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Construing Wills and Trusts During the Estate Tax Hiatus in 2010

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Construing Wills and Trusts During the Estate Tax Hiatus in 2010

S. Alan Medlin, Howard M. Zaritsky, and F. Ladson Boyle*

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Many estate planners have drafted wills and revocable trusts with dispositive provisions based on formulas. These formulas often use language based on transfer tax terminology. For clients who die in 2010, the language used in these formulas will be ambiguous, if not apparently meaningless, because Congress failed to re-institute the estate tax for 2010. The resulting 2010 estate tax hiatus will result in will and revocable trust construction problems for the estates of many decedents who die during the hiatus. Courts will have to use statutory and common law construction methods to attempt to determine the decedent’s dispositive intentions. This Article explains the hiatus construction problem and examines possible alternatives for attempting to determine the decedent’s intent.

Introduction

In 2001, Congress passed tax legislation dramatically increasing the amount of property that a decedent could transfer without the payment of estate taxes. This legislation included a temporary repeal of the federal estate tax in 2010. Under the sunset provisions of the 2001 Act, however, all of the changes made in 2001 will expire at the end of 2010, and the law will automatically revert to that which existed before the enactment of the 2001 Act.

After the enactment of the 2001 Act, many estate planners believed that the federal estate tax would be permanently repealed before 2010. That legislation did not pass. In more recent years, the mood shifted and most estate planners believed that the Congress would set new permanent estate tax rates and exemptions rather than permit a year in which there was no estate tax. That legislation did not pass, either. The 2010 federal tax surprise — no estate tax and no tax on generation-

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2. EGTRRA incrementally raised the estate tax exemption amount from $675,000 in 2001 up to $3.5 million in 2009. The amount free of gift taxes rose to $1 million under the 2001 Act but did not increase thereafter because it was de-coupled from the estate tax. In 2011, the gift tax exemption equivalent will remain at $1 million.
4. Id. § 901.
skipping transfers — has many tax implications that are discussed elsewhere.

I. OVERVIEW OF PROBLEMATIC SITUATIONS RAISING CONSTRUCTION ISSUES

A. Tax-Based Will Formulas

In addition to the tax issues, nontax state law concerns arise because there is no federal estate tax in 2010. One particular issue has the potential to cause significant problems for estates of decedents who die while there is no federal estate tax. Many wills and revocable trusts that are drafted to be estate-tax sensitive divide a decedent’s estate or revocable trust between a surviving spouse or a trust for a surviving spouse (hereinafter collectively described as a gift to a surviving spouse) and a gift to a bypass, credit shelter, or family trust or to someone other than the surviving spouse (hereinafter collectively described as a gift to the bypass trust).

The controlling document’s division between the surviving spouse and the bypass trust is often worded with formulas that use estate tax terms to describe the division. For example, such a formula simplistically might give the bypass trust “the maximum amount of property of the decedent’s estate that may pass free of estate taxes.” Alternatively, the formula might give the surviving spouse an amount equal to the maximum marital deduction — that is, all of the estate, but reduced by the greatest amount of property that can pass to others free of federal estate taxes. When these formulas use terms that refer to federal estate taxes, the unified credit, the applicable credit amount, the applicable exclusion amount, the exemption equivalent, or other such similar tax-based terms that have no tax meaning in 2010, the state law question

5 Although this article describes the absence of an estate or GST tax in 2010, that is not technically correct on either level. There is an estate tax in 2010 on recapture events with respect to estates of decedents who died before 2010, and on distributions from qualified domestic trusts. There is no tax on generation-skipping transfers, but the GST rules still appear to exist with respect to other issues involving the GST tax. I.R.C. § 2664.


becomes: how is the property of the decedent’s estate or revocable trust to be divided? To answer this question, it is first necessary to examine the variations in wording of the formulas that produced the same result when there was an estate tax, but potentially very different results when there is no estate tax.

B. Types of Formulas

Formulas that divide a decedent’s estate between gifts to a surviving spouse and a bypass trust to maximize estate tax savings at the death of the surviving spouse, consistent with deferral of the estate taxes until the surviving spouse’s death, usually can be classified as either pecuniary formulas or fractional share formulas. A pecuniary formula may be used to define the gift to the surviving spouse or the gift to the bypass trust. A fractional share formula used to divide the estate or trust between the surviving spouse and the bypass trust is usually a division of the residue of the decedent’s estate or reminder of the property in the decedent’s revocable trust.

A typical pre-residuary marital deduction formula might leave the surviving spouse an amount equal to the maximum federal estate tax marital deduction — that is, all of the decedent’s estate — but reduced by the most that may pass free of estate taxes, after taking into account the unified credit or the applicable credit amount, as well as such other possible adjustments as prior taxable gifts to someone other than the surviving spouse. Alternatively, the gift to the surviving spouse might be described as the maximum marital deduction, less the applicable exclusion amount, or as the minimum amount of property necessary to reduce the federal estate tax to zero or to the lowest possible amount.

A pre-residuary, pecuniary bypass trust formula might give the bypass trust the most property that can pass free of federal estate taxes, after various adjustments, with the residue given to the surviving spouse. Alternatively, the gift to the bypass trust might be described as an amount equal to the applicable exclusion amount or applicable credit equivalent.

The wording of each of these pecuniary formulas, or similar wording, may be used to define the numerator of a fractional share division of the decedent’s residuary estate or the remainder of the decedent’s revocable trust, with the denominator of the fraction being defined as the residue of the decedent’s estate or the remainder of the trust estate for a revocable trust.

When the estate tax is in effect, all variations of the pecuniary or fractional share formulas result in a division of the decedent’s property that was reasonably anticipated by the decedent and that was likely clear under the terms of the controlling document. For example, in 2009
each of the various formulas applied to a $5 million estate (after debts, expenses, and other deductible transfers) would have produced a $1.5 million gift to the surviving spouse and a $3.5 million bypass trust gift. The different formulas potentially resulted in differing divisions of estate income and appreciation or depreciation, but not in the allocation of the date-of-death (or alternate valuation date) value of the decedent’s assets.

In 2010, however, the results of these different formulas are potentially quite different because there is no estate tax and the technical tax terms used have no meaning. For example, a formula that gives the surviving spouse the maximum marital deduction less the greatest amount that can pass to other family members free of federal estate taxes seems to leave the surviving spouse nothing because the entire estate can pass free of estate taxes to other family members: the cutback provision takes everything away from the surviving spouse.

Alternatively, some of the formulas may produce a 100 percent gift to the surviving spouse. For example, a formula that leaves the bypass trust an amount equal to the applicable exclusion amount may be a gift of nothing because there is no applicable exclusion amount in 2010.

It might also be asserted that these formulas do not direct the disposition of the decedent’s property at all because the division is based on tax terms that have no meaning in 2010. These formulas are further complicated by collateral provisions often included in a will or revocable trust, such as the provision that the marital gift must be satisfied solely with property that qualifies for the federal estate tax marital deduction. For example, a gift to the bypass trust of the amount of the decedent’s applicable exclusion amount would seem to give the entire estate to the surviving spouse, because there is no applicable exclusion amount in 2010, but if the will then states that the spouse is to receive only assets that qualify for the federal estate tax marital deduction, the spouse would seem to receive nothing. In this situation, the residuary estate may, by default, pass by intestacy.

Similar issues arise when the decedent’s estate or revocable trust is divided between trusts that are exempt from the federal generation-skipping transfer (GST) tax and trusts that are not exempt. Often formulas are used for this division based on the GST exemption amount defined in section 2631(c) of the Internal Revenue Code. The 2010 hiatus problem exists for these types of formulas because the amount of the GST exemption is defined by section 2631(c) with reference to the “ap-

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8 A discussion of the consequences of pecuniary versus fractional share formulas is beyond the intended scope of this article. For a comparison of these types of formulas, see F. Ladson Boyle, Distinguishing Pecuniary and Fractional Devises, 5 Prob. Prac. Rptr. 1 (May 1993).
plecible exclusion amount under section 2010(c) for such calendar year.” For 2010 there is no applicable exclusion amount.

In addition, some testators make charitable gifts of their estate in excess of their applicable exclusion amount. The absence of an applicable exclusion amount in 2010 could result in the charity receiving the entire estate, or in the charity receiving nothing, depending upon the precise wording of the clause.

At the time this article went to print, Congress had been considering the enactment of bills that would resurrect the estate tax. Even if Congress resurrects the estate tax in 2010 and makes its application retroactive, the construction issues discussed in this article remain relevant. A will is read as of the time of the testator’s death. For decedents who die before any such new estate tax bill is enacted, for state law construction purposes the decedent’s will or trust, speaking at the time of the decedent’s death, will still have terms that are ambiguous, at best. A federal enactment that retroactively applies tax law does not necessarily retroactively affect state law construction issues. Beneficiaries will still argue about the meaning of the tax-based formulas in the will or trust. Moreover, it is not uncommon for tax-sensitive wills and trusts to define tax terms by referring to the Internal Revenue Code in effect at the time of the decedent’s death.

C. Other Possible Problems

Besides problems dividing a decedent’s estate or revocable trust in 2010 using tax driven formulas, the lack of an estate tax during the hiatus has potential spousal elective share implications. If a state’s spousal share calculation is affected, at least in part, by whether an interest to a surviving spouse qualifies for the federal estate tax marital deduction, when there is no federal estate tax in 2010, the reference to the federal estate tax marital deduction is meaningless for this purpose. One response to this possible abyss is to refer to the federal estate tax marital deduction as it existed before 2010. In states that have statutes imposing a state estate tax that is based on the federal estate tax, but whose statutes were not repealed in 2010 so a state estate tax is due, the problems are numerous. For example, state estate tax QTIP elections in some jurisdictions are dependent on a federal estate tax QTIP election

\[10\] See infra text accompanying note 54.
being made under section 2057(b)(7) of the Internal Revenue Code, which cannot be done when there is no federal estate tax.\textsuperscript{13}

D. A Matter of Construction

For decedents dying in 2010 when there is no estate tax, the nontax state law question about disposition of the decedent’s assets, by will or by revocable trust, becomes a matter of construction. The dispute will often be between the surviving spouse and the beneficiaries of the bypass trust; for GST issues, the pool of litigants may be broader.

A decedent who anticipated that Congress would not act to prevent the 2010 hiatus is likely to state his or her intent clearly in the document and construction should not be a problem. A decedent who did not express an intention in the documents or assumed that there would be an estate tax in 2010, however, presents a more difficult construction issue.

Underlying the traditional notions of the construction of wills and revocable trusts is the goal of determining what the decedent intended to do about a certain situation that is not clearly explained in the documents.\textsuperscript{14} Nevertheless, the traditional application of construction rules is predicated on the principle that the decedent had an intention about a particular issue but did not clearly express it.\textsuperscript{15} While it may be possible that the decedent had an intention about a division of assets during the estate tax hiatus but failed to express it in the documents, it is also possible, and perhaps likely, that the decedent did not even consider that possibility. Had the decedent considered the possibility of dying during the 2010 hiatus, the documents would probably express an intent about that prospect.

For example, a testator who anticipated the possibility of a year without an estate tax might have simply said to continue the 2009 division through 2010, so that both the surviving spouse and the beneficiaries of the bypass trust might share in the estate in the same manner that they would have done had the testator died a year earlier. Alternatively, a testator might have chosen to have the entire estate pass to the bypass share if the testator died in 2010, to minimize the estate taxes.

