

## LEGISLATIVE PROPOSAL

The Federal estate and GST taxes are repealed with respect to estates of decedents and (for the generation-skipping transfer tax) taxable transfers occurring after December 31, 2009 and before January 1, 2011. This will have a serious adverse effect on many estate plans that contain formula clauses tied to the applicable exclusion amount, unified credit, or GST exemption, because those items will no longer exist.

For example, a typical formula clause might leave to a decedent's children the largest amount that can pass without Federal estate taxes, and leave the rest of the estate to the decedent's surviving spouse. Such a clause would pass \$3.5 million to the children and the rest of the estate to the surviving spouse, if the decedent died on December 31, 2009. The same formula could be construed to pass the entire estate to the children if the decedent died on January 1, 2010, because the entire estate can pass free of Federal estate taxes.

On the other hand, another typical clause might leave the decedent's children an amount equal to the decedent's applicable exclusion amount. Such a clause would pass \$3.5 million to the children and the rest of the estate to the surviving spouse, if the decedent died on December 31, 2009. The same formula could be construed to pass nothing to the children and the entire estate to the surviving spouse if the decedent died on January 1, 2010, because there would be no applicable exclusion amount.

The result of such a formula may be further complicated by collateral provisions that: (1) reduce the nonmarital share to reflect property that otherwise passes without qualifying for the marital deduction, or (2) require that the marital share be satisfied solely from property qualifying for the marital deduction.

Furthermore, a document might leave the decedent's grandchildren the maximum amount that can be sheltered from the generation-skipping transfer tax by the decedent's available GST exemption. Such a clause would produce a \$3.5 million gift to the grandchildren if the decedent dies on December 31, 2009, but produce no gift to the grandchildren if the decedent dies on January 1, 2010, because there is now no GST exemption.

On the other hand, a formula clause that gives the grandchildren the greatest amount that can pass free of generation-skipping transfer tax may give them \$3.5 million if the decedent dies on December 31, 2009, but give them the entire estate if the decedent dies on January 1, 2010, because there is now no generation-skipping transfer tax.

None of these results reflect the intention of the testator or grantor. A state court construing these instruments, however, may not be allowed to consider extraneous testimony about the testator's intent, unless it deems the clause to be patently ambiguous. One could argue that none of these formulae are patently ambiguous – they express a clear intent to have tax considerations determine the division of the estate. Thus, the odd

result of the literal language of the clause would, arguably, represent the proper fulfillment of the decedent's actual goals.

It is possible that Congress will retroactively reinstate the estate and GST taxes, but this is far from certain, and legal challenges to the constitutionality of such reinstatement will take many years to resolve.

It is, therefore, proposed that the Virginia Legislature act, much as it did in 1982 and 1987, (See Va. Code § 64.1-62.1) to adopt a statutory rule of construction regarding such clauses.

## PROPOSED LANGUAGE

### **§ 64.1-62.2. Certain formula clauses to be construed to refer to federal estate and generation-skipping transfer tax rules applicable to estates of decedents dying on December 31, 2009**

A. A will or trust of a decedent who dies after December 31, 2009 and before January 1, 2011, that contains a formula referring to the “unified credit,” “estate tax exemption,” “applicable exemption amount,” “generation-skipping transfer tax exemption” or “GST exemption,” or that measures a share of an estate or trust based on the amount that can pass free of Federal estate or generation-skipping transfer taxes, or that is otherwise based on a similar provision of Federal estate tax or generation-skipping transfer tax law, shall be deemed to refer to the Federal estate and generation-skipping transfer tax laws as they applied with respect to estates of decedents dying on December 31, 2009. This provision shall not apply with respect to a will or trust that is executed or amended after December 31, 2009, or that manifests an intent that a contrary rule shall apply if the decedent dies on a date on which there is no then-applicable Federal estate or generation-skipping transfer tax. The reference to January 1, 2011 in this subsection shall, if the Federal estate and generation-skipping transfer tax becomes effective before that date, refer instead to the first date on which such tax shall become legally effective.

B. A proceeding to determine whether the decedent intended that the references under subsection A be construed with respect to the law as it existed after December 31, 2009, must be filed within twelve months following the death of the testator or grantor, and not thereafter. It may be filed by the personal representative or any affected beneficiary under the will or other instrument.