property had the refusal been an effective disclaimer under state law. Although the State disclaimer rules will be used to determine the transferee, the refusal need not be a valid disclaimer under local law.

The person to whom the transfer must be made is the person who would have received the property had the transferor made a qualified disclaimer. Presumably, that language was intended to require a transfer by the disclaimant to the person to whom the property would have passed had the disclaimer been valid under state law.

B. Writing Requirement

One of the more basic and straightforward requirements of section 2518 is that the disclaimer be in writing. Section 2518, however, does not specify whether the written disclaimer must be signed, or, if signature is required, who must sign. The proposed regulations specifically provide that the disclaimer must be signed, a requirement not expressly included in section 2518, and recognize that the legal representative of the disclaimant may sign. Thus, it appears that one of the questions not resolved by the passage of section 2518—whether a legal representative may disclaim on behalf of an individual who is incapable of disclaiming due to a legal incapacity of one form or another—is answered affirmatively by the proposed regulations.

The IRS has ruled that the personal representative of a deceased beneficiary may disclaim property passing to a deceased beneficiary's estate. The ruling did not indicate whether the result would have been different if the disclaimer had been made by a guardian or other form of legal representative. Presumably the precise title attached to the fiduciary will be considered irrelevant. The ruling did, however, emphasize the fact that the personal representative has the power to disclaim on behalf of the estate of the deceased beneficiary under state law.

The result where a legal representative does not have the power to disclaim on behalf of a deceased beneficiary under state law is less clear. Presumably, the 1981 amendment adding section 2518(c)(3)
will allow a legal representative to disclaim on behalf of the person he represents regardless of the validity of the disclaimer under state law.\textsuperscript{61}

C. Jointly Owned Property

The law of disclaimers as it applies to jointly held property, including tenancy by the entirety, has always been unclear. In a factual situation arising prior to the enactment of section 2518, the IRS ruled that jointly held property could not be disclaimed if the rights of each joint tenant vested upon the creation of the tenancy and no greater right accrues by the death of either.\textsuperscript{58}

The IRS appears to have changed its position with respect to the disclaimer of jointly held property. The proposed regulations sanction the disclaimer of jointly owned property if, in addition to the requirements contained in section 2518(b), the following requirements are met: (i) the disclaimer must be made with respect to the \textit{entire interest} in property which is the subject of the tenancy, and (ii) the disclaimer must be made within nine months of the creation of the tenancy.\textsuperscript{59}

The requirement that the disclaimer must be made with respect to the “entire interest” in property seems to prohibit the disclaimer of the accretive interest created by the death of a joint tenant. For example, where A and B own real property as joint tenants with the right of survivorship and A dies within 9 months of the creation of the tenancy, if B must disclaim his entire interest in the real property for his disclaimer to be qualified, B must not have an interest in the property after the disclaimer. It is not clear whether B will be able to disclaim his \textit{entire interest} in the property which he holds immediately after A’s death because the IRS may take the position that B has already accepted the benefits of owning an undivided interest that property, i.e. B has accepted the benefits of being a joint tenant prior to the death of A upon the creation of the tenancy. A more logical interpretation of this requirement would be to treat B as never having accepted the benefits executor to disclaim on behalf of the decedent’s estate.

\textsuperscript{51} See the discussion regarding the application of state law in text accompanying notes 35-46.

\textsuperscript{52} I.R.S. Letter Ruling 7911005, Nov. 29, 1978.

of Blackacre. The Regulations should specifically provide that one’s status as a joint owner of property will not be sufficient to constitute the acceptance of the benefits of ownership. Another consequence of the “entire interest” requirement is that it can be interpreted to prohibit the disclaimer of an undivided portion of the accretive interest created upon the death of a joint tenant.

The requirement that the disclaimer be made within nine months of the creation of the tenancy effectively prohibits the disclaimer of jointly held property in almost all situations. This can be illustrated by the following example. On January 1, 1982, A and B acquire a parcel of real property as joint tenants with the right of survivorship. On January 1, 1983, A dies. B, wishing to disclaim the accretive interest in the real property passing to him as a result of A’s death, files a disclaimer with the executor of A’s estate on January 2, 1983. B’s disclaimer is not qualified insofar as it was not made within nine months of the creation of the tenancy (because the tenancy was created on January 1, 1982).

The “entire interest” and “nine month” requirements for a disclaimer of jointly held property to be qualified are an unwarranted extension of the statute. The rules of section 2518(b) should apply to jointly held property just as they apply to all other forms of property. The disclaimer of the accretive interest in property should be considered qualified, and a joint tenant should not be considered as accepting the benefits of jointly owned property by virtue of being a joint tenant.

Since the creation of a revocable joint bank account is not a taxable transfer,54 the special rules for the disclaimer of jointly held property discussed above do not apply to revocable joint bank accounts.55 Moreover, the nine month disclaimer period does not begin to run until the death of the donor.56

One interesting question with respect to revocable joint bank accounts is whether the donor or transferor of the property can make a qualified disclaimer of his survivorship interest in the property on the death of the co-tenant. For example, if H using his individual funds creates a joint bank account with his wife, W, will H’s disclaimer of

the bank account upon the death of W be qualified? The IRS has ruled that it would not because "the estate and gift tax laws apply to the disclaimed interest . . . as if the interest had never been transferred to such person." Thus, the IRS reasoned that the qualified disclaimer rules are not available to the donor or transferor of the property, but are only available to the donee or transferee of the property. The ruling is clearly correct inasmuch as it requires a "transfer" of property before the disclaimer provisions can be activated. Since W died prior the the occurrence of a "transfer" of property, the "transfer" requirement has not been satisfied.

