

Drafting opportunities under the new Texas disclaimer statute

Glenn M. Karisch
Austin, Texas



The materials

The paper

- **Most of our focus will be on the new drafting section of the paper on pages 31 – 45**
 - There's a lot of information in the rest of the paper

Appendix 1

- The statutory text with section-by-section commentary

Appendix 2 and texasprobate.com

- Forms

These slides are available at texasprobate.com

- Click "Papers and Articles" under "Information for Professionals"



MS Word versions of the forms at texasprobate.com

- 1. Disclaimer of interest in a decedent's estate where a personal representative has been appointed
 - 1.1. Mailed
 - 1.1.1. Full disclaimer
 - 1.1.2. Disclaimer of interest in specific asset
 - 1.1.3. Formula disclaimer
 - 1.2. Hand Delivered
 - 1.2.1. Full disclaimer
 - 1.2.2. Disclaimer of interest in specific asset
 - 1.2.3. Formula disclaimer

- 2. Disclaimer of interest in a decedent's estate where no personal representative has been appointed
 - 2.1. Full disclaimer
 - 2.2. Disclaimer of interest in specific asset

- 3. Disclaimer of interest by a trustee
 - 3.1. Trustee's notice of intent to disclaim
 - 3.2. Waiver of trustee's notice of intent to disclaim

Introduction

The old law:

- Estates Code Chapter 122
- Trust Code Section 112.010

The new law:

- Texas Uniform Disclaimer of Property Interests Act: Property Code Chapter 240



There's no state law time limit

- Since 1977, Texas disclaimer laws had a 9-month deadline
 - Modeled after gift tax law, but it wasn't a perfect match
- The new law is de-coupled from tax law
- The new deadline: disclaimers are permitted **prior to acceptance**
 - Taking possession of the interest, or
 - Exercising dominion and control over the interest



But don't ignore the tax deadline

- The 9-month deadline for gift tax purposes still applies
 - A person disclaiming after the 9-month deadline could be making a taxable gift
 - But gift tax issues affect only a small fraction of the population
- The Texas Act contains a tax savings provision
 - If it is a valid disclaimer for gift tax purposes, it automatically meets the Texas requirements



Eliminating 9-month deadline enhances the use of disclaimers for creditor protection

- The new law preserves the relation-back doctrine
 - *Dyer v. Eckols*, later codified: A disclaimer relates back to the time of death or irrevocable transfer
- Pre-petition disclaimers work in bankruptcy
 - *Matter of Simpson* (5th Circuit 1994)
- Post-petition disclaimers don't work
 - *In re Schmidt* (Bkrtcy W. D. Tex. 2007)
- Disclaimers for Medicaid purposes don't work



Fiduciary disclaimers

- Court approval is required for:
 - Disclaimers by dependent administrators and guardians
 - Disclaimers by trustees of court-created trusts
 - **A disclaimer that would result in property or an interest in property passing to the fiduciary personally**
- Court approval is not required for disclaimers by:
 - Independent executors
 - Agents under powers of attorney
 - **A natural guardian (a/k/a parent) of a minor if the minor would have received the disclaimed property *only as a result of another disclaimer***
 - Trustees of non-court-created trusts, **but...**

Trustee disclaimers

- New (or at least clarified): a trustee may disclaim, keeping property from passing into the trust
- The trustee must either:
 - Give 30 days' notice to beneficiaries; or
 - Get court approval
- If court approval is *not* obtained, the disclaimer "must be compatible with the trustee's fiduciary obligations"
 - Concerned about liability? Get court approval
 - Concerned about saving money/complexity? Give notices



