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TAX AND ESTATE PLANNING NEWSLETTER

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The following tax and estate planning news may be of interest to you in your business or personal pursuits. If you have questions about any of these items, please call or e-mail one of the Tax and Estate Planning Attorneys listed below by clicking on the attorney's e-mail address or calling the telephone number.

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JOINT WILL CREATED A BINDING CONTRACT

While they were common many years ago, joint wills do not seem to be as common now. Nevertheless, they surface from time to time, and it is worth noting that the effect of a joint will may be to limit the testamentary options of the surviving spouse. For example, take the case of Kenneth and Lois Maude Loflin. In 1975, while living in Kansas, they executed a "Joint and Mutual Last Will and Testament." They had no children, and the joint will stated that the entire estate passed to the surviving spouse. Upon his or her death, the surviving spouse's estate was to be divided equally among Lois' brothers and sisters and Kenneth's nieces and nephews. The couple moved to Oklahoma where Kenneth died, and the joint will was probated. Lois then moved to Colorado where she executed a new will which revoked all prior wills. Lois' new will left a smaller portion of her estate to Kenneth's relatives than did the joint will. When Lois died, the Colorado court was asked to find that the joint will was in fact a contract between Kenneth and Lois and therefore made irrevocable by Kenneth's death, but the trial court found the joint will was not a contract. The trial court's opinion was reversed by the Colorado Court of Appeals (In re the Estate of Loflin v. Emery, 81 P.3d 1112 (Colo. Ct. App. 2003)). The appellate court applied the law of the state in which the will was executed (Kansas) to find that the parties to the will "intended a contract will." While the appellate court found that the Colorado will would determine Lois' wishes regarding her burial and the selection of a personal representative, it held that as to the distribution of Lois' estate, the joint will would control. Similarly, the Oklahoma Supreme Court upheld a contract will and imposed a constructive trust on the estate of the surviving spouse for the benefit of the beneficiaries of a joint will in Robison v. Graham, 799 P.2d 610 (Okla. 1990).

EFFECT OF DIVORCE ON IRA BENEFICIARY DESIGNATION

Deborah Steiner claimed that she was entitled to the benefits under her former spouse's IRA after his death. Although she was the primary beneficiary designated by the decedent, the designation was made before her divorce from the decedent. Her divorce property settlement agreement specifically stated that the parties waived the "right and/or benefits" which would arise under any IRA. Steiner argued she could not have waived her right to benefits under her husband's IRA because the right to receive benefits at the time of her divorce was an "expectancy" and not a "present property interest." The Court of Appeals of Indiana did not agree. The court found that the language of the property settlement agreement was intended by the parties to include *any* benefits to which Steiner was entitled as a beneficiary of the IRA. Steiner v. Bank One Indiana, 805 N.E.2d 421 (Ind. App. 2004). An Oklahoma Court reached a similar conclusion in the Matter of Estate of Bruner, 864 P.2d 1289 (Okla. 1993). In Bruner, the court found that in the divorce property settlement agreement the parties agreed that "each should receive his own IRA account." According to the court, that language was sufficient to clearly indicate the former spouse had renounced her interest in the decedent's IRA.

Okla. Stat. tit. 15, § 178 provides that if after entering into a written contract in which a beneficiary is designated for the payment of a death benefit, including "retirement arrangements," the party to the contract with the power to designate the beneficiary dies after being divorced, all provisions in the contract in favor of the decedents' former spouse are revoked. Indiana has a similar law. Do statutes of this kind apply to individual retirement accounts? In Steiner, the Indiana court ignored the statute in reaching its decision. Bruner was decided before Oklahoma's statute became effective. Nevertheless, the conclusion one can draw from the case law in this area is that a prudent practitioner will include in any divorce property settlement agreement a specific waiver of benefits from any individual retirement account.

CHANCES OF FEDERAL AUDIT OF ESTATE TAX RETURN SHRINKING

In 1989, the chances that the estate tax return for an estate which exceeded $5 million would be audited were 51.3 out of 100. The likelihood of such an estate tax return being audited has been falling ever since. Forty-eight percent (48%) of the returns filed by these estates were audited in 1994; 27.81% in 2000. In 2003 there were 5,714 such returns filed, only 1,570 of which were audited (27.48%). In 2003, the average proposed deficiency on an estate tax return for an estate which exceeded $5 million was $524,425.

Audits of estate tax returns filed by estates smaller than $5 million were up slightly from prior years. In 2003, an estate tax return for an estate valued at less than $5 million but more than $1 million had a chance of audit of 7.4%; while in 2002, the chance of audit was 7.28%. In 2003, an estate valued at less than $1 million had a chance of audit of 2.61%; while in 2002, the chance of audit was 2.19%.

In 2002, the chance of a gift tax return being audited was .63%. In 2003, 1,855 of the 282,625 gift tax returns filed were audited (.66%).