GENERAL 1

A. INTRODUCTION

The disclaimer is a strange creature. Though invented in England centuries ago (and referred to as waiver or renunciation),[1] the 1976 codification, in Section 2518 of the federal transfer tax law of disclaimer, popularized both the concept and the name "disclaimer." It is also conceptually strange, requiring the donee of a gift (either lifetime or testamentary) to reject it, so that the gift is never made.[2] Which begs the question, "Why would you refuse to accept a gift?"

There are two main reasons for doing so: first, the act of disclaiming, for federal transfer tax purposes, is not a transfer,[3] and therefore there is no tax on it from the disclaimant's perspective; and second, for state

1. *See, e.g.*, J. H. Martin, *Perspectives on Federal Disclaimer Legislation*, 46 U. CHI. L. REV. 316, fn. 2 (1979).

2. BROWN, PERSONAL PROPERTY, § 7.14 (3d ed. 1975).

3. § 2518(a). Regs. §§ 25.2518–1(b) and 25.2511–1(c)(2) ("a refusal to accept ownership does not constitute the making of a gift. . .").

law purposes (primarily debtor-creditor purposes), the disclaimant is deemed never to have possessed the disclaimed property.

The conceptual engine that drives the disclaimer is the "relation-back" concept: a disclaimer "relates back" to the original transfer of the interest disclaimed.[4] If Jane dies on July 1, 2008, leaving her estate to Bob and, within the time required, Bob makes a qualified disclaimer of that gift, the disclaimer is effective as of the date of Jane's death, not Bob's disclaimer. Jane's will or state law, or both, determine who takes her estate instead of Bob. Note that Bob has no say in where the estate assets go.

For example, Rev. Rul. 83–26[5] dealt with a husband's will that created a trust, all of the income of which was payable to the wife for life, with the remainder passing to the husband's children. After the husband died, his executor made a qualified terminable interest property (QTIP) election for the trust on the federal estate tax return. The wife later made a qualified disclaimer of her trust interest. The executor claimed that the QTIP election foreclosed the wife's disclaimer, and therefore the husband's estate was entitled to the marital deduction for the full value of the trust and the wife's subsequent disclaimer was actually a transfer of the QTIP property. However, the IRS ruled that, even though the executor's QTIP election had preceded the wife's disclaimer, the disclaimer related back to the date of the husband's death, so the disclaimed interest never passed to the wife and the transfer did not qualify for the QTIP election. The estate got no marital deduction, and the wife made no taxable transfer.

Disclaimers are governed by both state and federal law. Section 2518 introduced the term "qualified disclaimer" for federal transfer tax purposes, but it has little impact on the state law of disclaimers, and it does not apply to disclaimers made before 1977. For those earlier disclaimers (which are fairly rare), the tax law that applies involves a tangle of historical decisions, rulings, and regulations. Which means that the first thing a practitioner must do when determining whether a disclaimer is appropriate is to determine which federal law applies and how state law will affect it.

4. *See* § 2518(b)(2).
5. 1983–1 C.B. 234.

B. Overview of Federal Transfer Taxes

Section 2518 appears within Chapter 12 of the Internal Revenue Code, the gift tax chapter. However, the first sentence of Section 2518 makes it clear that this section provides the rules for disclaimer not only with respect to inter vivos gifts (Chapter 12) but also with respect to transfers of taxable estates (Chapter 11) and generation-skipping transfers (Chapter 13). Therefore, a very brief discussion of transfer taxes is appropriate. The transfer taxes (estate, gift, and generation-skipping transfer, or GST, taxes) are imposed on the gratuitous transfer of property,[6] based on a person's cumulative lifetime and testamentary transfers of property.[7] They are calculated on the fair market value of the property transferred.[8] The 2001 Tax Relief Act changed the tax rates, the unified credit exemption amounts, the deduction for qualified family-owned business interests, and the state death tax credit applicable in the interim before repeal.[9] Effective January 1, 2010, the estate and GST taxes were repealed. However, in December 2010, Congress (after much noise) reinstated the federal estate and GST taxes, with other significant changes, but only until December 31, 2012.[10]

The Tax Relief, Unemployment Reauthorization, and Job Creation Act of 2010, (the "2010 Act") allows for a $5 million exemption from estate, gift, and GST taxes and the "portability" of exemption between spouses, allowing a surviving spouse to use both his or her exemption as well as that of the predeceased spouse, for a total of up to $10 million of exemption.

6. *See* Regs. §§ 20.0–2(a); 25.0–1(b).
7. §§ 2001(b), 2502(a).
8. §§ 2032, 2032A, and 2512(b).
9. *See* Pub. L. No. 107-16, §§ 511, 521, 531, and 532.
10. *See, e.g.*, Beth S. Kaufman, *Finally, Legislation! Congress Kicks the Can Down the Road,* 38 Estate Planning 36 (June 2011).

C. OVERVIEW OF QUALIFIED DISCLAIMER

The overwhelming majority of disclaimers will be subject to the rules of Section 2518. The rare exception will be for the child who is a distributee of a pre-1977 decedent's estate or a beneficiary of a pre-1977 gift and who was a minor in 1976.[11] The regulations applicable to these early disclaimers generally permitted a disclaimer "within a reasonable time after knowledge of the existence of the transfer."[12] Arguably, the minority period for federal tax purposes[13] or local law minority period extends the "reasonable time." Further, the taker in default of a general power of appointment created under the will of a decedent who died before 1977 or under a pre-1977 inter vivos trust may still have years within which he or she can disclaim his or her interest because of the way in which the regulations determined the starting point for a disclaimer (however, if the power holder dies after 1976 and the power lasts until his or her death, the disclaimer is governed by Section 2518[14]).

The qualified disclaimer of Section 2518 must be made within nine months of the date of the decedent's death or the date of gift, or nine months after age 21 if the prospective disclaimant is under age 21 at that date.[15] A qualified disclaimer is an irrevocable and unqualified refusal to accept an interest, or undivided portion of an interest, in property,[16] which may include a power with respect to property.[17] The refusal must be in writing,[18] delivered to the transferor of the interest, his legal representative or the holder of the legal title to the property to which the interest relates, not

11. *But see* Ordway v. U.S., 89-1 USTC ¶ 13,802 (S.D. Fla. 1989), *rev'd*, 908 F.2d 890 (11th Cir. 1990), *cert. denied*, 501 U.S. 1261 (1991); Irvine v. U.S., 89-2 USTC ¶ 13,818 (D. Minn. 1989), *rev'd*, 936 F.2d 343 (8th Cir. 1991), *aff'd en banc*, 981 F.2d 991 (8th Cir. 1992), *rev'd*, 511 U.S. 224 (1994).
12. See Chapter 4.
13. *See, e.g.*, §§ 2503(c), 2518(b)(2)(B).
14. Regs. § 25.2518–2(c)(3).
15. § 2518(b)(2).
16. § 2518(b).
17. § 2518(c)(2).
18. § 2518(b)(1).

later than nine months after the date of the transfer creating the interest, or nine months after the disclaimant becomes 21.[19] The disclaimant must not have accepted the interest or any of its benefits.[20] As a result of the disclaimer, the interest must pass, without any direction on the part of the disclaimant, either to the spouse of the decedent or transferor[21] or to a person other than the disclaimant.[22] The details of these requirements will be discussed in future chapters.

19. § 2518(b)(2).
20. § 2518(b)(3).
21. § 2518(b)(4)(A). The spouse to whom the disclaimed interest passes can be the disclaimant. *See* PLR 200006052.
22. § 2518(b)(4)(B).