D. Disclaimer of Less Than Entire Interest

Section 2518 allows the disclaimer with respect to "an undivided portion of an interest." The meaning of the phrase "an undivided portion of an interest" is unclear. Consequently, a devisee is faced with the dilemma of whether the disclaimer of any of the following interests will be qualified: a fractional interest in property (an undivided one half interest), a portion of a pecuniary devise ($25,000 of a $50,000 devise), a portion of a specific devise (five acres of a ten acre tract) or a carved out interest (a life estate or a remainder from a fee).

Prior to the publication of the proposed regulations, many commentators believed that fractional and pecuniary interests in property could be disclaimed whereas a carved out interest could not. The proposed regulations seem to allow disclaimers of fractional interests as well as some forms of pecuniary and carved out interests. The Regulations attempt to clarify this uncertainty by formulating various highly complex and totally arbitrary rules. The paragraphs which follow attempt to explain and analyze these rules.

59. See Frimmer, supra note 5, at 322 (1978) and Note, supra note 5, at 202.
60. See Frimmer, supra note 5, at 322 (1978) and Note, supra note 5, at 202.
Partial Interest Rule

The first rule with respect to the disclaimer of an undivided portion of an interest is called “disclaimer of a partial interest.” The rule reads as follows: “[i]f the requirements of this section are met, the disclaimer of an entire interest in property may be qualified disclaimer even if the disclaimer has another interest in the same property.” It is rather curious that the above quoted sentence uses the term “entire interest” and the section of the proposed regulations in which it appears is entitled “disclaimer of less than entire interest.” Moreover, the subsection of the proposed regulations in which that sentence appears is entitled “[d]isclaimer of a partial interest.” This seems to evidence the fact that the IRS has not adequately defined the terms “interest”, “entire interest”, and “partial interest.”

The specific requirements of this first rule of partial disclaimers, although never clearly articulated in the proposed regulation, appear to center around the divisibility or aggregation of interests in a single piece of property. That is, whether the various interests of a disclaimant in a single piece of property should be aggregated and treated as one, or should be treated as separate divisible elements of a single piece of property. If the interests are considered divisible, the disclaimant may disclaim one interest and retain the other; if the interests are aggregated (i.e. treated as one), the disclaimant may only disclaim an undivided portion of his interest as aggregated.

In order to apply the aggregation rules discussed above, criteria must be established to determine whether various interests in a single piece of property should be aggregated. The proposed regulations contain two such rules. The first rule is that all income interests beneficially owned by a person shall be treated as one interest in property, and all beneficial interests in corpus shall be treated as one interest.

63. Id. (emphasis added).
66. Id.
For example, if Blackacre is devised with an income interest to A for ten years, an income interest to B for the next ten years, an income interest to A for the ten years after that, and then an income interest to C for ten years, remainder to A, presumably, A will be considered as having only two, not three, interests in Blackacre. A's first interest is the right to receive the income from Blackacre in years one through ten and in years twenty-one through thirty; A's second interest is the remainder interest. By aggregating each of A's income interests, the proposed regulation would not allow A to disclaim one of his income interests while retaining the other. The proposed regulation would, however, allow A to disclaim his income interest and retain his corpus interest, or to retain his corpus interest and disclaim his income interest.

The second rule of aggregation is that if the separate interests of the disclaimant are considered as merged under state law, the disclaimant must disclaim the entire merged interest or an undivided portion of such merged interest. Thus, if Blackacre is devised to A for life, remainder to A, and under state law A is considered as owning Blackacre in fee, A's disclaimer of his life estate in Blackacre will be qualified only if the disclaimer of a life estate from a fee is considered the disclaimer of an undivided interest. If A's interest is not considered as merged under state law, A's income and corpus interests will be considered separate divisible interests in Blackacre and A could make a qualified disclaimer of either.

The application of the doctrine of merger in this context, when viewed in isolation, appears reasonable. However, remembering that the intent of section 2518 was the creation of a uniform federal stan-

67. This result seems to follow from the example in the regulations where securities are devised to A for life, then to B for life, remainder to A's estate. The regulations state that A could disclaim his income interest, his remainder interest or an undivided portion of either; however, the regulations specifically state that A could not disclaim a ten year income interest from his life estate. The IRS must therefore not consider the disclaimer of a ten year from a life interest a disclaimer of an undivided portion of an interest. Prop. Reg. § 25.2518-3(a)(1)(i). But see Prop. Reg. § 25.2518-3(d) example 4 where a disclaimer of 40% of an income interest was qualified.

68. Prop. Reg. § 25.2518-3(a)(1)(i), 3(d) example 8.

69. Id.

70. This issue is discussed further at text accompanying notes 95-97.

standard for disclaimers, reliance upon state law to determine whether a disclaimant possesses divisible interests in a single piece of property appears to be another digression thwarting the uniform application of the statute. This can be illustrated by the following example. A devises Blackacre to B with B having an income interest until he attains age 40, then to B or B's estate. If in state #1 B's interests in Blackacre are not merged, B's disclaimer or his income interest and/or his remainder interest will be qualified. In state #2, if B's interests in Blackacre are merged, B cannot disclaim solely his income interest (or his remainder interest) in Blackacre; however, B can disclaim a portion of Blackacre if his disclaimer satisfies the undivided portion rule.

Possibly the most distressing provision of the proposed regulation dealing with partial disclaimers is contained in the following sentence: "[m]oreover, if the property is divided in a manner that would permit the disclaimant to avoid the limitations of section 2518, the separate interests created by the grantor are treated as one indivisible interest." The meaning of that sentence is totally unclear. If this is an IRS attempt to include a catchall in the regulations so that any disclaimer which it deems objectionable will be caught and treated as a taxable transfer, that sentence will contravene the entire purpose of section 2518 and inhibit the use of a provision of the Code which Congress intended to make available to taxpayers. If that sentence is merely intended to deal with a specific fact situation contemplated by the IRS, the IRS should address that situation in more specific terms.