\textsuperscript{13} See Blattmaehr, Gans, Zaritsky & Zeydel, supra note 6. A discussion of those issues is beyond the intended scope of this Article.

\textsuperscript{14} See RESTATEMENT (THIRD) OF PROPERTY: WILLS AND DONATIVE TRANSFERS § 10.1 (2003) (“The controlling consideration in determining the meaning of a donative document is the donor’s intention. The donor’s intention is given effect to the maximum extent allowed by law.”).

\textsuperscript{15} Id. See also, e.g., Estate of Swallen v. Commissioner, 98 F.3d 919 (6th Cir. 1996); Fleming v. First Union Nat. Bank, 555 S.E.2d 728 (Ga. 2001); Pringle v. Houghton, 88 N.W.2d 789 (Iowa 1958); In re Scheyer’s Estate, 59 N.W.2d 33 (Mich. 1953); Crockett v. Scott, 284 S.W.2d 289 (Tenn. 1955).
that would be imposed on the surviving spouse if the surviving spouse died after 2010.

When the decedent’s documents do not express an intent about the hiatus because the decedent did not even speculate about the lack of a federal estate tax, construction becomes more of a stretch and, perhaps, a guess. In that case, the determiner of fact is not trying to discover what the decedent actually intended but did not clearly state, but rather what the decedent would have intended had the decedent thought about a hiatus death. This may appear to be guesswork rather than construction, but probate courts do engage in similar speculation in other cases. For example, the doctrine of dependent relative revocation allows a court first to determine that a decedent revoked a will by mistake and then to decide whether to leave the will revoked or not. This process is akin to guessing what the decedent would have wanted if the mistake had not been made — guessing is necessary because it is likely the decedent never considered what should occur if the mistake were made or else the mistake would not have been made.16

For example, the court in Estate of Eastman17 used dependent relative revocation to correct a mistake. The testator’s will as originally executed devised his entire estate to his wife and, if she predeceased him, to his two sons equally. His wife died in 1988. The testator struck through certain portions of his will which, after the strikethrough, appeared to leave his entire estate to only one son. The testator did not sign the alterations. Upon the testator’s death, the sons disputed the effect of the alterations to the will.

The court cited the applicable Washington statute that recognizes as valid a complete or partial revocation of a will obtained through striking through the language of the will. The court would not allow, however, the unsigned alteration to increase the testamentary disposition to one of the two sons. Thus, the court had to decide the effect of the alteration other than as an effective disposition of the entire estate to one son. Relying on the doctrine of dependent relative revocation, the court reinstated the will in its original version and divided the estate between the two sons. As demonstrated by Eastman, the doctrine of dependent relative revocation properly applied looks at the testator’s intent. If the testator revoked the will by mistake, then a court may review relevant evidence to determine whether the testator would have preferred to retain the revocation despite the mistake or would not have revoked. In other words, the court should determine whether, after recognition of

the mistake, the testator would prefer the will to devise the estate as partially revoked or before partial revocation.\textsuperscript{18}

II. State Legislation

Various state legislatures are attempting to address the 2010 hiatus. The different approaches being taken in these statutes reflect the competing interests of simplicity, certainty, and optimal tax planning.

A. The Virginia Plan

Most of the states that are attempting to address this situation are adopting an approach first introduced in the 2010 Virginia General Assembly and thereafter enacted as Virginia Code Section 64.1-62.4.\textsuperscript{19} That statute interprets references to estate and GST tax terms and Internal Revenue Code sections in the will or trust of a decedent who dies in 2010 as if the decedent had died on December 31, 2009. Thus, a provision leaving a decedent’s children the maximum amount that can pass free of federal estate taxes will leave them $3.5 million, even though the entire estate could pass free of federal estate taxes in 2010. Similarly, a provision leaving the decedent’s children an amount equal to the decedent’s available applicable exclusion amount will leave them $3.5 million, despite the fact that there is no applicable exclusion amount in 2010.

This approach provides certainty and relative ease of operation, but it may not produce the best tax result. A will that leaves to a nonmarital trust for the exclusive lifetime benefit of the surviving spouse the largest amount that can pass free of tax and leaves the residue outright to the surviving spouse will, under the Virginia statute, creates a $3.5 million nonmarital trust and an outright marital residue. The residue will be subject to estate taxes if the surviving spouse dies after the estate tax is restored in 2011.

A better tax result would be achieved if the entire estate passed to the nonmarital trust because the spouse would receive the lifetime benefits of that trust and no portion of the estate would later be subject to estate taxes. The Virginia statute, therefore, provides a less favorable tax result than would have been achieved had the will been construed as creating a 100 percent nonmarital trust. Of course, a literal reading of a will or revocable trust that left the nonmarital trust an amount equal to

\textsuperscript{18} The \textit{Eastman} court made no attempt to determine the testator’s intent but instead automatically assumed that dependent relative revocation would apply to cancel the revocation simply because the attempt to increase the devise to one son was ineffective. This result, however, was virtually necessitated by its refusal to distinguish between attempted increases to nonresiduary and residuary devises.

\textsuperscript{19} H.B. 755 (2010).
the decedent’s unused applicable exclusion amount would be that the entire estate passes outright to the surviving spouse. Thus, in some cases, the Virginia statute produces a better tax result than that achieved by a literal reading of the documents. A number of states have followed the Virginia statute.20

Two states have attempted to address some of the situations in which the Virginia plan would achieve a less-than-optimal tax result. Delaware S.B. 282, signed by the governor on July 12, 2010, excludes from the operation of the December 31, 2009 rule situations in which the will or trust construction: (a) would move property between trusts with “substantially similar” beneficial interests; (b) would move property from a trust to an individual who is eligible to receive unlimited discretionary principal distributions; or (c) a combination of the foregoing. The proposal includes some rules for determining whether beneficial interests in two trusts are “substantially similar,” but not really general guidelines. Also, the Delaware bill would permit a disinterested fiduciary to “opt out” of the interpretative presumption if 30 days notice is given to the beneficiaries and none of them objects.

Wisconsin S.B. 670, effective on April 13, 2010, excludes from the operation of the December 31, 2009 rule situations in which: (1) the decedent is survived by a spouse and issue, all of whom are also issue of the surviving spouse; and (2) the surviving spouse is a current income beneficiary of each trust funded in whole or in part by the formula, or the sole beneficiary of any other property subject to disposition by the formula that does not pass in trust. In this situation, the document is construed as it is written, so that an unlimited marital or nonmarital share may be created.

B. The Florida Approach

Florida has taken an approach entirely different from that adopted in Virginia. Florida passed two statutes: one deals with trusts21 and one

20 See, e.g., Delaware S.B. 282, signed by governor (July 12, 2010); Georgia S.B. 461, signed by governor (May 27, 2010); Idaho H.B. 472, signed by governor (March 18, 2010); Indiana S.B. 65, signed by governor (March 12, 2010); Maryland S.B. 337, signed by governor (April 13, 2010); Michigan H.B. 6197, passed by House of Representatives (June 1, 2010), referred to Senate Judiciary Committee; Minnesota S.F. 2427, signed by the governor (May 13, 2010); Nebraska L.B. 1047, signed by governor (April 12, 2010); New Jersey S. 1952, introduced and referred to judiciary committee (May 20, 2010); New York A.O. 9857, signed by governor (August 13, 2010); North Carolina S.B. 1176, signed by governor (July 21, 2010); South Dakota H.B. 1201, signed by governor (March 11, 2010); Tennessee S.B. 3045, signed by governor (March 17, 2010); Utah S.B. 121, signed by governor (March 26, 2010); Washington S.B. 6831, signed by governor (March 10, 2010); and Wisconsin S.B. 670, signed by governor (April 13, 2010).
21 Florida S.B. 998, signed by the governor on May 27, 2010.
CONSTRUING WILLS

deals with wills. These statutes authorize the courts to construe a will or trust that contains references to estate tax or GST tax provisions, or that is otherwise tied to a specified desired tax result (such as avoiding estate taxes at the decedent’s death and minimizing taxes at the surviving spouse’s death), to determine what the decedent or settlor would have wanted. The wills statute states, in part, that the court may construe a will, upon request of the personal representative, whether or not interested, to define tax-related provisions in light of the repeal of the estate and GST taxes. The court is then directed to:

consider the terms and purposes of the will, the facts and circumstances surrounding the creation of the will, and the testator’s probable intent. In determining the testator’s probable intent, the court may consider evidence relevant to the testator’s intent even though the evidence contradicts an apparent plain meaning of the will.

The South Carolina General Assembly passed legislation similar to Florida. The South Carolina legislation permits affected parties to petition the probate court for a construction of documents that use federal estate tax terms to define gifts. It does not provide a preferred construction, as legislation in other states such as Virginia has done.

The Florida and South Carolina approaches are more likely to produce a favorable tax result than the Virginia plan in many cases, but it will require litigation in every case, delaying the division and distribution of the estate or trust and increasing administrative expenses. This litigation to divine the decedent’s intent may be simple, if all of the beneficiaries and the fiduciary agree to the proper construction, or it may be quite heavily contested, if the interests of different beneficiaries are adverse. For example, a will that leaves a decedent’s children a share equal to the applicable exclusion amount and leaves to the surviving spouse the residue may not raise a serious battle if the spouse is the parent of the children and likely to leave them his or her own estate at death. On the other hand, if the spouse and the children do not at all

22 Florida H.B. 1237, signed by the governor on May 27, 2010.
23 FL. STAT. ANN. § 733.1051 (2010).
24 See Act No. 521, R. 314, S. 1348, effective June 11, 2010. The statute, in its entirety provides:
The personal representative, trustee, or any affected beneficiary under a will, trust, or other instrument of a decedent who dies or did die after December 31, 2009, and before January 1, 2011, may bring a proceeding to determine the decedent’s intent when the will, trust, or other instrument contains a formula that is based on the federal estate tax or generation-skipping tax. The proceeding must be commenced within twelve months following the death of the decedent.
25 See the discussion of family settlements, infra at Part III.D., and to Bosch, infra at Part III.G.
get along, this dispute may be quite heated and, necessarily, expensive and time-consuming.

C. The Ohio Approach

Ohio appears poised to take a third approach, but that legislation has not yet passed as of the time this article went to press. The Ohio approach expands the state’s statutory authority for binding agreements among the parties settling disputes regarding the construction of wills and trusts. The expanded provisions would authorize nonjudicial settlement of disputes over the meaning of tax terms in 2010. The Ohio bill would also authorize judicial modification to address these issues and provide a default rule by which, as in the Virginia legislation, tax-sensitive provisions are construed in the same manner that they would have been had the decedent died on December 31, 2009.

The Ohio approach offers the most choices, but to the extent that it encourages the use of family settlement agreements to resolve these disputes, it may present a problem. The IRS will consider itself free to interpret the governing instrument differently from the manner that the family has chosen. A recent technical advice memorandum demonstrates that the IRS will even reject testimony of the drafter of the documents in construing ambiguous instruments, if it believes that a court would not properly have considered that testimony.