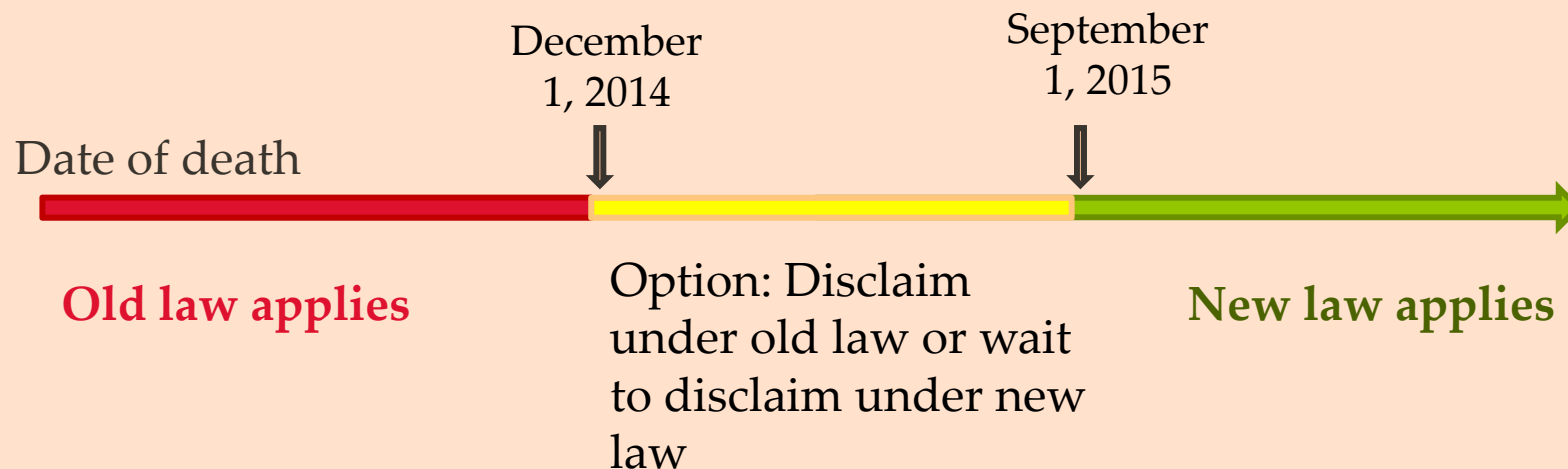
The mechanics of making a disclaimer

- Only one notice
 - No need to deliver notice to executor *and* file with court
 - The statute clearly states to whom the notice must be delivered for each type of property
 - Possible trap: It is possible that disclaimers must be sent to multiple persons
- **Special mailbox rule**
 - If mailed to intended recipient at good address by certified mail, delivery is considered to have occurred on the date of mailing *regardless of receipt*

Effective date

Texas Uniform Disclaimer of Property Interests Act:
Effective date: **September 1, 2015**

Operative date: **December 1, 2014**



Drafting opportunities

pp. 31 - 45

We will cover these four topics:

- Drafting estate planning documents in anticipation of possible disclaimers
- Drafting disclaimers themselves
- Drafting notices and waivers for trustees wishing to disclaim
- Drafting pleadings and related documents for court approval of disclaimers



Drafting EP docs with disclaimers in mind

pp. 31 - 32

- An old dog: disclaimer into the bypass trust
 - Supplementing a formula funding clause
 - A “disclaimer trust”
- A new trick: disclaimer out of the bypass trust
 - A way to get basis adjustment at the second death
 - It works “downstream,” but probably not “upstream”
 - **Solution: have an express provision addressing disclaimers by the trustee of the bypass trust in every case**

Drafting EP docs with disclaimers in mind

pp. 32 - 33

- Going crazy: directing disclaimers into and out of all trusts
 - Trustee disclaimer from bypass to QTIP, and vice versa
 - If trustees of bypass and QTIP both disclaim, property goes outright to surviving spouse
 - Trustee disclaimer from GST-exempt trust to non-exempt trust
 - Disclaimer into a special needs trust
 - Disclaimer into a QSST or ESBT
 - Disclaimer of retirement benefits into conduit trust
 - Disclaimer of retirement benefits out of conduit trust

Drafting EP docs with disclaimers in mind

pp. 33 - 34

- Consider using a special trustee to make disclaimers to avoid court approval
 - Court approval is required if a trustee disclaimer causes property or an interest in property to pass to the trustee individually
 - A disinterested special trustee with the power to disclaim solves this
 - Must be a “trustee,” not a trust protector or advisor
 - As a trustee, the special trustee will be subject to fiduciary duties but may be exculpated to the extent permitted by Trust Code
 - May a family member with an interest in the trust have the power to appoint a special trustee?

Drafting EP docs with disclaimers in mind

p. 34

- Should the trustee be exculpated for making disclaimer decisions?
 - The limits on exculpation in the Trust Code apply
 - This should not be a boilerplate provision
- Consider prohibiting trustee disclaimers
 - This must be done in the instrument creating the fiduciary relationship
 - A pour-over will cannot prohibit a disclaimer by the trustee of an inter vivos trust

Drafting EP docs with disclaimers in mind

pp. 35 – 36

- Using a disclaimer to make a defined-value gift
 - The gift instrument directs the property back to the donor or into a QTIP for the donor's spouse to the extent the donee disclaims
 - The donee makes a formula disclaimer
 - The *Wandry* case permits defined-value gifts without resorting to a disclaimer
- Using a disclaimer to defer the decision to pay gift tax or estate tax
 - May be useful if the donor believes the 2704 regulations are coming out in the next nine months
 - The donee has nine months to choose to make transfer subject to gift tax or estate tax
 - Does the IRS have a pre-arranged plan argument? (see the *Monroe* case, 5th Cir. 1997)