The regulations illustrate the application of this avoidance concept in one example. In that example, C devised 1/6 of his residuary estate to D with any disclaimed property to E, 1/6 of his residuary estate to D with any disclaimed property to F and 1/6 of his residuary estate to D with any disclaimed property to G. The regulation concludes that D's disclaimer of the 1/6 of the residuary estate which passes to E is not qualified because C divided the property in a manner that would permit

73. See the discussion in text accompanying notes 95-97.
75. Cf. the trust rule which is discussed in text accompanying notes 86-97, i.e. split transfer into separate trusts or make greater than one transfer so the disclaimant can disclaim part (avoid aggregation).
the disclaimant to avoid the limitations of section 2518. 76 It is not intuitively obvious why the IRS finds the facts of that example objectionable. If the remainder was devised in toto to D, D could clearly have disclaimed an undivided ½ interest in the property. 77 Moreover, D may have been able to disclaim 33 ⅓% of the value of the remainder. 78 In light of D’s ability to disclaim ½ of the property notwithstanding C’s perceived attempt to avoid the limitations of section 2518, the IRS’s only objection could be that C or D has directed the person to whom the property is passing. If the IRS’s objection to the disclaimer in the example discussed above is the disclaimant’s disposition of the disclaimed property, it is curious that this provision was not placed in the section of the proposed regulations dealing with the disclaimant’s direction of the property.

A more fundamental question is whether the actions taken by C and/or D constitute a transgression of the prohibition of directing the passage of the property. Section 2518(b)(4) clearly provides that the person making the disclaimer may not direct the passage of the disclaimed property. No mention is made of any prohibition of the actions of a person other than the disclaimant. Therefore, the actions of C, in directing who will receive the disclaimed property is not relevant to the qualifications of D’s disclaimer.

Has D directed the pasage of the property by virtue of his disclaiming a portion of a homogeneous property? Arguably, if the property is homogeneous, D has directed the property because he has been given, in effect, the right to choose the recipient of the property he partially disclaims among a group of three, E, F and G. Would the result be different if C devises his home (⅓ of his estate), his business (⅓ of his estate) and his other assets (⅓ of his estate) to D with a disclaimer of his home to E, with a disclaimer of his business to F, and with a disclaimer of his other assets to G? In this situation, D does not have any right to choose among E, F or G as to who will receive the disclaimed property. Thus, D’s disclaimer of any of the three specific devises should be qualified insofar as D’s disclaimer will have true eco-

76. See Prop. Reg. § 25.2518-3(d) example 14.
77. Prop. Reg. § 25.2518-3(b). It may be possible under the severable property rule or the pecuniary interest rule for D to have disclaimed 33 ⅓% of the property if it had been devised to him in total. See example 4 of Prop. Reg. § 25.2518-3(d).
78. Prop. Reg. § 25.2518-3(d); 25.2518-3(d).
nomic significance.  

**Severable Property Rule**

The second rule of partial disclaimers, the "severable property rule" is a logical application of the requirement that a disclaimer must involve an undivided interest in property. That rule allows a disclaimer to disclaim a severable interest in property if specific reference is made to specific items of property. Severable property is defined as "property which can be separated from other property to which it is joined and which after severance, maintains a complete and independent existence." The proposed regulation indicates that shares of corporate stock are severable property. Presumably, real estate will be considered severable so that the disclaimer of five acres of a ten acre tract will be qualified.

The IRS has had the opportunity to apply its definition of the term "severable property" in two recent private letter rulings. In Letter Ruling 8113061, the devisee of two-thirds of a residuary estate disclaimed his interest in the residuary estate to the extent that it exceeded a debt to the estate. The IRS, although never directly stating that the portion of the residuary estate disclaimed by the devisee was severable from that which he retained, discussed the severable property rule in the paragraph immediately before the paragraph in which it concluded the disclaimer was qualified. In Letter Ruling 8145036, the IRS ruled that the disclaimer of a portion of a child's intestate share would be qualified. The IRS's rationale again appeared to be the severable property rule. Since neither ruling made mention of the type or

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79. Cf. the trust income allocation rules contained in I.R.C. § 651(b) (1954); 622(b) (1954); Treas. Reg. § 1.652(b)-2(b) (1960); the partnership allocation rules contained in I.R.C. § 707(b)(2) (1954).
81. Id. See I.R.S. Letter Ruling 8113061, Dec. 31, 1980, where the IRS seems to have ruled that the remainder of an estate consists of severable property.
82. Prop. Reg. § 25.2518-3(d) example 1 contains other examples of severable property.
nature of the property owned by the estate, it appears that these rulings may support the proposition that a remainder interest is comprised of severable property, and that the IRS is interpreting the severable property rule liberally to allow the disclaimer of a specific percentage of a residuary estate.

**Trust Rule**

The third rule of partial disclaimers deals with the application of the first rule of partial disclaimers, the disclaimer of a partial interest to property held in trust. That is, all interests in trust income are treated as a single interest and all interests in trust corpus are treated as a different single interest. The proposed regulations illustrate this rule with the following example:

A disclaimer is not a qualified disclaimer under Section 2518 if the beneficiary disclaims income derived from specific properties transferred in trust while continuing to accept income derived from the remaining properties in the same trust. Similarly, since all interests in the corpus of a trust are treated as a single interest, in order to have a qualified disclaimer of an interest in corpus the disclaimant must disclaim all such interests, either totally or as an undivided portion.

The language of the above quoted example appears to create a distinction between a partial disclaimer of an income interest in trust property and a partial disclaimer of an interest in the corpus of a trust. This distinction arises as a result of the omission of the qualifying language that “the disclaimant must disclaim all such interests, either totally or as an undivided portion” from the portion of the example dealing with the partial disclaimer of an income interest.