D. The Pennsylvania Approach

The Pennsylvania approach is a hybrid of the Virginia and Florida plans. The Pennsylvania approach, represented by an amendment to Senate Bill 53 (June 18, 2010), first adopts a rebuttable presumption that any reference to the applicable exclusion amount, applicable credit amount, or other tax-related terms in the instrument of a decedent dying in 2010 refers to the amounts determined as if the decedent died on December 31, 2009.

The Pennsylvania bill also, however, provides that a decedent’s personal representative, trustee, or any affected beneficiary can bring an action to interpret the formula clause, that a court can modify the language of the instrument as part of such action, and that in determining the proper interpretation of the clause the court shall consider:

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26 Amendment to S.B. 251, introduced in the Ohio Legislature (April 27, 2010), and reported favorably by the Senate Judiciary Civil Justice Committee (June 2, 2010).
27 See TAM 201004022 (Jan. 29, 2010) (settlement agreement that was approved by lower court, without evidentiary hearing, rejected by IRS as basis for estate tax charitable deduction).
(1) The provisions and purposes of the will, trust, or other dispositive instrument.

(2) The facts surrounding the creation of the will, trust, or other dispositive instrument.

(3) The decedent’s known or probable intent, based on all the facts and circumstances surrounding the creation of the will, trust, or other dispositive instrument. In determining this intent, the court may consider evidence that contradicts the plain meaning of the will, trust, or other dispositive instrument.

(4) The identity and interests of beneficiaries of different shares resulting from the application of the formula clause.

The Pennsylvania bill does not state what the goal of this construction may be. It does not expressly state that the instrument should be construed to effectuate the decedent’s probable intent. It does, however, give the court the power to modify a provision in the will, trust, or other dispositive instrument “in a manner that is not contrary to the decedent’s probable intention in order to achieve the decedent’s tax and other objectives.” The bill also provides that a judicial modification or interpretation may be made effective as of the date of the decedent’s death.

III. OTHER CONSTRUCTION TOOLS

In states other than those enacting legislation adopting the Virginia approach, courts will have to resort to common law construction methods or existing statutory tools to resolve ambiguities. The case law involving the resolution of ambiguities in wills and trusts is both rich and instructive. In addition to the basic common law construction rules, courts attempting to decipher hiatus language have other available options. Construction cases specific to historical tax issues include attempts to deal with questions arising from the marital deduction transition rule, tax apportionment, and the state death tax credit. One innovative approach is the doctrine of probable intent — not widely used yet but seemingly right on point for hiatus death situations. In addition, the family settlement may be available to cure the problem. In some cases, relying on the law dealing with contracts concerning succession might prove useful. And for trust construction cases, relevant Uniform Trust Code provisions may provide a fix. Lurking in the background of some of these methods is the prospect of an attempt by the Service to apply *Bosch* — although *Bosch* may not be applicable. Each of these potential tools, as well as the *Bosch* issue, is discussed in greater detail below, but ultimately, each is designed to have a court
determine the testator’s intent when it is not clearly expressed in the hiatus death document.

A. Common Law Construction: Resolving Ambiguities

Historically, courts dealing with wills were reluctant to use extrinsic evidence for the fear that it was less reliable than what appeared within the four corners of a valid testamentary document executed with the formalities deemed by the legislature to preserve the best reliable evidence of testamentary intent. However, the reluctance of courts to use extrinsic evidence began to dissipate in more recent decisions, particularly when dealing with latent ambiguities.

1. Guidance from Cases

For example, in *Estate of Fabian*, one daughter among seven siblings gave birth to an illegitimate child in 1942. The daughter’s parents and the four oldest siblings swore to treat the illegitimate child as the legitimate child of the parents. From that time on, the parents treated the illegitimate child as their legitimate son and the seven siblings treated him as their brother. On the deaths of several family members, the obituaries named the illegitimate child as the son of the parents and as the brother of the seven siblings. However, upon the death of another of the siblings in 1994, one of the siblings serving as personal representative refused to treat the illegitimate child as a brother of the testator entitled to take under the testator’s will. The trial judge found the will’s use of the term “brother” to be unambiguous and refused to admit extrinsic evidence showing that the testator considered the illegitimate child to be her brother.

Using extrinsic evidence proving the family’s treatment of the illegitimate child, the appellate court determined that the will’s use of the term “brother” was ambiguous. As the court noted, “[o]rdinarily, brother means male sibling [but] the facts of this case are far from ordinary.” Consequently, the court reversed and remanded with instructions to the trial court to use extrinsic evidence to resolve the latent ambiguity and determine what the testator intended by her use of the term “brother” in her will.

The appellate court adopted the modern, and better, view of the use of extrinsic evidence both to find and to resolve a latent ambiguity.

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29 See, e.g., Garcia v. Celstron, 2 So. 3d 1061 (Fla. App. 2009) (using extrinsic evidence to construe testator’s intent about parameters of given life estate); Matter of Stull Living Trust, 2008 WL 217622 (Cal. App. Jan. 28, 2008) (allowing extrinsic evidence to resolve question of settlor’s intent as to allocation of expenses and fees); Estate of Zahrobsky, 731 N.W.2d 385 (Wis. App. 2007) (allowing extrinsic evidence to define “ap-
in the will. By definition, a latent ambiguity does not appear on the face of the will. Thus, the only way to determine the existence of a latent ambiguity is through the use of extrinsic evidence. Once a court uses extrinsic evidence to find that a latent ambiguity exists, it is not a far stretch to also use extrinsic evidence to resolve the ambiguity. Courts construing wills can use extrinsic evidence to clarify and explain, but should not use extrinsic evidence to vary or contradict. Although the statement of policy seems clear enough, application in a particular fact pattern can be problematic.

Although courts have generally exhibited a greater reluctance to use extrinsic evidence to resolve patent ambiguities, those that appear on the face of the will, that attitude appears to be evolving as well.\footnote{30} The Restatement (Third) of Property: Wills and Other Donative Transfers section 11.2, comment d (2003) ignores the categorical difference: “Once an ambiguity, patent or latent, is established, direct as well as circumstantial evidence of the donor’s intention may be considered in resolving the ambiguity in accordance with the donor’s attention.”

Whether a term in the will referring to the estate tax that does not exist in 2010 presents a patent or latent ambiguity is arguable.\footnote{31} If the

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\footnote{31} For a case distinguishing patent from latent ambiguities, see Berry v. Ford, 829 N.E.2d 1052 (Ind. App. 2005). In Berry, the testator’s 1997 will listed the names of five of his children. It continued on to divide his residuary estate among four of those children, expressly disinheriting the fifth named child although providing that the testator loved the fifth child as much as the others. However, in 1991 the testator had consented to a decree establishing his paternity for a sixth child, not mentioned at all in the will. The sixth child contended that the will contained an ambiguity because it failed to include her in the list of the testator’s children nor did it expressly disinherit her. Finding no ambiguity, the trial court refused to admit extrinsic evidence.

The appellate court reviewed the two types of ambiguities. A patent ambiguity appears from the face of the will, while a latent ambiguity arises through the application of extrinsic evidence, which demonstrates an ambiguity not facially apparent. The appellate court ruled that the testator’s intent about the sixth child was unclear. Consequently, it held that the trial court should have admitted extrinsic evidence to explain the ambiguity and should not have denied the sixth child’s request to construe the will.

However, the appellate court may have jumped the gun with its reasoning. The Berry court appears to have found the existence of a latent ambiguity without the use of extrinsic evidence - a neat trick. The better ruling would have been to send the case back to the trial court to undergo both steps of the latent ambiguity process, using extrinsic
court takes judicial notice that the estate tax does not exist in 2010 and that the terms are estate tax related, then the ambiguity could be patent. Conversely, if the court reads the terms literally, then only extrinsic evidence will demonstrate that a latent ambiguity exists. If the state has enacted a statute expressly allowing the consideration of extrinsic evidence for hiatus deaths, then the distinction will be moot. In states without statutory guidance, the distinction may make a difference, unless the court takes the trending Restatement view that extrinsic evidence is permissible to resolve both types.

In such cases, absent some testimony or other proof about statements by the decedent about dispositions during a hiatus death, the extrinsic evidence will likely focus on relationships, especially in the estate tax cases, between the decedent and the surviving spouse on one hand and the bypass beneficiaries on the other. Based on those relationships, would the decedent want to exclude the spouse or the beneficiaries, or make gifts to both the spouse and the beneficiaries? For those courts that are stricter about the use of extrinsic evidence, a reasonable result seems doubtful. In those cases, if the documents are silent about the possibility of a hiatus death, determining the decedent’s intentions will be difficult if not impossible: the formula language in the documents will make no sense.

Some case precedent may present construction situations analogous to the use of terms that do not have current meaning. For example, in Matter of Stull Living Trust, the settlor, who died in 2004, created an inter vivos trust establishing two subtrusts: a marital deduction trust, which was further divided into a real estate and a residuary share, and a bypass trust. The bypass trust was initially funded with $1.5 million. The marital trust’s initial value was approximately $10 million. The trustee of the marital trust allocated administration expenses and fees to both the marital trust and the bypass trust. Contending that the settlor intended that the marital trust absorb all expenses and fees, the trustee of the bypass trust contested the allocation. The bypass trustee cited the only provision in the trust dealing with expenses or fees: “any attorneys’ fees and other probate expenses and administrative costs . . . shall be charged to the [Bypass] Trust.” The bypass trustee argued that the quoted language demonstrated the settlor’s intent that only expenses and fees related to probate were allocable to the bypass trust. Because evidence to see if a latent ambiguity exists and, if so, to clarify it. According to the testator’s estate, the only extrinsic evidence would explain that the testator meant to disinherit the sixth child.

32 See supra Part II.B.
there was no probate proceeding for the settlor, the bypass trustee claimed that no fees or expenses were related to probate.

The marital trustee responded that the marital trust was “a pecuniary marital trust,” which by definition required the allocation of expenses against the bypass trust. The trial court refused to allow the bypass trustee to introduce testimony, finding that the trust was unambiguous and ruling that the bypass trust should bear the burden of the fees and expenses.

The appellate court reviewed the only authority cited by the trial court for its conclusion, which was an excerpt from the materials of a continuing education presentation. The appellate court found no authority cited by the materials for the proposition that, when a pecuniary marital/residuary credit formula is used, administrative expenses must be allocated to the bypass, or residuary, share. Without any authority, the cited materials provided no legitimate insight into the settlor’s intent. “The intent issue can be resolved only by considering the facts of each case, not by resort to ipse dixit statements in legal publications.”

Instead, the appellate court ruled that extrinsic evidence was necessary to determine the settlor’s intent about allocation of expenses and fees and remanded the case.

In Stull, the reference to probate in the allocation clause created an effective ambiguity because there was no probate. Similarly, terms referencing the estate tax in hiatus death wills create an effective ambiguity because there is no estate tax.

Arguably, any case in which the court was trying to fill in a blank or explain a term that has no current relevant meaning could serve as an analogous precedent to the hiatus death construction cases. Estate of Herceg34 offers an example. In Herceg, the testator’s will included a residuary clause that failed to name any beneficiary. The pre-residuary devises disposed of approximately 90 percent of the testator’s estate, so that the residue governed only about 10 percent of the estate. The personal representative, the widow of the testator’s nephew, proposed that the court fill in the omission by inserting the same pertinent language from the three previous versions of the testator’s will, which left the residue of her estate to her nephew if he survived her and alternatively to the nephew’s widow. The drafting attorney confirmed the personal representative’s position by blaming the omission on computer software.

