DADE COMMUNITY FOUNDATION
Professional Notes
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Professional Tax & Estate Planning Notes

USE OF QUALIFIED DISCLAIMERS IN ESTATE PLANNING

ISSUES IN THE NEXT SERIES:

Estate Planning for Individuals & Non-Traditional Families

Estate Planning for Retirement Assets

This issue of Professional Notes focuses on the use of the qualified disclaimer in estate planning. Often overlooked when drafting a will, the qualified disclaimer can be thought of as a "post-mortem" planning device, but one that should be considered in advance. It allows your clients to give their heirs the flexibility to determine whether they need assets long after a will is written when circumstances may have changed. And if a qualified disclaimer is used to provide for a charity, such as the Dade Community Foundation, it has the added advantage of reducing the taxable estate.

A disclaimer is a renunciation of property passing upon another's death, whether the assets are to pass by will, pension or insurance beneficiary designation, or by state intestacy laws. For Federal estate, gift, and generation-skipping transfer tax purposes, the renounced property is treated as if it had never been transferred to the person making the qualified disclaimer (the disclaimant). Under Florida law, the property passes as if the disclaimant predeceased the decedent. The disclaimed property then passes, either outright or in trust, to the named alternate beneficiary.

To be effective for both Florida property law purposes and for Federal gift tax purposes (i.e., the transfer is not treated as a gift), the disclaimer must comply with both the provisions of the applicable disclaimer statute and Section 2518 of the Internal Revenue Code. For Federal gift tax purposes, a qualified disclaimer is defined in Section 2518(b) as an irrevocable and unqualified refusal by a person to accept an interest in property, but only if:

(1) the refusal or disclaimer is in writing;
(2) the written refusal is received by the transferor of the interest or his legal representative (usually the executor) not later than nine months after the date on which the transfer creating the interest in the disclaimant is made (generally the date of death), or, if later, after the disclaimant's 21st birthday;
(3) the disclaimant has not accepted the interest or any of its benefits; and
(4) as a result of the refusal, the interest passes, without any direction by the disclaiming person, to either the spouse of the decedent or a person, including charity, other than the disclaimant.

If these requirements of Section 2518(b) are not met, the renouncing person will be deemed to have received the assets and to have made a taxable gift. An exception under Section 2518(c) provides that a renunciation that is valid under state law and meets requirements similar to those set forth under Section 2518(b) will be treated as a qualified disclaimer.

General Use of the Qualified Disclaimer. The qualified disclaimer can be used to renounce an interest in any type of property passing upon another's death. It might be used, for example, when a husband dies leaving all his assets to his wife, or if she does not survive, to their children. If the wife concludes she does not need all of the assets, she may wish to disclaim a portion of her interest in her husband's estate. By disclaiming assets worth up to $1,500,000, the Federal estate tax exclusion amount for 2004, the disclaimed portion does not become part of the wife's estate, and no Federal estate tax will be due on the assets passing to the children.

Or the husband might have planned for the possibility of a disclaimer, providing in his will that any disclaimed part would go into a trust that pays income to his wife for her life. For example, a credit shelter trust. The trustee may have the power to invade the trust principal to support the wife, and the remainder could then be distributed to their children or to designated charities. As in the prior example, if the wife disclaims assets up to $1,500,000, the husband's estate can take advantage of the Federal estate tax applicable exclusion amount and the disclaimer trust assets will not become part of the wife's estate.

A disclaimer may be made of all of an interest passing at death, or of a portion of the interest. For example, a beneficiary might renounce 40 shares of a block of 100 shares of stock bequeathed to him, or he might renounce an undivided 40 percent interest. Or a disclaimer might be made of a specific dollar amount; for example, the residuary beneficiary might disclaim $40,000 of the residuary estate.

A survivorship interest also may be disclaimed. At one time, the Internal Revenue Service had taken the position that a survivorship interest had to be disclaimed within nine months of the transfer creating the joint tenancy. In 1990, the Service conceded that in states such as

Florida, where a joint tenant can partition property at will, the interest is deemed created when the interest vests, and not when the joint tenancy first occurred. Therefore, the nine-month period for making the disclaimer begins at the death of the joint tenant.

Use of the Qualified Disclaimer to Benefit Charity. As indicated earlier, if the disclaimed assets pass to charity, the estate will benefit from an estate tax charitable deduction. As combined Federal and state (not Florida of course), estate tax rates can still exceed 50 percent, the savings can be significant. However, the statutory restriction against redirection or control of the disclaimed property by the disclaimant, either directly or indirectly, is given a broad interpretation by the IRS. The testator must designate in his or her will the charity to which a disclaimed interest is to pass; the testator may not provide the disclaimant with any discretion in that decision. In addition, the testator must be careful about the relationship of the potential disclaimant to the designated charity.