The IRS's interpretation of the interrelation between the “severable property rule” and the “trust rule” creates another artificial distinction in determining whether a partial disclaimer is qualified. Although

86. See supra text accompanying notes 62-75.
88. Id.
89. Id.
the IRS seems to take the position that severable items of property lose their identity as severable property when placed in trust, there does not appear to be any justifiable reason for distinguishing between a situation where A makes a gift to B of a life interest in two paintings followed by B’s disclaimer of one life interest, and the situation where A creates a trust with the two paintings as the corpus giving B an income interest in the trust followed by B’s disclaimer of the income generated by one specific painting. In the first situation, B’s income interests in each painting will be considered severable property and therefore B’s disclaimer of his life estate in one of the paintings will be qualified. The language of the proposed regulation seems to consider the disclaimer in the second situation to be disqualified merely because the property has been placed in trust. The final regulations will hopefully clarify this situation.

If taxable transfers to the same trust are made at different times or by different transferors, a qualified disclaimer is permitted with respect to each transfer, because each transfer will be treated as though it were a transfer to a separate trust. Query: is it possible to avoid the partial disclaimer rules as they apply to trusts by transferring property to a trust in installments? For example, will the result in the first situation posed above be different if A transferred painting number 1 to the trust on January 1, 1982, and transferred panting number 2 to the trust on January 2, 1982. Would the result be different if painting number 2 were transferred on January 1, 1983?


94. See Prop. Reg. § 25.2518-3(a)(1)(i). Is this a situation where the IRS would attempt to invoke that provision of the proposed regulations? On its face, that provision appears applicable because the property has not been “divided”. The IRS may take the position that the proximity in time of the transfers require their aggregation notwithstanding the proposed regulation.
**Undivided Portion Rule**

The "undivided portion rule" of partial disclaimers seems to be the IRS's attempt to interpret the language of section 2518 which allows the disclaimer of an undivided portion of an interest. The proposed regulations define the term "undivided portion of an interest" as:

... a fraction or percentage of each and every substantial interest or right owned by the disclaimant in such property and must extend over the entire term of the disclaimant's interest in such property and in other property into which such property is converted. A disclaimer which disclaims some specific rights and retains other rights with respect to an interest in the property is not a qualified disclaimer of an undivided portion of the disclaimant's entire interest in property. Thus, for example a disclaimer is not a qualified disclaimer if the disclaimant disclaims the fee simple in Blackacre, but retains a life estate.

Thus, the proposed regulation seems to expressly sanction the disclaimer of an undivided one-half interest in a fee.

**Pecuniary Interest Rule**

The fourth rule of partial disclaimers, the "pecuniary interest rule," seems to be a logical interpretation of the term "undivided portion of an interest". That rule allows the disclaimer of part of a specific pecuniary amount. Thus, the disclaimer of $10,000 of a $50,000 bequest will be considered the disclaimer of an undivided portion of an interest.

The definition of a specific pecuniary amount is not clear. For example, the proposed regulations advise us that V, the devisee of the income from a 500 acre farm, could make a qualified disclaimer of 40% of his income interest in the farm. The example is intended to illustrate the disclaimer of a part of a specific pecuniary amount.

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95. I.R.C. § 2518(c)(1).
97. Id.
100. This is apparent by the reference in section 25.2518-3(c) to the example.
The application of the pecuniary interest rule appears to be at odds with the application of the partial interest rule, the trust rule and the undivided portion rule. Those rules provide that the disclaimer of an income interest for ten years from a life estate would not be qualified. If an income interest is considered a specific pecuniary amount, the pecuniary interest rule, which only specifies that “part” of the specific pecuniary amount must be disclaimed, should be interpreted to allow that disclaimer. There does not appear to be a logical reason for treating the disclaimer of 40% of a life interest as qualified, while treating the disclaimer of a ten year income interest from a life estate as not qualified.

E. Nine-Month Rule

Prior to the enactment of section 2518, the regulations provided that “a refusal to accept ownership does not constitute the making of a gift if the refusal is made within a reasonable time after knowledge of the existence of the transfer.” On its face, this requirement seemed logical and understandable. However, the reasonable time requirement became an unworkable standard for determining the federal tax consequences of a disclaimer. The primary problem in using such a standard was the fact it had to be applied on a case by case basis. There-

104. This result seems to follow proposed regulations section 25.2518-3(D) example 4.
105. For a collection of cases illustrating this point, see W. PAGE, PAGE ON THE LAW OF WILLS 46, 46-47, nn.5-9 (1960). There was both a common law requirement of reasonable time and a federal law requirement of reasonable time. However, in many cases, they were treated as a single standard. See Keniath v. Comm'r, 480 F.2d 57, 61 (8th Cir. 1973); Estate of Rolin v. Comm'r, 68 T.C. 919, 927 (1977); Estate of Dreyer v. Comm'r, 68 T.C. 275, 291 (1977), acq. 1978-12 I.R.B. 6 Contra, Jewett v. Comm'r, 70 T.C. 430, 436 (1978). See also Treas. Reg. § 25.2511-1(c) (1972).
106. WAYS AND MEANS COMM. REPORT, supra note 6, at 66-67.
107. See Estate of Dreyer v. Comm'r, 68 T.C. 275 (1977). Therein the court held: “[w]hat is the reasonable time varies with the circumstances of each case. The time may be very long if injury to others will not result.” Id. at 293 (citing In re Estate of Mexter, 83 Misc. 2d 290, __, 372 N.Y.S.2d 296, 299 (N.Y. Country Surr. Ct. 1975)).
fore, prior to the enactment of section 2518, it was nearly impossible to decide with certainty whether a disclaimer was made within a reasonable time.