Drafting disclaimers

p. 36

- See the paper for an extensive discussion (pp. 12 – 18)
- See the forms (Appendix 2, texasprobate.com)
- Make sure the disclaimer is delivered to the proper person

Using the notice provisions for trustee disclaimers

pp. 36 – 38

- Who is entitled to notice?
 - Current beneficiaries
 - Presumptive remainder beneficiaries
 - “ ... in the absence of notice to the trustee of the exercise of the power of appointment...”
 - *Revocable* versus *irrevocable* exercise of a power of appointment
 - Minor or incapacitated beneficiaries
 - Court-appointed guardian or conservator
 - Minor with no court-appointed guardian or conservator: to a parent
 - Notice to the Attorney General if a charity is a beneficiary
 - AG notice is not required merely because a charity is:
 - A permissive object of an unexercised power of appointment or
 - A remote contingent beneficiary

Using the notice provisions for trustee disclaimers

pp. 38 – 41

- Exceptions to the notice requirement
 - A known beneficiary who cannot be located after reasonable diligence; an unknown beneficiary
 - There is no requirement for an ad litem or notice by publication
 - A descendant of a beneficiary “to whom the trustee has given notice” if the beneficiary receiving notice virtually represents the descendant
 - **A beneficiary who waives the notice requirement**
 - A form of waiver is included in Appendix 2
- See the notice examples, pp. 39 – 41



Using the notice provisions for trustee disclaimers

pp. 38 – 41

- Be aware of these traps when using waivers
 - **Notices still may be required even if all adult beneficiaries and charities sign waivers**
 - Notice must be given to the ancestor virtually representing his or her descendants – a waiver by the ancestor is insufficient
 - Notice must be given to a parent of a minor child – a waiver by the parent is insufficient
 - Notice must be given to the Attorney General if a charity is involved – a waiver by the Attorney General is insufficient
 - **Best practice: Don't wait until the last minute.** The 30-day notice requirement could frustrate the plan even if waivers are anticipated
 - **Use extreme caution about including a release in the waiver**
 - A release supported by consideration may be considered an acceptance of benefits, disqualifying the disclaimer for tax purposes, or be evidence of a pre-arranged plan (see the *Monroe* case)

Using the notice provisions for trustee disclaimers

p. 41

- The notice must contain specific statements
 - It must state that the trustee “intends to disclaim,” but a trustee giving notice is not obligated to disclaim
 - It must specify “the earliest date the trustee intends to make the disclaimer”
 - It must include statements about the disclaimer’s effect and the beneficiaries’ rights
- Other disclosures may be required, even though the Disclaimer Act doesn’t say so
 - A disclaimer is probably a material fact affecting the beneficiary’s rights
- The notice must be “given not later than the 30th day before the date the disclaimer is made”
- The form of a notice is included in Appendix 2



Using the notice provisions for trustee disclaimers

pp. 41 – 42

- Notice must be sent by personal delivery, first-class mail, facsimile, e-mail, or any other method likely to result in the notice's receipt
- When may the trustee disclaim?
 - The trustee may not disclaim before the earliest date specified in the notice
 - The trustee may not disclaim before the 30th day after the notice is "given"
 - Is notice "given" when sent or when received? – Use personal delivery, fax or email to eliminate this issue
 - **Best practice:**
 - **The "earliest date" in the notice should be 30 days after notice is sent**
 - **The trustee should not disclaim until 30 days after notice is received by the beneficiary**

Using the notice provisions for trustee disclaimers

p. 43

- What should a beneficiary opposed to the disclaimer do when receiving a notice?
 - A beneficiary does not lose his or her right, “if any,” to sue the trustee for breach of fiduciary obligations
 - This suit may occur after the disclaimer
 - **After the disclaimer, it cannot be undone based on breach of fiduciary duty**
 - The statute does not state a mechanism for objecting to the disclaimer
 - Giving the trustee notice of objection does not prevent the trustee from disclaiming
 - Filing a suit before the disclaimer and **seeking injunctive relief is the only way to stop the disclaimer** if the trustee is determined to make it

Seeking court approval of fiduciary disclaimers

pp. 43 – 45

- Necessary parties
 - The Disclaimer Act doesn't specify necessary parties, so the necessary party rules for the type of fiduciary apply. For example, Tex. Trust Code §115.011 applies to trusts.
- Forum
 - The Disclaimer Act doesn't specify the jurisdiction of courts to hear actions related to disclaimers, so the jurisdiction rules applicable to different types of fiduciaries apply
- Judgment
 - Should the fiduciary agree to the terms of the judgment? Preferably not, but it probably does not present an acceptance of benefits problem



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Austin, Texas