The Surrogate recognized the extent to which the general reluctance to correct a mistake by filling in the name of an omitted beneficiary would be stretched. The Surrogate cited the generally-accepted rule that prevented the correction of a mistake by supplying missing names.

34 747 N.Y.S.2d 901 (Sur. 2002).
However, the Surrogate also cited the line of cases allowing extrinsic evidence, such as the prior wills and the drafting attorney’s testimony, to clarify an ambiguity. The Surrogate noted that the presumption against intestacy, especially in the case of a residuary devise, buttressed the position for allowing extrinsic evidence to resolve an ambiguity. “On the one hand the court is not supposed to supply what the testator has not, through extrinsic evidence or otherwise. On the other hand, the primary objective is to ascertain the intention of the testator in order to avoid intestacy.”

The Surrogate then considered applicable precedent, stating that the trend seemed to be moving away from the rigid prohibition against the use of extrinsic evidence towards the consideration of all extrinsic evidence to ascertain the testator’s intent. The Surrogate cited Tentative Draft No. 1 of the Restatement of the Law of Property (Donative Transfers) section 12.1, which approves the use of extrinsic evidence to determine intent, but only if the evidence is clear and convincing. The Surrogate also cited precedent allowing extrinsic evidence to supply language missing from a will and to correct mistakenly-named beneficiaries. Although the Surrogate admitted that proposed relief — using extrinsic evidence to supply a missing name — was a significant step beyond those cases, the evidence clearly and convincingly showed the testator’s intent to name the personal representative as the alternate residuary beneficiary.

The failure of formula drafting to clearly state the testator’s intent has arisen in the context of devises described as the most that may pass free of estate taxes. When the formula uses technical language, but is incomplete or inaccurate, problems arise. Some cases have construed ambiguities in wills with formula clauses that referred to the unified credit — the amount that could pass free from estate and gift tax under earlier law — without expressly offsetting the unified credit amount for adjusted taxable gifts. For example, in Matter of the Estate of Fern L. Brown, the testator made a gift to a group of individuals of “... the amount of monies my estate may claim under the Unified Credit of Section 2010 of the Internal Revenue Code.” At the time of her death, the unified credit was $192,800, and the equivalent value was equal to $600,000. The testator devised the residue of her estate to charities.

When consulting with the drafting attorney, the testator did not disclose that she had made substantial taxable gifts. Because the lifetime gifts consumed a portion of her unified credit, the decedent’s estate would be exhausted and nothing would pass to the charities after the specific devises and nonprobate transfers.

35 559 N.W.2d 818 (N.D. 1997).
The individual devisees argued that they should receive up to $600,000 before anything would pass to charity. The charities argued that the decedent expressed an intent to “zero out taxes.”

The trial court determined that the language of the will was ambiguous because both interpretations were reasonable. And although the trial court believed that the decedent intended for the charities to receive something, it ruled for the individuals. It reasoned that, because the will also contained a provision that required estate taxes to be paid from the residue, the testator knew that her estate might not pass free of estate taxes.

The appellate court stated the question as:

. . . whether Brown’s group gift, “the amount of monies my estate may claim under the Unified Credit,” was intended by her to be a maximum-formula gift up to the entire $600,000 exemption-equivalent amount (if the size of her probate estate permitted it), or whether it was intended by Brown to be used with the exempt charitable gifts to save estate taxes.

The difference in the two interpretations lies in the failure to state whether the amount should be adjusted for the decedent’s lifetime gifts. The appellate court held for the charities and chose an interpretation that saved the residuary gift by limiting the gift to the noncharitable beneficiaries to the most that can pass free of estate taxes. It relied heavily on the wording: “the amount of monies my estate may claim under the Unified Credit.” It interpreted this to mean only the amount unused by the decedent during her lifetime. The drafting attorney testified that “the amount of the unified credit her probate estate ‘may claim’ under the Internal Revenue Code is reduced by taxable lifetime and non-probate transfers.” This statement is correct only in a colloquial sense, but not as a technical matter. All estates are entitled to a full unified credit at death — $192,000 in the year of this decedent’s death, which would exempt $600,000 of property from estate taxes, but for purposes of computing the estate taxes, the amount of the decedent’s adjusted taxable gifts is added to the value of the taxable estate. Thus, the net effect is as the court concludes but that may not reflect the literal meaning of the words in the decedent’s will.

The court dismissed the argument about the decedent anticipating estate taxes by providing that any estate taxes should be paid from the residue because it concluded that the decedent’s estate could have owed estate taxes in all events if the prior gifts and non-probate transfers had exceeded the amount that may pass free of estate taxes.36

36 See also Matter of Ettinger, 149 Misc.2d 308, 564 N.Y.S.2d 691 (Sur. 1990), in which the Surrogate considered a will with provisions devising “the ‘largest amount’ enti-
2. Drafting Attorney’s Testimony

If a hiatus death court allows the admission of extrinsic evidence, the drafting attorney’s testimony will often be of primary importance.\(^{37}\) Of course, putting the drafting attorney on the stand may create a Catch-22. If the drafting attorney ascertained the testator’s intent about a possible hiatus death and failed to expressly provide for that possibility, the court should consider that evidence to be important and perhaps dispositive, but the drafting attorney may be held responsible for the costs of the construction action for failing to anticipate Congress’s inaction. If, however, the attorney did not ascertain the client’s intentions in the event of a hiatus death, any extrinsic evidence would simply facilitate the guessing about what the client might have preferred if the issue had been addressed and considered, and the attorney in that case might be liable for failing to address the issue with the client.

B. Possible Precedent from Tax History

In addition to common law construction cases, some tax cases might provide guidance to the hiatus construction problem.

1. Transitional Rule Cases

In construing the intent of hiatus decedents, it may be possible to analogize to the transition to the unlimited marital deduction under the Economic Recovery Tax Act of 1981 (ERTA) section 403(e).\(^{38}\) Prior to ERTA, the marital deduction was limited to the greater of $250,000 or half the estate. ERTA eliminated the cap and permitted for the first time an unlimited estate and gift tax marital deduction.

ERTA contained a transitional rule that construed a formula clause calling for the maximum marital deduction to mean the pre-1981 limited marital deduction unless the testator amended the will post-ERTA or a state enacted a statute construing such clauses as providing the liberalized marital deduction gift and estate tax deduction. The purpose of the transitional rule was ostensibly to protect the testator’s intent and the interests of non-spousal beneficiaries, although one might conjecture that a hidden agenda was to increase estate tax collections.\(^{39}\)

\(^{37}\) See infra Part III.A.2.


\(^{39}\) See Estate of Bruning v. Commissioner, 888 F.2d 657 (10th Cir. 1989), aff’g T.C. Memo. 1988-5. For some other transitional rule cases opining that the rule’s purpose was to preserve intent, see Estate of Pouser, 975 P.2d 704 (Ariz. 1999), and Liberty Nat. Bank
Unlike the 2010 hiatus, however, Congress thought about the impact of the transition to the unlimited marital deduction as evidenced by its transitional rule. Of course, no such transitional rule exists for the 2010 hiatus. Analogies to what Congress may have intended by not providing a transitional hiatus rule with its provision of the transitional rule in ERTA seem speculative at best. Unlike the transitional rule cases, inferring that Congress’ inaction was intended to preserve a testator’s intent will be problematic.

However, some cases dealing with the transitional rule may be instructive for a methodology in construing hiatus documents. For example, in Estate of Klein v. Commissioner,40 the court refused to be bound strictly by the terms of the transitional rule and instead looked to the testator’s intent as evidenced by the entire document.41

While the transitional rule experience consequently may not provide airtight analogies for hiatus constructions, the methods of determining the testator’s intent in some transitional rule cases may be helpful as arguable precedent.

2. Tax Apportionment Cases

Will and trust construction problems to determine a testator’s or grantor’s intent regarding tax-related terms arise commonly in tax apportionment cases. State law, such as the Uniform Estate Tax Apportionment Act,42 and sections 2205 to 2207B of the Internal Revenue Code provide rules to apportion estate taxes against those with a financial interest in an estate, but all of these statutes permit a decedent to provide otherwise. Because the amount of estate taxes can be quite large for a large estate, the impact on a beneficiary of having to pay or not pay can be significant. When the testator’s or grantor’s intent is not clear regarding application of the statutory provisions, controversies arise. The allocation of estate taxes can make a substantial difference in the dispositive plan of the decedent.

Cases of this type deal with language of documents that did not “make sense” when the impact of taxes was considered. The 2010 hiatus presents the problem of construing documents with tax terms do not make sense. Fundamentally, in each instance, the court must decide what the decedent likely meant in circumstances that it is not at all clear...
that the decedent actually knew the meaning of the words used or the need to use additional words to give a desired result. Tax apportionment construction cases abound, but a few examples should be instructive.

In *Estate of Miller*\(^4\), the decedent was the beneficiary of a testamentary QTIP trust established by her predeceased spouse. The trust provided the decedent with an income interest for life and upon her death funded a family trust. The personal representative of the spouse's estate made a QTIP election for the trust.

After her husband died, the decedent executed a will that provided, “I direct my Personal Representative . . . to pay all my legal debts . . . and without reimbursement or contribution, all estate taxes . . . assessed by reason of my death . . . .” The decedent subsequently executed two codicils, but neither altered the tax clause.

Computed at the marginal rate, the taxes attributable to the inclusion of the QTIP trust in the decedent’s estate exceeded $400,000. The personal representative of the decedent’s estate demanded that the QTIP trustees pay the additional taxes. When the trustees refused, the personal representative brought an action to interpret the will’s tax clause to determine if it exonerated the QTIP trust from tax apportionment.

Without recovery from the QTIP trust of some portion of the taxes, the decedent’s estate did not have sufficient assets to pay “various specific bequests” set out in the decedent’s will. (The opinion did not identify the specific and residuary beneficiaries.) The personal representative based the claim for contribution on Code section 2207A, which provides that a QTIP trust is responsible for payment of estate taxes in the surviving spouse’s estate, computed at the marginal rate, unless the decedent “otherwise directs by will.” No state law was cited in support of the estate’s claim.

The trial court ruled that the will directed that the QTIP trust and the decedent’s estate share the taxes. Moreover, it held that the decedent did not waive her estate’s right to reimbursement. The trial court’s order effectively required the QTIP trust to pay all estate taxes attributable to it. The trustees appealed.

The trial court based the ruling on its interpretation of the decedent’s intent. Generally, “a court must ascertain this intention from the terms of the will itself.” The trial court, however, considered “extrinsic evidence on the grounds that [the decedent’s] will was latently ambiguous.”

The appellate court rejected the use of extrinsic evidence because it found that the decedent’s will was not ambiguous. According to the appellate court, a latent ambiguity exists when the will is clear on its face but the decedent does not own the property given or the property or its recipient is mis-described. Because neither of these situations applied, extrinsic evidence was not admissible. The court determined that although the decedent was aware of the QTIP trust and the related taxes, she “still intended this tax-exoneration provision” in her will. It concluded that “[j]ust because a testator’s plan does not work out how she envisioned . . . does not mean that the plan itself was not intended.”