The Eighth Circuit’s decision in *Kenaith v. Commissioner*108 was primarily responsible for the enactment of the nine-month rule. In *Kenaith*, the disclaimant had a vested remainder subject to divestiture. The disclaimer was made nineteen years after the creation of the interest but only six months after the death of the life beneficiary. The court was faced with the difficult question of determining when the period of reasonable time commences. The Tax Court109 held that a reasonable time should be interpreted according to a federal standard,110 and nineteen years was held not to be a reasonable time. The Eighth Circuit reversed the Tax Court saying:

In determining ‘reasonable time’ and the related issue of when the reasonable time commences, we perforce, absent a federal statute or regulation defining reasonable time, must look to the law of the states. We are not conclusively bound by the state law, but this is the only field to probe for legal decisions and discussions on the phrase ‘reasonable time’ as used in the context of making valid disclaimers.111

After examining many authorities, the court concluded that when a vested interest subject to divestiture is involved, the reasonable time period commences after the death of the life beneficiary, not at the time the interest was created.112 The result in *Kenaith* was a disclaimer

108. 480 F.2d 57 (8th Cir. 1973); *WAYS AND MEANS* COMM. REPORT, *supra* note 6, at 66-67.
110. The Tax Court relied on Fuller v. Comm’r, 37 T.C. 147 (1961) which held a disclaimer 25 years after the creation of the interest was not within a reasonable time. These Tax Court decisions create a federal standard, which measures a reasonable time from the creation of the interest whether the interest is a present interest or a future interest, and whether it is vested or contingent. See Jewett v. Comm’r, 102 S. Ct. 1082 (1982).
111. 480 F.2d at 61.
112. We hold . . . that under the prevailing common law and, in particular, the jurisdiction of the State of Minnesota the holder of a vested remainder interest subject to divestiture has a reasonable time within which to renounce or disclaim the remainder interest after the death of the life

https://nsuworks.nova.edu/nlr/vol7/iss2/2
made nineteen years after the creation of the interest, but six months after the death of the life beneficiary, was within a reasonable time. At that point, it became clear that allowing local law to dictate what a "reasonable time" was presented an inadequate method of determining the federal tax consequences of a disclaimer.

Section 2518 eliminated the confusion surrounding the reasonable time rule by requiring the disclaimer to be made not later than nine months after the date on which the transfer creating the interest in such person is made.113 Section 2518, however, does not eliminate the confusion surrounding the issue of when the transfer creating the interest occurs.

The Supreme Court has recently decided a pre-Section 2518 disclaimer case in which the question presented was when did the "transfer" creating the interest occur.114 The Court held that the disclaimer by a trust beneficiary of a contingent interest in a testamentary trust thirty-three years after the trust was created, but while the interest was still contingent, was a taxable transfer because the word "transfer" includes the creation of future interests and contingent remainders.115 Thus, the Supreme Court interpreted "transfer" as taxable transfer.

The proposed regulations provide that the nine month period is determined with reference to each taxable transfer.116 A taxable transfer occurs with respect to intervivos transfers when there is a completed gift for federal gift tax purposes; a taxable transfer occurs with respect to testamentary transfers upon the date of decedent's death.117 This definition is in accord with the definition of transfer intended by Congress.118

If transfer is defined as taxable transfer, it necessarily follows that

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beneficiary and that an unequivocal disclaimer filed within six months thereof is made within a reasonable time.

Id. at 64; contra Jewett, 102 S. Ct. 1082. In Jewett, the court measured the time from the creation of the interest, rather from the interest became indefeasibly fixed, and concluded 30 years was not reasonable.


115. Id.


117. Id. See also I.R.S. Letter Ruling 8008078, Nov. 28, 1979.

the disclaimer of certain interests in property will become almost im-
possible. One such interest in property is created by the exercise of a
special power of appointment. Where a donee is given a special power,
the gift (or devise) is a taxable transfer. The donee must disclaim
within nine months from that date in order for the disclaimer to be
"qualified." If the donee chooses not to disclaim and subsequently exer-
cises the power, the appointee’s disclaimer must be made within nine
months of the transfer of the power to the donee for it to be qualified.
The nine months do not begin when the power is exercised since the
exercise of a special power is not a taxable transfer. Consequently,
the "transfer" creating the appointee’s interest is the creation of the
power. The harshness of this interpretation is somewhat ameliorated
by the extension of the nine month disclaimer period for disclaimants
less than twenty-one years of age.

In many cases, the donee of the power will refrain from exercising
it for a period in excess of nine months. In such cases, the appointee
will be precluded from making a qualified disclaimer even though as he
is unaware of his interest until it is too late.

In addition to making a qualified disclaimer of some interests im-
possible, Congress‘ definition of transfer as taxable transfer allows
some “qualified” disclaimers to be made many years after the interest
was created. If we assume that a special power of appointment can
reach the hands of the holder of the power without the occurrence of a
taxable transfer (which can easily happen when the holder acquired it
for full and adequate consideration, for example section 2516), when
will the nine month period begin for the appointee under the special

119. The exercise of a special power of appointment is not a transfer (completed
gift for gift tax purposes). See I.R.C. § 2514 (1954) and Self v. United States, 142 F.
Supp. 939 (Ct. Cl. 1956). The death of B with a special power of appointment is not a
taxable transfer. See I.R.C. § 2041 (1954); Clauson v. Vaughan, 147 F.2d 84 (1st Cir.
1945); James v. Reynolds, 57 F. Supp. 609 (D. Minn. 1944). The reason the exercise
of a special power of appointment is not a transfer is because powers of appointment
are not interests in property. The following cases, although prior to I.R.C. § 2041, are
useful to demonstrate that a power of appointment (general or special) is not an inter-

in a decedent’s gross estate because of I.R.C. § 2041
(not I.R.C. § 2033).
power? It is easier to determine when the nine month period does not begin. We know it does not begin when the holder acquired the power since that is not a "transfer." We know it does not begin when the power is exercised since the exercise of the special power is not a "transfer." Insofar as no other events occurred, we must conclude that the period never commenced. Logic tells us that a period which never commenced can never end. Therefore, in certain situations, the appointee may have the opportunity to disclaim many years later (assuming he has not accepted the interest or its benefits) and have it qualify.

