

## Advanced Estate Plan Challenges for Second Marriages: QTIPs, Unitrusts, Disclaimers and More

TUESDAY, AUGUST 15, 2017

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

L. Paul Hood, Jr., Director of Planned Giving, **The University of Toledo Foundation**, Toledo, Ohio

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**Steve Leimberg's Estate Planning  
Email Newsletter Archive Message #2512**

**Date:02-Feb-17**

**Subject: Paul Hood on Tom Clancy's Estate: The Intersection of Estate Tax Apportionment and Blended Families, A Legal Thriller!**

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*This means that your client must describe his or her intentions to you relative to estate tax apportionment. You also can and should provide for whose share is charged with the expenses of administering the estate or trust, since those expenses can be significant. Again, client intent is critical here. After making some assumptions about tax rates and applicable exclusion amounts, there could be a significant multi-million dollar swing in what the surviving spouse and children would receive: the children or the surviving spouse will likely both fight each other and the executor and pursue your E&O carrier for that kind of change.”*

In [Estate Planning Newsletter #2250](#), **Bruce Steiner** reviewed the lessons that could be learned from Tom Clancy's will. Now, **LISI** closes the week with **Paul Hood's** analysis of the litigation Clancy's estate plan generated.

**L. Paul Hood, Jr.** received his J.D. from Louisiana State University Law Center in 1986 and Master of Laws in Taxation from Georgetown University Law Center in 1988. Paul is a frequent speaker, is widely quoted and his articles have appeared in a number of publications, including BNA Tax Management Memorandum, CCH Journal of Practical Estate Planning, Estate Planning, Valuation Strategies, Digest of Federal Tax Articles, Loyola Law Review, Louisiana Bar Journal, Tax Ideas and Charitable Gift Planning News. Presently, He has spoken at programs sponsored by a number of law schools, including Duke, Georgetown, NYU, Tulane, Loyola

(N.O.) and LSU, as well as many other professional organizations, including AICPA and NACVA. From 1996-2004, Paul served on the Louisiana Board of Tax Appeals, a three member board that has jurisdiction over all Louisiana state tax matters. Paul is co-author with **Steve Leimberg** of [The Tools & Techniques of Trust Planning](#) and [Tools & Techniques of Charitable Planning](#), which are published by The National Underwriter.

Here is his commentary:

## **EXECUTIVE SUMMARY:**

Estate planners can learn a number of important lessons from Tom Clancy's will and the litigation that it generated.

## **FACTS:**

Novelist Tom Clancy died on October 1, 2013, survived by his second wife, Alexandra, their minor daughter, and four adult children of his first marriage.

On October 10, 2013, his estate was opened; and Clancy's last will and testament, dated June 11, 2007, ("Original Will"), along with the codicils dated September 18, 2007 and July 25, 2013 ("Second Codicil"), were admitted to probate. J. W. Thompson "Topper" Webb, Esq., who was named in the Second Codicil, was appointed as personal representative. The Original Will and both codicils (collectively referred to as "the Will"), were drafted by the law firm of Miles & Stockbridge, P.C., where Mr. Webb is a partner.

The Original Will provided instructions on the payment of inheritance and estate taxes., and the codicils provided additional stipulations as to the disposition of Clancy's personal and real property and his residuary estate. The Will divides the residuary estate into three shares: (1) the Marital Trust, for the benefit of Alexandra; (2) the Non-Exempt Family Residuary Trust, ("Family Trust"), for the benefit of Alexandra and their daughter; and (3) two trusts (collectively referred to as the "Older Children's Trust"), for the benefit of Clancy's children from his prior marriage.

In the Original Will, Clancy provided for a three-way split of his residuary estate as set forth above. However, the Family Trust was not QTIPable for several reasons, i.e., in that it terminated on the earlier of Alexandra's death or remarriage, and it was for the immediate benefit of both Alexandra and their minor daughter.