The court also rejected the estate’s argument that the QTIP trust was not exonerated from the application of section 2207A because the decedent did not specifically refer to that section’s right to reimbursement. The court found that section 2207A does not require the decedent to make a specific reference to it, even though section 2207B does require a specific reference for exoneration. 44 The court reasoned that Congress knew how to require specific reference to a section to negate exoneration, but chose not to in section 2207A.

The result in Miller should be compared with Will of Gordon, 45 in which the New York Surrogate’s Court determined that a decedent’s will did not override Code section 2207A and a similar New York statute. As a consequence, the assets of a QTIP trust were not exonerated from payment of estate taxes. The decedent’s husband died, leaving $1,800,000 in a trust for which an 80 percent QTIP election was made. After the decedent’s death, the QTIP trust was divided among her deceased husband’s sisters. The decedent left her estate to Albert Einstein College of Medicine in New York City. Her will, executed after her husband’s death, provided:

I direct that all Estate inheritance and death taxes (including any interest and penalties) imposed by any jurisdiction by reason of my death with respect to any property includable in my estate for the purpose of such taxes, whether such property passes under or outside my will be paid out of my Residuary Estate as a administration expense, without apportionment.

The decedent died before the QTIP election was made for her husband’s estate.

Concluding that the decedent had to make a specific reference to the QTIP property to exonerate the QTIP trust from tax apportionment, the court held that “it is not conceivable that she would exonerate

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44 Section 2207A was amended in The Taxpayer Relief Act of 1997, Pub. L. 105-34, to require specific reference to section 2207A for section not to apply.

the trust from contributing its share of estate taxes recognizing that by doing so she would totally wipe out her residuary gift to charity.”

Another New York court reached an opposite conclusion on somewhat similar facts. In In re Bruce, another New York court reached an opposite conclusion on somewhat similar facts. In In re Bruce,46 the decedent’s will provided in part: “All estate taxes payable by reason of my death shall be chargeable against and payable out of my residuary estate without contribution by anyone.” The decedent’s executors sought to have recipients of nonprobate assets (life insurance and joint accounts) contribute to the payment of the estate taxes imposed. The attorney who drafted the decedent’s will testified that he was unaware of the nonprobate assets when he drafted the will and that the purpose of the provision was to exonerate a specific bequest made in the will. Nevertheless, the trial court and the appellate court determined that the decedent’s intent was clear and that no taxes were apportionable against the nonprobate assets.

In Estate of Tovrea v. Nolan,47 the decedent was the life beneficiary of a $4 million QTIP trust. Upon her death, the trust was payable to her stepchildren — children of the decedent’s predeceased husband. Before she died, the decedent named her daughter as the beneficiary of a $2.7 million insurance policy. The decedent’s taxable estate, which totaled almost $9 million, was composed of the QTIP trust, the insurance policy, and approximately $2.1 million of probate assets.

The decedent’s will directed that her estate taxes be paid from her residuary estate, except for the taxes associated with the QTIP trust. Because of the large life insurance policy, the decedent’s probate estate was insufficient to pay all taxes and was unable to pay creditors or to pay specific gifts under the will.

In an action to force the personal representatives of the decedent’s estate to seek reimbursement for a pro rata share of estate taxes from the beneficiary of the insurance policy, the issue was whether the decedent’s will overrode IRC section 2206, which provides that taxes are apportioned against the recipient of life insurance proceeds unless the decedent directs otherwise.

Two prior Arizona decisions involving similar facts considered the question, although in each of those cases the wills specifically exonerated nonprobate assets from taxes, whereas the decedent’s will gave a general direction to pay all taxes from the residue except those associated with the QTIP trust.

The proponents of apportioning taxes asserted that the decedent’s direction was not sufficiently specific to override the tax apportionment statute. The appellate court disagreed. It determined that the dece-

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dent’s use of the word “all” meant all taxes including taxes on the nonprobate life insurance. In addition, the court concluded that the decedent was aware of taxes on nonprobate assets such as the QTIP trust and understood how to separate taxes on nonprobate assets from her general direction to pay her estate taxes from the residuary estate.

In Maurice F. Jones Trust v. Barnett Banks, the decedent’s second husband, a resident of Indiana, predeceased her. Before his death, the decedent’s second husband created an inter vivos trust that provided the decedent with a life income starting at the husband’s death. Upon the decedent’s death, the trust terminated and distributed to the husband’s relatives and charitable organizations. The personal representative of the husband’s estate elected to QTIP a portion of the trust for the federal estate tax marital deduction.

Several years after the husband’s death, the decedent executed a will that benefitted her daughter (who was not the child of her predeceased second husband). Her will provided also that

all estate... taxes... which may be levied or assessed by reason of my death... shall be considered a cost of administration of my estate, and that such taxes, together with all debts which I am legally obligated to pay at the time of my death... shall be paid out of my residuary estate without apportionment.

After the decedent’s death in Florida, the personal representative of her estate sought reimbursement for the estate taxes attributable to the QTIP being included in the decedent’s estate. The trustee of the QTIP trust countered by bringing a declaratory action in Indiana to determine if the QTIP trust was subject to tax apportionment under Code section 2207A.

The trustee of the QTIP trust asserted that a “plain reading” of the decedent’s will exonerated the QTIP trust from estate tax apportionment. The personal representative of the decedent’s estate responded that the phrase “which I am legally obligated to pay at the time of my death” created an ambiguity as to whether the decedent intended to exonerate the QTIP trust from tax apportionment and, as a result, extrinsic evidence was admissible to establish that she did not.

The Indiana court determined that Florida law controlled the admissibility of extrinsic evidence because the decedent died in Florida and her will was written, executed, and probated in Florida. Under Florida law, extrinsic evidence is admissible if an ambiguity exists and is either latent or patent. The court then determined that the quoted phrase created an ambiguity that needed clarification, and it conse-

quently accepted various affidavits that resolved the ambiguity in favor of non-exoneration.

In Estate of Patouillet, the decedent’s will, executed in 1984, directed that all of his estate taxes were to be paid out of his residuary estate, including taxes associated with nonprobate assets. A trust created by the decedent in 1991 provided that the trust was to pay over to the executrix of the decedent’s estate “such sums as such representative shall state [in writing] to be necessary for the payment of the expenses of . . . federal estate taxes.” The provision provided further for the payment of state transfer taxes. The executrix of the decedent’s estate followed the instructions of the decedent’s trust and made a written request for payment of the decedent’s estate taxes.

The trustee of the trust petitioned the court to determine whether the provisions of the decedent’s will relieved the trust of paying any of the decedent’s estate taxes, unless the decedent’s residuary estate was exhausted. The personal representative countered that the trust controls, so that the decedent’s estate taxes were payable from the trust.

New York statutory law states that a nontestamentary document providing for the payment of taxes controls tax apportionment, if it is dated later than the decedent’s will and it refers to the tax apportionment provision of the earlier document. The trustee asserted that the statute was not satisfied because the trust did not refer to the previously executed will. The court held that the trust needed to refer only to the obligation to pay taxes. Because the trust was obligated to pay such amounts as the executrix requested, the reference required by the statute was satisfied. It was not necessary to refer to the will specifically or to its date of execution.

Ultimately, the court sought to determine the decedent’s intent. The decedent’s will left the bulk of his estate to his sisters, evidencing an intent to provide for his sisters. The trust benefitted the decedent during his lifetime and at his death paid over to non-relatives. The trustee’s interpretation would cause the decedent’s estate to be exhausted, leaving nothing for his sisters. Thus, the trustee’s interpretation would make meaningless the decedent’s will. The court refused to accept that the decedent intended to revoke the gifts to the sisters by “employing the circuitous, convoluted method proposed by” the trustee.

Even in states that have statutes similar to New York, courts have been less reluctant to permit a trust to provide an alternative to tax apportionment. In Estate of Roe, the decedent’s will left her entire estate


to an inter vivos trust created the same day as her will. The will made no provision for payment of estate taxes. The trust provided that the trustee was to pay all taxes without apportionment. It then made several specific gifts and directed the division of the remainder of the trust corpus. Notwithstanding the direction in the trust instrument against estate tax apportionment, the Michigan Court of Appeals held that only the decedent’s will may override the Michigan version of the Uniform Estate Tax Apportionment Act. Thus, the estate taxes were apportioned against all of the trust beneficiaries. One appellant argued that the tax should be apportioned against the trustee rather than the beneficiaries because the trustee was the person interested in the estate and the division of the trust assets was based on the contract (the trust agreement). The court declined to consider the argument.

3. State Death Tax Cases

Another line of cases that can be analogized to the hiatus death construction cases arises from the systematic elimination of the federal estate tax state death tax credit by EGGTRA beginning in 2002. A number of cases have examined the intent of the state legislature responding to the phase-out of the state death tax credit. Commonly, former “sponge tax states” enacted a new state estate tax that recognized the expiring state death tax credit. As the credit expired, however, courts have been required to construe the language of the applicable state statutes, attempting to determine legislative intent in much the same way they will have to determine the intent of a testator dying during the hiatus.

Many of these controversies involve disputes with state tax authorities concerning the amount of state death taxes that must be paid. Demonstrative of this process of judicial reasoning is *Brooker v. Madigan*,51 which also provides a concise history of the phase-out. In *Brooker*, the decedent’s estate was valued at more than $68 million. The decedent’s parents predeceased her in rapid succession. Consequently, the section 2013 previously taxed property (PTP) credit exceeded $9.2 million, and the estate did not need to claim the state death tax credit to avoid paying federal tax. In 2003, the state death tax credit would have been approximately $1.7 million. The state treasurer claimed that the estate owed more than $3.5 million in state estate taxes, based on the state’s conversion from a pick-up tax state in light of the phase-out of the federal death tax credit, plus interest and penalties. The estate argued that, because the estate did not claim a state death tax credit on the federal return, no state estate tax was due.

The majority first recounted the history of the state estate tax. Prior to EGTRRA, the federal estate tax granted a tax credit for state death taxes paid. Thus, Illinois followed the general state approach and imposed a state estate tax that equaled the amount of the federal state death tax credit. Consequently, the estate did not have to pay additional tax to the state because of the concomitant credit on the federal side. The effect of the state death tax credit and the imposition of the state pick-up tax was to charge no more overall tax to the estate but to transfer tax dollars from the federal to the state side.

However, EGTRRA phased out the state death tax credit. The section 2011 credit was reduced by 25 percent in 2002, then 50 percent in 2003, and 75 percent in 2004, with complete elimination in 2005. As the majority described it, the federal government “was turning the table on the states” by keeping its own tax dollars. As was typical, Illinois responded by amending its state estate tax laws, which have been depicted as “likely the most complex decoupling law enacted among the states.” The effect of the amendment was to impose a state estate tax based on what the state death tax credit would have been in 2001.

The estate cited the state statute’s use of the term “allowed” instead of “allowable.” Arguing that as tax terms of art these words had different meanings, the estate asserted that the state death tax credit was not “allowed” because the estate did not take it, resulting from the benefit of the PTP credit.

The majority determined that the legislative intent was to impose a state estate tax and did not mean to differentiate between the terms “allowable” and “allowed.” Thus, by reading “allowed” to mean the same as “allowable,” the majority concluded that the state estate tax was payable despite the estate’s failure to actually claim the state death tax credit.