The result in the above discussion would be vastly different if the donee is given a general power as opposed to a special power. Since the exercise of a general power is a taxable transfer, the appointee will have nine months from the exercise of the power in which to disclaim. Thus, an appointee under a general power will always have nine months to disclaim; whereas, the appointee under a special power (especially if it is a testamentary power) will rarely have such an opportunity.

The obvious question that arises regarding the commencement of the nine-month period, is whether a disclaimer of property passing by the exercise of a special power should be treated differently than a disclaimer of property passing by the exercise of a general power. If we focus upon the disclaimant's right to disclaim, there is no justification for such a distinction. The appointees under both the general and the special power are similarly situated. They have no way of knowing if they will be appointed, when they will be appointed or what they will receive if appointed. In each case, their ownership arises as a result of the exercise of the power. Therefore, it is of little concern to the appointee what type of power the holder exercised.

The sole distinction between a general and a special power is with


[I]n the case of a general power of appointment where the other requirements are satisfied, the person who would be the holder of the power will have a 9 month period after the creation of the power in which to disclaim and the person to whom the property would pass by reason of the exercise or lapse of the power would have a 9 month period after a taxable exercise, etc., by the holder of the power in which to disclaim.
respect to the federal taxation of the holder of the power. The holder of a general power is taxed upon its exercise; the holder of a special power is not.\textsuperscript{122} The imposition of a transfer tax upon the holder of the power is an inadequate basis to justify disallowing the disclaimer by an appointee under special power (if made within nine months of the exercise of the power), since the tax is unrelated to the rights of the appointee. Therefore, it is unreasonable to require the disclaimer made by an appointee under special power be within nine months of the transfer creating the power (which may be prior to the exercise of the power), when an appointee under a general power is permitted to disclaim within nine months after the exercise of the power. To remedy this unwarranted distinction, as well as to cure the situation where no transfer occurs, section 2518 should be amended or regulations promulgated defining transfer in a manner which treats the appointee under a general and a special power similarly in all cases. Florida Statutes section 732.801\textsuperscript{123} provides an excellent example of when an interest must be disclaimed to assure that the recipient of any interest in property has a fair opportunity to disclaim:

(5) Time for Filing Disclaimer — A disclaimer shall be recorded at any time after the creation of the interest, but in any event within 9 months after the event giving rise to the right to disclaim, including the death of the decedent; or, if the disclaimant is not finally ascertained as a beneficiary or his interest has not become indefeasibly fixed both in quality and quantity at the death of the decedent, then the disclaimer shall be recorded not later than 6 months after the event that would cause him to become finally ascertained and his interest to become indefeasibly fixed both in quality and quantity.\textsuperscript{124}

The requirement that the disclaimant not accept any interest in the disclaimed property provides an adequate safeguard to prevent any abuse that may arise as a result of allowing additional interests to be disclaimed.

\textsuperscript{122} \textit{See} I.R.C. § 2514 & 2041; Treas. Reg. § 25.2514-1(a)(1) (1958). The Generation Skipping Tax rules contained in I.R.C. § 2601-2614 may provide the required "taxable transfer" in certain situations where special powers are created.


\textsuperscript{124} \textit{Id.}
Formula Clauses

It is often impossible to determine whether or not a disclaimer should be made or the amount of property which should be disclaimed within nine months from the date the property was transferred. In large estates, the property may not yet have been valued and there may be considerable litigation concerning the title to property as well as the validity of claims filed against the estate. Thus, the disclaimant may be faced with the dilemma of guessing whether a disclaimer is necessary or how much property he must disclaim. Section 2518 does not expressly provide a disclaimant relief from this problem.

In several private letter rulings, the IRS has ruled that a partial disclaimer will be qualified where the disclaimant uses a formula based disclaimer. For example, a beneficiary’s disclaimer of only so much of the decedent’s estate as is needed to cause property equal to the optimal marital deduction to pass to the surviving spouse will be qualified. This is a logical as well as practical interpretation of the statute.

F. Acceptance of Benefits

Both the common law of disclaimers and Section 2518 provide that the disclaimant must not accept any of the benefits of the disclaimed property for the disclaimer to be qualified. The proposed regulations similarly provide that the disclaimant cannot expressly or “impliesly” accept the benefits of the disclaimed property prior to making the disclaimer. If the disclaimant is also a fiduciary, his actions in such capacity to preserve or maintain the property are not considered an acceptance of the benefits of the property. The proposed regulations do not define the term “implied acceptance” other than by the use of one example. In that example, Blackacre was devised to A. A never resided in Blackacre, but when the property taxes became due A

paid them out of his personal funds. A later attempted to disclaim Blackacre. The example concludes that A’s payment of the property taxes was an “implied acceptance” of Blackacre. That result seems to be an extremely harsh interpretation of the non-acceptance requirement in light of the fact that A was merely intending to preserve the property. If this example is altered to provide that A, instead of paying the property taxes, made a monthly mortgage payment on property devised to him subject to a mortgage, presumably the IRS would consider the mortgage payment an “implied acceptance”.

It is doubtful that Congress intended the nine month period for disclaimers to be shortened where there is a gift or devise of encumbered property. In the case of a family residence, the beneficiary or devisee will be faced with the dilemma of deciding whether to disclaim the property prior to the first mortgage payment becoming due or to not make the payment of the mortgage and possibly causing a default and/or foreclosure.

The IRS in several recent private letter rulings has taken a more rational position with respect to acceptance of benefits. In letter ruling 8140025, the IRS ruled that the disclaimant’s payment of utility and light bills on property later disclaimed by the executor of the disclaimant did not constitute an acceptance of the benefits of the property. It is difficult to find a conceptual distinction between paying the property taxes on devised real property and paying the utility and light bills on such property. Hopefully, the final regulations will be more coherent in this respect.

In an example in the proposed regulations, the IRS has taken an erroneous position with respect to the interaction between the nine month rule and the acceptance of benefits rule. In that example, ten shares of stock were given to H under the State X uniform gift to minors act. Majority in state X is eighteen. At the time of the gift, H was fifteen years old. Upon attainment of the age of eighteen, the ten shares were delivered and registered in H’s name. H, within nine months of attaining the age of twenty-one, disclaimed the ten shares.