The Original Will contained the following estate tax apportionment clause:

*All estate, inheritance, legacy, succession and transfer taxes (including any interest and any penalties thereon) lawfully payable with respect to all property includible in my gross estate or taxable in consequence of my death\_ shall be paid by my Personal Representative out of my residuary estate, subject, however, to the provisions hereinafter contained in Item SIXTH hereof with respect to the Marital Share therein created. [that item contained the following language: The Marital Share shall not be charged with or reduced by any estate, inheritance, succession or other tax of any kind.]*

According to the Orphans' Court opinion, the undisputed federal estate tax apportionment under the Original Will would have been:

Total Tax Liability: \$26.0M

Marital Trust:

Receives: \$21.25M

Tax Payment: \$0.0

Family Trust:

Receives: \$15.7M

Tax Payment: \$13.0M

Older Children's Trust:

Receives: \$15.7M

Tax Payment: \$13.0M

Two months prior to his death, Clancy signed the Second Codicil, which, *inter alia*, made the Family Trust QTIPable. The estate tax apportionment provision in the Original Will was not changed by the Second Codicil.

On September 5, 2014, Alexandra filed a Petition for Declaratory Judgment, Construction of Will, and Removal of Personal Representative. There were procedural disagreements as to whether the Orphans' Court possessed the jurisdiction to entertain a petition for declaratory judgment. However, the substantive disagreement was over the proper estate tax apportionment *vel non* of the Family Trust.

With respect to the procedural jurisdictional issue, the Orphans' Court sidestepped its lack of jurisdiction over declaratory judgment actions, which it held that it lacked, by interpreting the petition as a petition to interpret the will, over which it held that the court had jurisdiction.

The Orphans' Court then turned to the substantive issue of federal estate tax apportionment. The Orphans' Court noted that Alexandra's interpretation of the Second Codicil would have the following estate tax apportionment:

Total Estate Tax Liability: \$11.8M

Marital Trust:

Receives: \$21.25M

Tax Payment: \$0.0

Family Trust:

Receives: \$28.7M

Tax Payment: \$0.0

Older Children's Trust:

Receives: \$16.7M

Tax Payment: \$11.8M

The Orphans' Court noted that the executor's interpretation of the Second Codicil would have the following estate tax apportionment:

Total Estate Tax Liability: \$15.7M

Marital Trust:

Receives: \$21.25M

Tax Payment: \$0.0

Family Trust:  
Receives: \$20.8M  
Tax Payment: \$7.85M

Older Children's Trust:  
Receives: \$20.8M  
Tax Payment: \$7.85M

The parties disagree whether the amendment to Item Twelfth (D) of the Second Codicil ("Savings Clause") exempts the Family Trust from estate tax liability. The Savings Clause is set forth below:

*No asset or proceeds of any assets shall be included in the Marital Share or the Non-Exempt Family Residuary Trust as to which a marital deduction would not be allowed if included. Anything in this Will to the contrary notwithstanding, and whether or not any reference is made in any other provision of this Will to the limitations imposed by this Paragraph D, neither my personal representative nor my trustee shall have or exercise any authority, power or discretion over the Marital Share or the Non-Exempt Family Residuary Trust or the income thereof, or the property constituting the Marital Share or the Non-Exempt Family Residuary Trust, nor shall any payment or distribution by my personal representative or my trustee be limited or restricted by any provision of this Will, such that, in any such event, my estate would be prevented from receiving the benefit of the marital deduction as hereinbefore set forth. My Wife shall have the power at any time by written direction to compel my trustee to convert unproductive property held in the Marital Trust into income producing property. Likewise, my Wife shall have the power at any time by written direction to compel my trustee to convert unproductive property held in the Non-Exempt Family Residuary Trust into income producing property"*

The Orphans' Court correctly concluded that the Family Trust as set forth in the Original Will did not qualify for the federal estate tax marital deduction. However, Orphans' Court noted that the Family Trust was modified in the

Second Codicil in order to make it QTIPable and, further, that the executor made a QTIP election over the Family Trust.