For example, a decedent had provided that a bequest to her daughter would pass to the family's private foundation in the event the daughter disclaimed all or part of her interest. The IRS ruled that the disclaimer qualified under Section 2518 only because the foundation's bylaws were amended to prohibit the daughter and her husband (as two of the directors of the foundation) from participating in the distribution of the bequeathed funds and, instead, conferred the sole authority of disposition upon the foundation's two independent directors. See PLR 9141017, PLR 9317039, PLR 200149075, PLR 2004 20007.

Such problems can be avoided if the testator directs potential disclaimed assets to a community foundation, such as the Dade Community Foundation. In Private Letter Ruling 9532027, a father provided for property held in trust to pass to his two sons at his death, or if they predeceased him, to their children. Under the terms of the trust, if either son refused his interest, his share of the property was to go to a fund the decedent established at a community foundation, and the disclaiming son was permitted to serve as the advisor with respect to grants from the fund.

The Service ruled that the irrevocable refusals by the sons constituted qualified disclaimers even though the sons could make recommendations to the community foundation regarding distributions from the fund that received the disclaimed property. The Service concluded that neither disclaimant had the power to direct the redistribution, because any grant recommendations were merely advisory in nature. One of the sons was a member of the community foundation's board of directors, but in accordance with the private letter rulings mentioned earlier, he could not vote on distributions from the fund he advised.

This private letter ruling offers a substantial planning opportunity. A client may provide for a gift to his or her children, which, if refused, would be distributed to a fund at The Dade Community Foundation, reducing the taxable estate. The Foundation offers a professional grant staff to carry out the donor's charitable interests, and, if desired, the children (or other heirs) would have the opportunity to suggest grants from the fund.

Other Uses of Qualified Disclaimers. A qualified disclaimer also may be used with respect to interests outside the probate process, including interests in life insurance and employee benefit plans.

For example, a participant in a retirement plan may wish to name his or her spouse as the primary designated beneficiary of the plan and a charity as the contingent successor beneficiary. After the death of the plan participant, if the surviving spouse determines that he or she does not need the funds from the retirement plan, the surviving spouse can disclaim his or her interest and the funds will instead pass to charity. If the surviving spouse wishes, he or she can make a partial disclaimer of only a portion of the funds. Since funds in a retirement plan may be subject to both estate tax and income tax when passing to individual beneficiaries, such funds are often a good choice of asset for satisfying a plan participant's charitable goals.

Conclusion

Advising your clients about the qualified disclaimer when they are planning for their estates can provide flexibility when it is needed and reduce the taxable estate. If your clients have charitable interests, they can name a charitable successor beneficiary, benefiting charity and ensuring that their philanthropic concerns are honored, while reducing the taxable estate at the same time.

For further reference, see:
IRC Section 2518, Qualified Disclaimers
IRC Section 2055, Estate Tax Charitable Deduction
IRC Section 2010, Unified Credit
Revenue Ruling 72-522, 1972-2 C.B. 525
Private Letter Ruling 9532027
Private Letter Ruling 200149075
FLA STAT Sec.S689. 21 & 732. 801

If you know a colleague who would like to receive complimentary copies of Professional Notes, or if you wish to obtain past issues, please call our office at (305) 371-2711. You can access past issues on our Web site at www.dadecommunityfoundation.org in our Professional Advisors Guide section.

LEAVING A LEGACY OF GIVING THROUGH YOUR WILL

The foresight of community leaders has helped Dade Community Foundation plan for tomorrow by building a permanent, growing endowment that will enable future generations to address community needs. Much of the growth experienced by Dade Community Foundation has come through bequests, the simplest and oldest of all planned gifts.

Wills and trust agreements should be drafted by an attorney. When including in one's will, a bequest to Dade Community Foundation the following language may be used. This example can be adapted to provide for any special restriction or to define a field of charitable interest. Sample language:

I devise_____________________________ (describe gift) to Dade Community Foundation, Inc. Miami, Florida, for the establishment of the "________________________________FUND" (name of charitable fund) where earnings from this devise shall be distributed annually to meet the emerging (or field of charitable interest) needs of Miami Dade County.

A bequest to Dade Community Foundation through your will establishes your legacy of giving as you create a permanent source of good for your community.

Below are some examples of donors who continue to give back to our Miami-Dade community

Anthony Sumegi Fund

Anthony Sumegi grew up in Ohio. At a very young age, he began working at General Motors to support his family. As this nation entered World War II, he left his home and job to serve honorably in the military. He participated in the African and Italian campaigns. After the war, he returned to General Motors where he continued to work until his retirement. He moved to Miami in the 1970's. A reclusive man, he established a charitable fund in his will to assist the homeless of Miami-Dade County. He leaves a legacy of caring for those in need of support and shelter.