The dissent chided the majority for finding that the statute was unambiguous — and thus subject to the plain meaning rule — while ignoring the plain meaning of the word “allowed” and substituting the word “allowable.” The dissent noted that those two terms do have different tax meanings, which the majority disregarded. Importantly, the dissent observed that the majority did not need to subvert the legislature’s meaning in this case to protect the state’s stream of revenue because, in most cases, the estate would take the federal estate state death tax credit. Only in rare cases, such as this one when the state death tax credit would not reduce the federal tax, would the estate escape paying the state estate tax.

State death tax cases can involve more than just a dispute with state taxing authorities but instead a dispute among beneficiaries. An even more direct example of the analogy between state law changes resulting
from the state death tax credit and the reasoning process available to 
hiatus death construction courts is demonstrated by Estate of Zahrobsky. In Zahrobsky, the testator devised the excess of her estate “over 
the applicable estate exemption” to a local scholarship fund. At the 
time her will was executed in 2000, Wisconsin was a sponge tax state 
and did not have a separate state estate tax. Thus, at the time of execution, 
the only applicable estate tax exemption was the federal exemption of 
$675,000. Between the time of execution and the date of death, Wiscon-
sin enacted a state estate tax. At the time of the testator’s death, the 
state exemption was $675,000 and the federal exemption was $1.5 mil-
ion. Her estate was valued at approximately $1 million. The testator’s 
nephew, apparently a devisee of the exempt portion, argued that the will 
referred only to the federal exemption and that, consequently, the local 
scholarship fund received nothing. The scholarship fund countered that 
the testator must have meant to refer to the state exemption because 
she “obviously intended to make a donation . . .”

The court determined that the term “applicable estate exemption” 
was ambiguous, so it allowed the introduction of extrinsic evidence for 
clarification. The will drafter, a nonlawyer accountant, testified that he 
advised the testator that she could avoid taxes by giving the excess of 
her estate over the exemption amount to charity. He claimed that, al-
though there was no state estate tax at that time, “he knew the state 
could impose a tax in the future.” Thus, he drafted the will so that any 
assets in excess of the state exemption amount would pass to the schol-
arship fund charity.

The nephew introduced the testimony of an estate planning attor-
ney, who insisted that the testator could not possibly have referred to 
the state exemption amount because “in 2000, even the idea of a Wis-
cconsin estate tax ‘wouldn’t have been in anybody’s vocabulary.”

The court ruled that the testator meant to refer only to the federal 
exemption amount, so that there was no excess for the scholarship fund 
to receive.

The court recognized that the result of the case depended on whose 
testimony to believe: the accountant will drafter or the estate planning 
attorney offering expert testimony. Usually, the testimony of a drafter 
is an important factor, if not the most important factor, in determining 
the testator’s intent.

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52 731 N.W.2d 385 (Wis. Ct. App. 2007).
53 Left unsaid by the court was why it chose to disregard the testimony of the will 
drafter and instead believe an expert witness estate planning attorney who had not com-
municated with the testator. One cannot help but imagine the court’s weighing of the 
testimony was substantially based on the notion that an accountant should not have been 
preparing the will to begin with. See supra Part III.A.2.
The opposite conclusion might be reached by applying the presumptions that a testator's will speaks at death and that consequently the testator is presumed to know the facts and the law that apply at death. In that event, the testator would have been presumed to know the applicable state exemption amount, although that still would leave unresolved the issue of which amount she intended to apply.

C. Doctrine of Probable Intent

Perhaps the most appropriate theory for dealing with hiatus construction cases is the doctrine of probable intent, which uses “common human impulses” in construing a will by filling in gaps in the dispositive plan. New Jersey pioneered the doctrine of probable intent, as demonstrated by the decision in Estate of Payne. In Estate of Payne, the testator and his former same-sex partner bought a house in Maine, titled as joint tenants with right of survivorship. The testator subsequently entered into another relationship with a same-sex partner. Both suffered from AIDS. They resided together in the testator's New Jersey home. In 1998, the testator executed a will, directing sufficient assets to the pay-off of the mortgages on the Maine property, as the co-owners had agreed. The 1998 will made no provision for the testator's current partner. On several later occasions, according to the partner, the testator promised to leave the New Jersey home to him, free from debts and liens. Eventually, the testator contacted his attorney to change his will. In 2000, the attorney sent a draft of a new will, with the only significant change being a devise of the testator's personal property to the current partner, but the testator did not execute the new will. Instead, he wrote the attorney to tell him that he intended to give not only the personal property but also the home to his partner. During this time, the testator's health deteriorated; he had to leave his job, and his partner began taking care of his personal needs.

The attorney sent a revised draft to the testator. The testator again wrote the attorney to express some concerns about the draft. He wanted his partner described as a partner rather than as a friend. He stated his intention that his real estate pass to his beneficiaries “free and clear” because he did not want the “properties” to be sold to pay off the mortgages. Believing that the testator’s letter referred only to the Maine property, the attorney prepared yet another draft, with the only significant difference being the change in terminology from friend to.

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54 See, e.g., Schilling v. Schilling, 2010 WL 2306509 (Va. June 19, 2010); In re Estate of McFarland, 167 S.W.3d 299 (Tenn. 2005); In re Medeiros Testamentary Trust and Life Ins. Trust, 96 P.3d 1098 (Haw. 2004) (“A will speaks from the time of testator’s death, and that which is spoken is subject to the laws in force at that time.”).
partner. On the day before the attorney had arranged to have the testator execute the will, the testator was hospitalized. The attorney visited the testator in the intensive care unit, where he executed the new will. Although the new will did not make specific reference to the pay-off of any mortgage on the New Jersey home, it did contain a general “pay all just debts” clause. The testator fell into a coma the next day and did not return to consciousness before his death.

The partner claimed that the testator intended for the mortgages on the New Jersey home to be paid off from the estate, so that he would receive that property free from any debts or liens. The estate contended that the will contained no such provision and thus that the partner took the home subject to the mortgages.

The trial court ruled in favor of the estate. It was unimpressed by the partner’s contention that the “pay all just debts clause” expressed the testator’s intention to pay off the New Jersey mortgages. The trial court reasoned that, if the testator thought that the just debts clause sufficed to require pay-off of the mortgages, then he would not have needed to include specific language in the will requiring the payment of the Maine mortgages. The trial court supported its conclusion by noting that testimony indicated that the testator was “detail-oriented.”

The appellate court reversed. It concluded that the doctrine of probable intent, which considers common human impulses in construing a will to fill in dispositive gaps, required a finding in favor of the partner. The appellate court considered the partner’s argument that “common human impulses” would lead a testator to leave a debt-free home to a surviving spouse — which the partner argued he was in effect. Although the appellate court may well have reached the proper result based purely on a look to the testator’s intent, especially in light of the last letter to the attorney indicating the desire to devise all the properties “free and clear,” the doctrine of probable intent is often counterintuitive to the policies supporting the strict construction of wills.\footnote{At least one even more esoteric doctrine to construe a will has been advanced. See Estate of Klauzer, 604 N.W.2d 474 (S.D. 2000) (personal representative offered the doctrine of “grammatical geometrics” to determine the testator’s intent).}

Hiatus formula divisions issues fall within the dispositive gap genre, so probable intent could be an operative construction tool. However, this doctrine has so far seen limited application. Nevertheless, the concept behind the use of the doctrine of probable intent is consistent with that underlying the use of dependent relative revocation.\footnote{See supra text accompanying notes 15–17.}

Determining the probable intent of a decedent in hiatus construction cases may be quite difficult. Most decedents will not actually have considered the proper distribution of their estates when there is no es-
state tax. Clients who actually considered this issue usually agreed to include in the instrument some specific provisions applicable only in 2010. By way of example, the Florida statute does not apply when the governing instrument expresses a clear intention for the disposition of the assets in years in which there is no estate tax. Therefore, the courts will have to determine what the decedent’s intent would have been had he or she actually considered this issue. This is far different from determining the actual intent that is expressed in a governing instrument.

D. Family Settlements

One way to avoid the risks of an unwelcome court determination is to reach a family settlement agreement. These agreements are widely accepted. Moreover, courts are typically allowed, but not required, to accept the terms of a family settlement agreement.

The Uniform Probate Code recognizes the ability of parties to enter into family settlement agreements and of courts to approve them.

UPC section 3-912 allows parties to enter into a binding private settlement without court approval:

Subject to the rights of creditors and taxing authorities, competent successors may agree among themselves to alter the interests, shares, or amounts to which they are entitled under the will of the decedent, or under the laws of intestacy, in any way that they provide in a written contract executed by all who are affected by its provisions. The personal representative shall abide by the terms of the agreement subject to his obligation to administer the estate for the benefit of creditors, to pay all taxes and costs of administration, and to carry out the responsibilities of his office for the benefit of any successors of the decedent who are not parties. Personal representatives of decedents’ estates are not required to see to the performance of trusts if the trustee thereof is another person who is willing to accept the trust. Accordingly, trustees of a testamentary trust are successors for the purposes of this section. Nothing herein relieves trustees of any duties owed to beneficiaries of trusts.

UPC sections 3-1101 and 3-1102 provide a process for court approval. Section 3-1101 provides that

58 See supra Part II.B.
59 See UNIF. PROBATE CODE § 3-912 (amended 1993).
60 See id. §§ 3-1101, 3-1102.
A compromise of any controversy as to admission to probate of any instrument offered for formal probate as the will of a decedent, the construction, validity, or effect of any governing instrument, the rights or interests in the estate of the decedent, of any successor, or the administration of the estate, if approved in a formal proceeding in the Court for that purpose, is binding on all the parties thereto including those unborn, unascertained or who could not be located. An approved compromise is binding even though it may affect a trust or an inalienable interest. A compromise does not impair the rights of creditors or of taxing authorities who are not parties to it.

Section 3-1102 governs the court’s authority to approve if requested:

The procedure for securing Court approval of a compromise is as follows:

(1) The terms of the compromise shall be set forth in an agreement in writing which shall be executed by all competent persons and parents acting for any minor child having beneficial interests or having claims which will or may be affected by the compromise. Execution is not required by any person whose identity cannot be ascertained or whose whereabouts is unknown and cannot reasonably be ascertained.

(2) Any interested person, including the personal representative, if any, or a trustee, then may submit the agreement to the Court for its approval and for execution by the personal representative, the trustee of every affected testamentary trust, and other fiduciaries and representatives.

(3) After notice to all interested persons or their representatives, including the personal representative of any estate and all affected trustees of trusts, the Court, if it finds that the contest or controversy is in good faith and that the effect of the agreement upon the interests of persons represented by fiduciaries or other representatives is just and reasonable, shall make an order approving the agreement and directing all fiduciaries subject to its jurisdiction to execute the agreement. Minor children represented only by their parents may be bound only if their parents join with other competent persons in execution of the compromise. Upon the making of the order and the execution of the agreement, all further disposition of the estate is in accordance with the terms of the agreement.
Hopefully, courts, which usually favor family settlements, will recognize the special exigency of clarification during the hiatus. Family settlement agreements, however, have possible Bosch risks.