The example concludes that H's disclaimer is not qualified because H received fee ownership of the shares on his eighteenth birthday but failed to disclaim the shares within nine months thereafter. Interestingly, the Regulation did not cite H's acceptance of the benefits of the property as its basis for concluding the disclaimer was not qualified. The conclusion in this example is clearly wrong if it is based on the fact that H's disclaimer was not qualified solely because it was not made within nine months of H's eighteenth birthday. Section 2518(b)(2)(B) clearly provides that H had nine months after the day on which he attained the age of twenty-one in which to disclaim.

It appears to be the IRS's position that the receipt of trust income by a beneficiary does not preclude the beneficiary from disclaiming his interest in corpus.\textsuperscript{133} The proposed regulation illustrates this point in the following example. The current income beneficiary of a trust, B, is to receive one-half the corpus upon attainment of the age of forty. B received one income distribution and then attempted to disclaim his interest in the income and corpus of the trust. The example concludes that B's disclaimer of the income is not qualified insofar as he has accepted income prior to making the disclaimer. However, B's disclaimer of the corpus is qualified. Even though the "partial disclaimer rule" treats B's interest in income and corpus as two separate interests, the IRS is quite liberal in its interpretation that B has not accepted the benefits of the corpus in this example.

G. Use of Disclaimers as a Method of Achieving Tax Savings

\textit{Charitable Remainders}

It is not uncommon for individuals to make charitable dispositions of their property upon their death. One popular form of charitable transfer is the creation of a trust, inter vivos or testamentary, with the corpus passing to a charity upon the occurrence of a stated event or the expiration of a stated number of years.\textsuperscript{134} To be deductible for estate tax purposes, the transfer of a remainder interest in trust property must qualify as a charitable remainder annuity trust or a charitable remain-

\textsuperscript{133} Prop. Reg. § 25.2518-2(d)(1)(iii) example 1.
\textsuperscript{134} See I.R.C. § 2055 (1955).
der unitrust. There are numerous highly technical requirements which must be satisfied for a trust to fall into these categories. If for any reason a trust fails to satisfy the requirements, the estate tax deduction will be lost. Therefore, extreme care must be exercised to avoid the slightest transgression of the charitable transfer rules.

If a decedent makes a transfer of a remainder interest to a charity which is not in the required form, it is still possible to salvage a charitable deduction for the decedent’s estate. Assume that D dies with an estate of $100,000,000 and his will creates a trust with a corpus of $50,000,000 for the benefit of his son, S, for life, remainder to Nova Law Center. Under the terms of the trust, S is guaranteed an annual distribution of $2,000,000 and the trustee has the power to invade corpus for the benefit of S. The trust is not a charitable remainder annuity trust or unitrust because S does not have the right to receive at least 5% of the initial corpus annually and an amount other than the payment of a sum certain (or fixed percentage) of corpus may be paid to S. Therefore, D’s estate will not be entitled to a charitable deduction.

If S disclaims each of his interests in the trust, the transfer will be deemed to have been made directly from D to Nova Law Center which entitle D (or his estate) to a charitable deduction. Therefore, S’s disclaimer of his interest in the trust will salvage the charitable deduction for D’s estate.

Marital Deduction and Unified Credit

A 1978 amendment to section 2518 made it possible for property to pass to a decedent’s spouse as a result of a disclaimer even if the

137. I.R.C. § 2055(e)(2).
140. Rev. Rul. 78-152, 1978-2 C.B. 296. In Letter Ruling 8031018, March 21, 1980, the IRS ruled that as a result of a beneficiary’s disclaimer, his income interest never arose, thus, the charity was considered as having received its interest in the estate immediately.
surviving spouse was the disclaimant.\footnote{141}{Tax Reform Act of 1978, Pub. L. No. 95-600, § 702(M), 92 Stat. 2934 (1978), amended I.R.C. § 2518(b)(4).} This amendment is important because it allows a surviving spouse to disclaim an interest in a marital trust and take the property under a non-marital trust assuming the decedent’s will is set up properly.\footnote{142}{The decedent’s will must contain a marital bequest (one which qualifies for the marital deduction) and a non-marital bequest (one which does not qualify for the marital deduction and does not cause the property to be included in the spouse’s gross estate), with the decedent’s spouse named as the beneficiary under each trust. The non-marital trust should be drafted in manner so as to give the spouse all the incidents of ownership consistent with its exclusion from the spouse’s gross estate. In addition, it is advisable to include in the decedent’s will a clause which provides that any property disclaimed shall pass to the non-marital trust.} A spouse will only make such a disclaimer when the marital bequest exceeds the “optimal” marital deduction.\footnote{143}{The optimal marital deduction is not necessarily the maximum marital deduction allowable because consideration must be made for items such as the unified credit and other deductions available to the estate.} One common situation where the marital bequest exceeds the optimal marital deduction occurs where the decedent’s will fails to take the unified credit into consideration when funding the marital trust. The estate of every decedent who was a citizen or resident of the United States at the time of death is entitled to a credit against his estate tax.\footnote{144}{I.R.C. § 2010 (1976).} In 1982, the credit is $62,800.\footnote{145}{I.R.C. § 2010(b) (1976).} The $62,800 credit means that a taxable estate of $225,000 or less will not have to pay any estate tax.