E. W. Blower Fund

The E. W. Blower Memorial Fund was established by Ruth Blower Weiner to honor the memory of her father, who passed away in 1954. This is administered as a perpetual fund, using the interest earned to support pediatric research at the University of Miami School of Medicine and to benefit pediatric patients at Jackson Memorial Hospital.

Dorothy, Edward and Robert Frohlich Fund

Edward Frohlich was a Lieutenant Colonel in the U.S. Army Air Corps who fought in World War II (Europe) and Dorothy Frohlich was an amateur painter. Their son, Robert, passed away after an illness at a young age. Mr. Frohlich passed away in 1982, and his wife died in 1996. Through her will, she made it possible to establish their Field of Interest fund to help local institutions that specialize in children's health and care. Children will be helped in perpetuity through this memorial to Robert Frohlich.

Helen A. & Bertram J. Goldsmith Memorial Fund

In the late 1950's, the Goldsmiths established roots in South Florida. Bertram J. Goldsmith, the family's patriarch, was a successful real estate investor and philanthropist. This fund, established through the Goldsmiths' wills, distributes grants annually to local nonprofit organizations that help college students in need of financial assistance. A new generation of Goldsmiths, Bertram Jr. and Susan, continue the family's legacy by providing additional support to this charitable fund.

ABOUT DADE COMMUNITY FOUNDATION

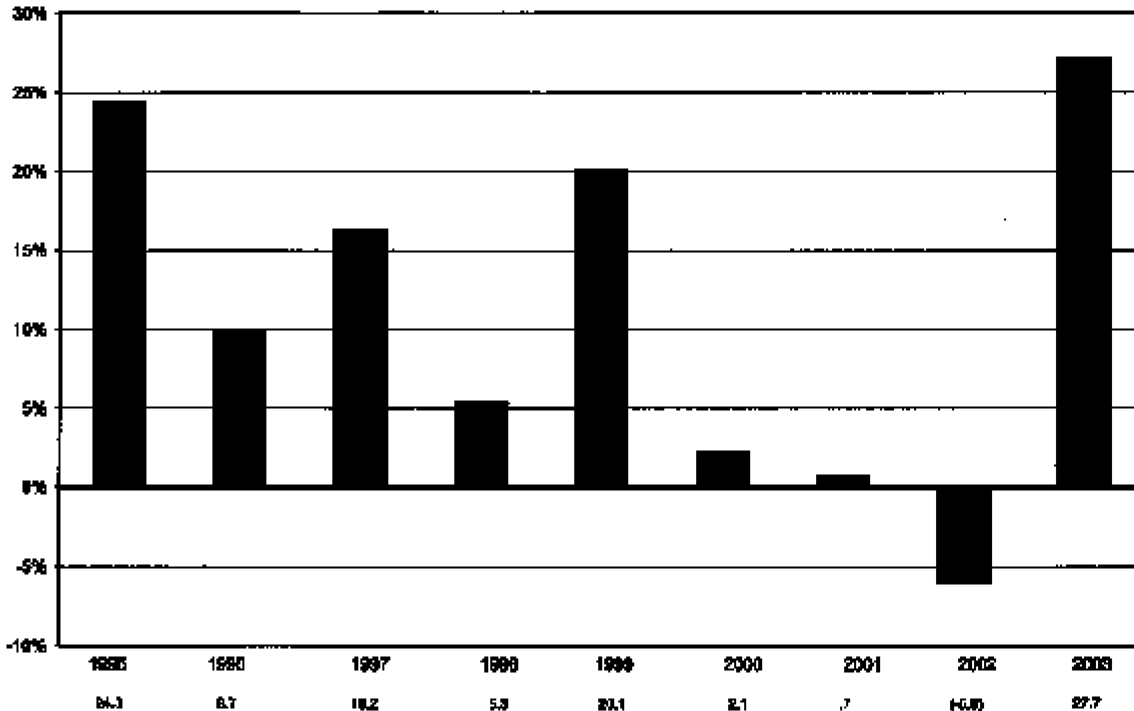
For 37 years, Dade Community Foundation has been the community foundation for Miami-Dade County, an aggregate of funds created by individuals, families, and corporations to benefit the world around them -- especially the people of our community.

The Foundation is governed by a 21 member Board of Governors composed of community leaders. Its staff is recognized for experience in grant making, financial administration, and donor services.

*Since 1967 Dade Community Foundation has made grants of almost $80 million to Greater Miami's nonprofit agencies. For more information about the Foundation call Joe Pena, Director of Development and Communications at **305-371-2711**.*

Investment Growth of Foundation Pooled Assets

Founded in 1967 with assets of $250,000, the Dade Community Foundation has assets today of more than $100 million. Below is a chart demonstrating the financial investment performance of the Foundation's pooled funds from 1995-2003.



This material was originally developed for the use of professionals by The New York Community Trust, one of the nation's largest community foundations. It was published with the understanding that neither the publisher nor the authors are engaged in rendering legal, accounting, or other professional services. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.

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