E. Contracts Concerning Succession and Related Remedies

Presumably, many of the ambiguous hiatus death wills and trusts will be part of a mutual and reciprocal estate plan between husband and wife. In those cases, the will or trust of the surviving spouse will have provisions, and tax-based terms, similar to the deceased spouse’s documents. One way that a court could consider extrinsic evidence to determine the deceased spouse’s intent would be through the theory of a contract concerning succession. The law generally allows a husband and wife to enter into a contract concerning succession, including contracts to make a will, not to revoke a will, to die intestate, or to not die intestate. Depending on the result that might arise if a court did not use extrinsic evidence to resolve the problems caused by the use of estate tax related terms by the deceased spouse, the surviving spouse may have an argument that the deceased spouse breached the contract to make a will or not to revoke a will, or even not to die intestate if an intestacy would result without the aid of extrinsic evidence.

Contracts concerning succession are often determined and construed through the use of extrinsic evidence. For example, Uniform Probate Code section 2-514 provides:

A contract to make a will or devise, or not to revoke a will or devise, or to die intestate, if executed after the effective date of this Article, may be established only by (i) provisions of a will stating material provisions of the contract, (ii) an express reference in a will to a contract and extrinsic evidence proving the terms of the contract, or (iii) a writing signed by the decedent evidencing the contract. The execution of a joint will or mutual wills does not create a presumption of a contract not to revoke the will or wills.

The UPC allows extrinsic evidence to establish the contract, although the evidence must be written, unless the will expressly refers to the contract. If the surviving spouse of the hiatus death deceased spouse contends that the deceased spouse somehow violated a contract concerning succession, the court should consider extrinsic evidence and, even in states without a statute expressly allowing the use of extrinsic evidence for hiatus wills, the courts would arguably be less reluctant to continue

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62 See infra Part III.G.
the use of extrinsic evidence to determine the deceased spouse’s intent as part of a broader determination of the contract issue.

Even if the surviving spouse would be unsuccessful in arguing the existence of a contract concerning succession because of a lack of written evidence, the argument about the deceased spouse’s obligation might be raised under a couple of other theories.

One of these theories involves the assertion of a fiduciary duty owed by the deceased spouse. For example, in Matter of O’Rourke, the 1970 will of the decedent’s husband created a trust for the decedent. The terms of the trust included a testamentary general power of appointment to qualify the trust for the federal estate tax marital deduction. In default of the exercise of the power of appointment, the marital trust assets passed to descendents of the decedent’s husband.

The decedent died in California in 1993. Her will exercised the power of appointment in favor of her children from a prior marriage. The son of the decedent’s husband sued in New York to impose a constructive trust over the assets of the marital trust. The son alleged that, before the husband signed his will, the decedent and her husband entered into an oral agreement that she would not exercise the power of appointment.

The court reviewed the grounds for the imposition of a constructive trust: “(1) a confidential or fiduciary relationship, (2) a promise, (3) a transfer in reliance thereon, and (4) unjust enrichment.” Applying this criteria to the facts, the appellate court sustained the trial court’s imposition of a constructive trust. The decedent and her husband had an understanding before he executed his will that she would not exercise the power of appointment, and the decedent’s husband relied on the understanding. The decedent violated the agreement, and her children were unjustly enriched at the expense of the descendents of the decedent’s husband.

The court’s decision is similar to Chapman v. Citizens and Southern National Bank. In Chapman the decedent held at the time of her death a testamentary general power of appointment over a testamentary trust created by her husband. The testamentary trust provided that, in default of the exercise of the power of appointment, the trust assets passed to the husband’s children. The decedent’s will, however, exercised the power and appointed the property to her children. There were numerous letters in the record establishing that the decedent promised

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64 Prior to 1981, to qualify for the marital deduction, the deceased spouse had to transfer at least a life estate plus a general testamentary power of appointment to the surviving spouse.
her husband that she would not exercise the power. Because a confidential relationship existed and the decedent broke her promise, the court imposed a constructive trust in favor of the children of the decedent’s husband.

Because the decedent did not change her mind about following her husband’s wishes until after he died, the Chapman court rejected the argument made by the decedent’s children that not permitting the decedent to exercise the power of appointment was “tax fraud.” The O’Rourke opinion did not discuss the tax issue, although it was clearly present. For the decedent’s issue, having the court rule that the decedent did not have the power of appointment should preclude an estate tax inclusion for the value of the marital trust. The existence of the power of appointment is a state law question. This situation is different from Estate of Alperstein v. Commissioner,66 in which the issue was not whether there was a valid power of appointment, but whether it was taxable because the powerholder was never mentally competent to exercise it.67

The other theory involves promissory estoppel. The reliance on this theory is demonstrated by Satcher v. Satcher.68 In Satcher, the testator enticed one of his grandsons to leave his job and help him work his farm. The grandson moved into the testator’s house and borrowed money to purchase equipment and to provide operating capital for the farm. The grandson farmed the land continuously. The testator died in 1998, leaving a will that devised the house and much of the farm to the grandson’s uncle, who tried to evict the grandson from the property. The grandson contended that the testator had promised the farm and

67 The tax consequences to the estate of the decedent’s husband are less clear. Assuming the estate of the decedent’s husband claimed a marital deduction, no estate taxes will ever be paid on the property contained in the trust. The inclusion of the marital trust in the decedent’s estate is based on the decedent possessing a general power of appointment taxable under Code section 2041—a result the Service will not like and one that is inconsistent with the public policy of the marital deduction. Nevertheless, the Service’s remedies seem limited. The normal statute of limitations has expired. Only if the Service asserts and proves fraud will the limitations problem be side-stepped. Alternatively, if the personal representative of the estate of the husband is still alive, the Service might attempt to pursue the personal representative, if it can be established that the personal representative was aware of the agreement between the decedent and her husband not to exercise the power of appointment. The tax problem presented in O’Rourke and Chapman does not arise when the marital trust is a QTIP trust. If a valid election is made on the first spouse’s estate tax return, there is an inclusion in the second estate. The inclusion is not based on a state law right.
the house to him, and sought title under the theories of oral gift, oral contract to make a will, and promissory estoppel.

The court observed that, under any of those theories, the grandson could avoid the Statute of Frauds only by clear, cogent, and convincing evidence, which the court described as more than a preponderance of the evidence but less than the standard for reasonable doubt. The court listed the elements of promissory estoppel as: (1) a clear promise; (2) reasonable reliance by the grandson; (3) reasonable foreseeability on the promise by the testator; and (4) injury suffered by the grandson.

Several witnesses testified that the testator promised the house to his grandson. Thus, the court found clear and convincing evidence of the promise. The court also found that the grandson relied on the promise by leaving his job, moving to the house, and beginning to work the farm — expending an “extreme amount of time and energy.” Moreover, the court determined that such reliance was foreseeable by the testator. By failing to receive the house, the grandson suffered injury. Consequently, the court held that the grandson was entitled to the house under the theory of promissory estoppel. However, the court ruled that the grandson failed to provide clear and convincing evidence that the testator unambiguously promised the farmland to him, mainly because no witness was able to specify an amount of acreage or otherwise particularly describe what land was promised, and rejected the grandson’s claim to the farmland.

The court refused to award the farm to the grandson under the theory of an oral gift. It stated that, to avoid the Statute of Frauds, the grandson either had to take possession of the land and perfect title by adverse possession or prove partial performance. According to the court, the grandson failed to prove by clear and convincing evidence that he made sufficient improvements to the farm to satisfy the second Statute of Frauds exception. In addition, the court held that the grandson failed to prove that the testator delivered possession of the property. Also, the grandson expressed shock that the testator failed to devise the farm to him, which the court concluded conflicted with his argument of an outright inter vivos gift.

Apparently, the grandson asserted the theory of an oral contract to make a will only as to the house because the court stated that, having ruled in his favor on the promissory estoppel argument, it did not need to address the contract to make a will argument. The applicable state statute, based on Uniform Probate Code section 2-514, allowed oral proof of a contract to will if the contract was entered into before the effective date of the probate code.

Consequently, if the surviving spouse asserts a contract concerning succession, a constructive trust, or promissory estoppel, a court may be
inclined to delve into the use of extrinsic evidence and ultimately determine the meaning of the tax terms.

F. Modification and Reformation of Trusts

In those situations when the tax-based terms are contained in a trust created by the hiatus decedent, a trustee or beneficiary could rely on a court’s authority, either at common law or by statute, to modify or reform the trust.

A reformation reforms the language of the trust to reflect the settlor’s true intent that for some reason was not accurately portrayed in the language of the trust document. With reformation, the court amends the language of the trust but not the settlor’s actual intent. Another method of amending a trust involves seeking a court-approved modification. In that case, the court is asked to change not only the language of the trust but also the settlor’s intent.

Although a state’s common law may allow reformation and modification, the Uniform Trust Code codifies a number of principles distilled from case law and adds some innovations.

The UTC recognizes the typical methods of modifying an otherwise irrevocable or unamendable trust, either by the consent of the settlor and all the beneficiaries or by the consent of all the beneficiaries when all the trust’s material purposes have been accomplished. Moreover, the UTC specifies that, for purposes of the latter method, a spendthrift provision is not in itself considered to be a material purpose. UTC section 411, however, allows a court to modify a trust even when all the beneficiaries have not consented, if the court determines that the trust could have been modified if all the beneficiaries had consented and that the interests of the non-consenting beneficiaries will be protected.

UTC section 412 codifies the common law concept that the administrative provisions of a trust may be modified by a court because of a change in circumstances. However, that section takes a rather dramatic step by also authorizing the modification of the dispositive provisions of a trust for the same reason, even if the consent of all the beneficiaries has not been obtained. The comment offers the example of increasing the support distributions for a beneficiary who suffers a serious illness or debilitating accident. Any modification under section 412 must be made with court approval. The comment also notes a difference with Restatement (Third) of Trusts section 66(1) in that the UTC does not expressly impose a duty upon a trustee who is aware of an actionable change of circumstances to petition the court.
Section 416 of the UTC codifies the approach taken by Massachusetts courts in allowing the reformation of a trust to accomplish the settlor’s tax objectives.\(^6\)

Perhaps the most useful of the UTC’s tools is found in section 415, which authorizes the reformation of a trust’s terms “even if unambiguous, to conform the terms to the settlor’s intention if it is proved by clear and convincing evidence that both the settlor’s intent and the terms of the trust were affected by a mistake of fact or law, whether in expression or inducement.”

One recent UTC-based case, the first reported from a UTC state, demonstrates how the UTC can facilitate reformation and modification. In *Matter of Harris Testamentary Trust*,\(^7\) the trustees petitioned for reformation of a testamentary trust with the consent of all beneficiaries. The settlor died in 1969. The trustees sought three changes to the trust, for the purpose of binding the IRS and protecting the beneficiaries from creditors’ claims.

The first change would limit the discretionary power of the testator’s son as trustee to invade principal. The trustees were concerned that, unless an ascertainable standard was added to limit his discretionary authority, the trust principal would be included in the son’s estate because he otherwise held a general power of appointment. The trustees contended that such a change was consistent with the settlor’s intention to minimize transfer taxes, as evidenced by his use of general language limiting the ability of a trustee to disqualify certain trust property from compliance with the marital deduction requirements. Moreover, they produced an affidavit from the settlor’s attorney representing that the settlor intended to minimize taxes. Also, the remainder beneficiary of the trust was a charity. The trustees claimed that the lack of ascertainable standard language in the document was the result of a drafting mistake.