Sound estate planning dictates that the decedent’s taxable estate not be less than the amount of the credit against estate tax available to the decedent.\footnote{146}{If the taxable estate is less than the credit, the excess of the credit over the decedent’s estate tax liability will be wasted. The credit is also used to reduce the tax payable on certain gifts made during the decedent’s lifetime, thus, the entire credit may not be available at the decedent’s death.} The concept is illustrated by the following example. D dies with a gross estate of $450,000. His wife, W, has no separate property. D wishes to avoid all estate tax upon his and W’s death. D’s will provides:

\[\text{If my spouse survives me, I give to my trustee, hereinafter named,}\]
a pecuniary amount equal to the maximum marital deduction allowable to my estate for federal estate tax purposes, less the aggregate amount of marital deductions, if any, allowed for interests in property passing or which have passed to my spouse otherwise than by the terms of this article.

Since ERTA 1981, the maximum marital deduction is 100% of D’s gross estate. Therefore, the provision of D’s will transfers D’s entire estate—$450,000—to a marital trust created for W. Since D’s estate will be entitled to a marital deduction of $450,000, D’s taxable estate will be zero and no estate tax will be payable on D’s death. W will have a taxable estate of $450,000 because the corpus of the marital trust will be included in her estate upon her death. If W also dies in 1982, her estate will be taxed on $450,000, yielding a tax of $138,800, and her estate will be entitled to a credit of $62,800.

If D’s will provided that the marital bequest was to be reduced to take into consideration the value of the credit available to D with the remainder of D’s estate used to fund a non-marital trust for the benefit of W, D’s estate tax would remain zero and there would be no tax payable on W’s death because W’s taxable estate would be limited to $225,000 and the credit available to W’s estate, $62,800, would reduce the tax to zero. Thus, no estate tax would be payable on the death of D and W, an estate tax savings of $76,000 over the situation above.

In those situations where a decedent’s will does not allow for the reduction of the marital bequest by the amount of credit available to the decedent’s estate, the situation can be corrected by having the decedent’s spouse disclaim the portion of the marital bequest which is necessary to allow the decedent to make full use of his credit. In the situation posed above, W would disclaim $225,000.

The benefits to be derived by such a disclaimer are the securing of the optimal marital deduction and the exclusion of the disclaimed property from the disclaimant’s gross estate. In theory such a disclaimer is

147. ERTA 1981.
148. I.R.C. § 2056 (1954) (amended by 1981 ERTA). I assume that the marital trust was a qualified terminable interest trust.
149. See I.R.C. §§ 2033-2042 (1976). The non-marital portion ($225,000) would not be included in W’s estate because she would not have an interest in property of a character which is includible in her estate.
an effective post mortem estate planning device, but before a spouse makes such a disclaimer, he or she will have to be convinced that it is a beneficial course of action. The proposed regulations inhibit the ability of a surviving spouse to disclaim in this circumstance by providing that "[i]f the surviving spouse . . . retains the right to direct the beneficial enjoyment of the disclaimed property in a transfer that is not subject to Federal estate and gift tax, such spouse will be treated as directing the beneficial enjoyment of the disclaimed property."\textsuperscript{150} The proposed regulation should be revised to provide that the typical powers given to a surviving spouse as part of a non-marital trust should not taint an otherwise qualified disclaimer.

\textit{Special Use Valuation}

Generally, the property included in a decedent's gross estate is valued at its fair market value at the date of the decedent's death.\textsuperscript{151} If certain conditions are satisfied, real property included in a decedent's estate will be valued on the basis of its current use rather than its fair market value.\textsuperscript{152} To be eligible for the special valuation, the real property must be used for farming or other closely held business purposes and must pass to a qualified heir.\textsuperscript{153} A qualified heir includes an ancestor or lineal descendant of the decedent and the decedent's spouse or parent.\textsuperscript{154} The IRS has ruled that a devise of real property not satisfying the requirements for special use valuation may be effected by the use of a disclaimer.\textsuperscript{155} In that ruling, a farm was bequeathed to A, a

\textsuperscript{150.} If the marital trust is a qualified terminable interest trust, the property interests the spouse receives in the non-marital trust are extremely similar to the property interests that spouse had in the marital trust. The spouse can receive, under a non-marital trust, the following: a life estate, a special power of appointment, a five and five general power of appointment, a general power of appointment subject to an ascertainable standard, and the trustee can be given the power to invade the corpus for the spouse's comfort or maintenance. But see proposed regulations section 25.2518-2(e)(2) which requires the surviving spouse to give up certain of the powers that the spouse could otherwise enjoy as part of the non-marital trust.

\textsuperscript{151.} See I.R.C. § 2031(a) (1954).
\textsuperscript{152.} I.R.C. § 2032A (1976).
\textsuperscript{153.} I.R.C. § 2032A(e)(2) (1976).
\textsuperscript{154.} Id.
qualifying heir, and A was given a testamentary special power of appointment. The class of permissible appointees available to A included non-qualifying heirs. Since A had the power to appoint the property to non-qualifying heirs, the property did not qualify for special use valuation. The IRS ruled that the disclaimer by A of his special power of appointment made it possible for the property to be specially valued because, as a result of the disclaimer, the remainder vested in a qualified heir.

IV. Conclusion

This article has attempted to trace the law of disclaimers from the date of enactment of section 2518 in 1976, to the present. In the six year period beginning with the enactment of section 2518, the IRS has not issued final regulations. Moreover, the IRS has interpreted section 2518 in a manner that caused Congress to amend that section in 1981 to carry out the expressed purpose of the 1976 legislation.

On July 22, 1980, the IRS published proposed regulations interpreting section 2518. Those regulations contain many definitional flaws and examples which at best are misleading. The treatment of the disclaimer of jointly held property in the proposed regulations clearly impose rules not contained in the statute and effectively prohibits the disclaimer of most interests in jointly held property. The IRS has created numerous vague and arbitrary tests for determining whether partial disclaimers are valid. One major shortcoming with the IRS approach is reliance upon state law to determine whether a partial disclaimer is qualified.

It is distressing that the IRS has yet to issue final regulations, and has continued, in one way or another, to impose the peculiarities of state law upon section 2518. Hopefully, the IRS will carefully review the proposed regulations and rethink its position.

156. Id.
157. Id.