The second amendment involved changing the trust language to be consistent with the settlor’s intent to protect the beneficiary’s interest from the claims of creditors. By changing a “shall” to a “may” with respect to the trustees’ power, the trustees wanted to clarify that their power to distribute in certain instances was discretionary and not mandatory. The trustees contended that the settlor’s separate use of a spendthrift clause evidenced his intent to provide protection from creditors, and the proposed amendment would be consistent with that purpose.

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\(^7\) 69 P.3d 1109 (Kan. 2003).
The final amendment involved the addition of a provision empowering the trustees to divide the trust into separate beneficial shares for qualified subchapter S trust (QSST) purposes. Without that amendment, the trust would not qualify as a QSST because it had multiple income beneficiaries. Otherwise, the trust without amendment could not own stock in an S corporation. The trustees claimed that the absence of a power to divide into separate shares resulted from a scrivener’s mistake and once again the settlor’s intent was evidenced by other tax-saving provisions in the trust.

The court observed that the state version of the Uniform Trust Code became effective on January 1, 2002 — the first state to adopt a version of the UTC. The Kansas UTC provides that its provisions are retroactive without a clear indication of a settlor’s contrary intent. The court found nothing to prevent the application of the Kansas UTC and observed that the questions were ones of first impression. The court noted that the UTC differentiates between a reformation — which applies when the document fails to reflect the settlor’s original intent — and modification — involving a change in terms that are not the result of a mistake in the original document but are not inconsistent with the settlor’s probable intent.

The court determined that reformation was appropriate under the UTC for the first requested amendment because the trustees satisfied the necessary standard of clear and convincing evidence that the original language, or absence of language, resulted from a mistake of fact or law. The court ruled that modification was the proper theory to effect the second change under the UTC, allowable when the modification of administrative or dispositive provisions, spurred by a change in circumstance not anticipated by the settlor, accords with the settlor’s probable intent. The court also used modification to approve the third requested change, noting that the UTC specifically allows the combination or division of trusts unless the change would impair the rights of a beneficiary or adversely affect accomplishment of the trust’s purpose.71

The theories for the approved reformation and modification requests may exist in other jurisdictions at common law or by statute, but Harris demonstrates how the UTC compiles in one place a number of grounds for a court to generously consider a request for modification or reformation of a trust.

71 See also In the Matter of the Virginia S. Biggs Charitable Remainder Trust, 109 P.3d 1253 (Kan. 2005) (court uses Kansas versions of UTC section 412, allowing modification for change of circumstance, and section 416, allowing modification to accomplish settlor’s tax objectives, to modify trust in attempt to qualify as charitable remainder trust).
G. Bosch

No matter which of the various routes to interpret a hiatus will or trust is used, the lower court order, including one approving a family settlement, is potentially subject to IRS challenge unless the lower court order is appealed to the highest court of a jurisdiction. Under Commissioner v. Estate of Bosch,\textsuperscript{72} the IRS and the federal courts are not required to recognize a construction by a local court if they believe that it is not consistent with the interpretation that would have been rendered by the highest court in the state. The IRS and the federal courts need only give “proper regard” for the views of the lower courts. A trial court order construing a will that leaves the decedent’s children an amount equal to the applicable exclusion amount as establishing a $3.5 million children’s share may be viewed by the IRS and the federal courts as incorrect, and as actually constituting a $3.5 million gift by the surviving spouse. If the nonmarital share is held in a trust for the spouse and descendants, the assets deemed given away by the spouse could be includible in the spouse’s gross estate under sections 2036, 2038, or 2041.\textsuperscript{73} In a law review article reviewing circuit 34 years of case law applying Bosch in tax cases, Paul Caron found that over 59% of the tax cases decided by the courts of appeals declined to follow the decision of the lower state court. The federal trial courts were found to be even less likely to accept the decision of lower state courts.\textsuperscript{74} Professor Caron stated:

In many of these cases, the federal courts have cavalierly disregarded the state court’s interest in being the final arbiter of laws within the state, characterizing state court decisions with which it disagreed as merely “another evidentiary factor” . . . to consider or as an example of “judicial fiat.” . . . One federal court brazenly noted “the very limited role that state trial court decisions may play in determining federal tax liability” . . . and instead called upon federal courts “to reexamine de novo the state court decisions.” . . . Other courts emphasized that they were “free to differ” with the state court’s interpretation of state law . . . and that to allow state court

\textsuperscript{72} 387 U.S. 456 (1967).

\textsuperscript{73} See, e.g., TAM 199903031 (Jan. 22, 1999) (rejecting state court interpretation of trust clause that appeared to give spouse a lifetime power to appoint trust funds to someone else, finding that although state court reformed trust so as not to give spouse a power of appointment, spouse had such a power under state law and the trust did not qualify as a QTIP).

decisions to bind federal courts in later federal tax litigation “would subject the federal tax system to ‘the whim of the state courts.’” . . . Another court characterized the “lesson” of Bosch as follows: the Service, “having been absent from the State court proceeding that established rights to the decedent’s property, is entitled to have its day in Federal court.”

* * * *

The language of these federal courts, whether ultimately rejecting or accepting the state court’s interpretation of state law, is striking in their disrespect for state courts. . . . At best, the federal courts give mere lip service to the Bosch “proper regard” standard. . . . In most cases, the federal courts engage in de novo review of state law without giving any weight to the state court decision. . . . In addition, many federal courts also have reverted to a pre-Bosch focus on the adversariness of the state court decision. . . . For example, in Estate of Delaune v. United States . . . the Fifth Circuit stated that where “the state court adjudication arises out of a manifestly non-adversarial proceeding and the relevant federal tax statute indicates no preference for the sanctity of the state court’s ruling, we need accord no particular deference, and must conduct our own investigation of the relevant state law.” . . . In other cases, however, federal courts have noted that Bosch intended the “proper regard” test as a substitute for the nonadversary proceeding test.75

Lower court construction or interpretations, especially non-adversarial family settlements, will be more open to IRS scrutiny because of the Bosch rule.76 When the lower court order is supported by reasonable evidence, such as testimony of the drafting attorney as to the decedent’s intent, possible correspondence to or from the decedent, and statements made to independent parties, there is less likelihood of a successful IRS challenge. In the context of actions to determine the decedent’s intent concerning how a tax-sensitive formula is to be construed, it is unlikely that there will be any precedent to the contrary. Bosch concluded that the highest court of New York, based on existing precedent, would not have affirmed the friendly ruling of the trial court, but Bosch involved a question of law.77 No such legal precedent will exist

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75 Caron, supra note 74, at 763–64.
76 See TAM 201004022 (Jan. 29, 2010) (settlement agreement that was approved by lower court, without evidentiary hearing, rejected by IRS as basis for estate tax charitable deduction).
77 In Bosch, Mrs. Bosch released a general power of appointment to convert it into a special power. After Mr. Bosch’s death, his estate sought to have the trial court nullify
for construction of formula provisions: formula construction actions and settlements will determine the decedent’s intent, which is a question of fact, not law as was involved in Bosch.\textsuperscript{78}

Moreover, the Caron statistics consider the number of reported decisions, but not the possible number of state court rulings that were not challenged by the Service in audit or beyond in the appeal process (or even not audited at all). There is no ready statistical database with this information, but these cases surely exist. There will be tens of thousands decedents, and maybe more, dying in 2010 with documents that use tax-sensitive formulas in need of construction. Each estate will be unique as to each decedent’s intent, even when similar language is used. It is always going to be a question of fact, so Bosch should not present a problem.

The Service may not agree with this conclusion. In a 1996 Action on Decision\textsuperscript{79} concerning Estate of Goree v. Commissioner,\textsuperscript{80} the Chief Counsel’s Office stated:

\begin{quote}
Estate of Bosch does not require the application of an appellate review standard to factual findings related to lower state court determinations. Rather, Estate of Bosch holds that lower state court judgments are not binding on the Tax Court, including factual determinations, and that the Tax Court should reconsider such judgments de novo.
\end{quote}

\textit{Goree} involved disclaimers that the Service contended were not valid under state law (Alabama), although approved by a probate court order. In reaching its decision, the Tax Court applied the Alabama standard of review for factual issues: “whether the probate court’s decision was ‘plainly and palpably erroneous.’” The action on decision recommended against an appeal in Goree. The Chief Counsel was unsure whether “the ultimate conclusion of the Tax Court would have been altered by the adoption of the proper standard for review of factual conclusions of the state court.”

\textsuperscript{78} The maxim “No will has a brother” is often used to indicate that virtually every will construction case is dependent on its unique set of facts because the goal is to determine the intent of that testator. See, e.g., Bank of Boston Connecticut v. Brewster, 628 A.2d 1354 (Conn. Super. Ct. 1992).


\textsuperscript{80} T. C. Memo 1994-331.
The North Alabama District Court in *Estate of O'Neal v. Commissioner*, favorably cited *Goree*. However, the Fifth Circuit in *Delaune v. United States*, cited but did not follow the *Goree* holding concerning the standard on review by the federal courts.

Estate planners should be careful, however, with family settlements and other friendly trial court orders. If the order produces a result that is not supported by the facts or that is not reasonable, the IRS will have a better shot. For an example in a different context, assume a spouse makes a one-third elective share claim against a decedent’s estate, but the claim is settled for an omitted spouse’s one-half interest. This result is arguably not reasonable and may not withstand *Bosch* scrutiny and may result in a taxable gift by the party that consented to the excessive settlement.

**IV. Conclusion**

What is clear about hiatus deaths is that the decedent’s documents are likely to be based on formula divisions that rely on tax terms of art for an estate tax that does not exist at the decedent’s death. Although the potential problems are fairly certain, the resolutions are not. Perhaps one of the construction tools discussed above will suffice, but if not, some remedy will have to be found.

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81 81 F. Supp. 2d 1205 (N.D. Ala. 1999), aff’d in part, remanded in part 258 F.3d 1265 (11th Cir. 2001), on remand 228 F. Supp. 2d 1290 (N.D. Ala. 2002) (Bosch issue not addressed on appealed).
82 143 F.3d 995 (5th Cir. 1998).
83 Some of the problems discussed in this article might be resolved by the use of tax qualified disclaimers. A properly executed disclaimer could resolve the state property law issue determining whether property passes under the decedent’s will or trust. And if such a disclaimer complies with Internal Revenue Code section 2518, there should be no gift tax consequences to the claiming taxpayer. For example, assume a will leaves to the decedent’s adult children an amount equal to the most that can pass free from federal estate taxes, which would mean all of the estate in 2010, and the balance to a share for the decedent’s surviving spouse. A disclaimer by the decedent’s children of some portion or all of their devise will fund the marital share to the extent of the disclaimer and without gift tax consequences, if the disclaimer qualifies under section 2518. Of course, not all problems can be solved by disclaimers because a disclaimer may not send the property to the desired trust or persons. For example, a gift of the GST exemption amount to a GST trust and the balance to a surviving spouse cannot be fixed by a disclaimer by the surviving spouse because the spouse’s disclaimer would likely result in property passing by intestacy and not to the GST trust. Moreover, some parties interested in the decedent’s will or trust may not be inclined to disclaim. A full blown discussion of disclaimers is beyond the intended scope of this article, however.