The Orphans' Court framed the parties' disagreement over the Savings Clause as follows:

*[Alexandra] contends that the Savings Clause restricts the [executor] from requiring the Family Trust to contribute to the payment of estate taxes. [Alexandra] asserts that qualifying for the marital deduction necessarily restricts the payment of estate taxes as each payment of estate taxes causes the Family Trust to lose a portion of the marital deduction.*

*In opposition, [the executor] contends that the Savings Clause only reflects an intent for the Family Trust to qualify for the marital deduction, but has no effect on eliminating the Family Trust's liability on the payment of estate taxes. [The executor] asserts that the Tax Clause of Item Third (A) and Sixth is controlling and that the Savings Clause is only effective after the payment of estate taxes.*

The Orphans' Court spilled a lot of ink over the estate tax apportionment issue, discussing whether the Will set aside the Maryland estate tax apportionment law. On this issue, the Orphans' Court concluded as follows:

*Therefore, this Court make [sic] no determination whether Item Third and Sixth clearly and unambiguously set aside the apportionment statute, but shall accept Respondent's contention that Item Third and Sixth exhibit an intent to have estate taxes paid without apportionment for the remainder of my analysis, given the weight of the majority view and that the issue was uncontested by Petitioner.*

The Orphans' Court then turned its attention to the Savings Clause, concluding:

*This Court agrees with [Alexandra]. In my view, the Savings Clause is a valid interpretive aid savings clause. The Savings Clause is applicable to the entire will and is not dependent on a court ruling or IRS determination. Instead, it is a clear*

*expression of the testator's intent to have the Family Trust qualify for the marital deduction.*

The Orphans' Court further observed:

*[The executor] claims that qualifying for the marital deduction only ensures that the Marital Share and Family Trust are not included in the calculation of estate taxes, but has no effect on excluding them from the payment of estate taxes. This Court is not persuaded by [the executor's attempt to distinguish qualifying for the marital deduction and the payment of estate taxes as separate issues. Rather, this Court find [Alexandra's] construction more sound, as the cascading effect from the payment of estate taxes necessarily affects the calculation of estate taxes and causes the Family Trust to lose the "benefit" of the marital deduction, which the Savings Clause was intended to protect.*

The executor appealed to the Court of Appeals of Maryland. In a 4-3 decision, the majority telegraphed its decision by beginning with the famous quote from John Maynard Keynes: "The avoidance of taxes is the only intellectual pursuit that still carries any reward," holding in a *de novo* review that the Family Trust was exempt from federal estate tax apportionment.

The majority buttressed its opinion with Rev. Rul. 75-440 and the following rationale:

*Moreover, were the Family Trust to bear the burden of federal estate taxes, at the time of Mr. Clancy's death, the corpus of that trust would be subject to imposition of federal estate taxes twice, at the time of Mr. Clancy's death as well as when [Alexandra] died. The establishment of the QTIP Trust in Mr. Clancy's Will insures that the Younger Child will have to pay estate taxes when [Alexandra] dies. 26 U.S.C. § 2044. Certainly, as each party agrees, Mr. Clancy intended to minimize the impact of federal estate taxes in the entirety of his Will, an intent that would be eviscerated by double taxation.*

Thankfully, there was a spirited and well-reasoned dissenting opinion, which pointed out:

*The reading of the will urged by [Alexandra] would achieve a smaller additional tax reduction (from \$15.7 million to \$11.8 million), but would cast aside the plan for equal distributions from the residual despite the fact that the language of the will directing equal distributions was not amended -and skew the distributions from the residual in her favor (63% - 37%).*

*The Majority opinion opts for [Alexandra's] interpretation of the will -an interpretation in which an amended savings clause is construed to contradict basic terms of the original will that remained unchanged. However, we ordinarily read provisions of wills to be consistent unless there is no way to do so. In my view, the savings clause can be read consistently with the original will to achieve the tax savings for which codicil was intended without discarding the basic estate plan. Accordingly, I would adopt the reading of the will offered by [the executor].*

The dissenting opinion concludes:

*[Alexandra's] interpretation -adopted by the Majority opinion - would skew the distribution of the residual estate significantly in her favor contrary to basic provisions of the will while reducing the estate's tax liability somewhat more than what it would otherwise be. It does so by interpreting the Savings Clause to effect a radical change in the estate plan without any explicit direction to do so. The [The executor's] construction of the will and codicil would treat the Savings Clause for what it is -a savings clause -and maintain the equal distribution of the residual specified in the will, both originally and as amended, while achieving the significantly reduced tax liability that is the evident aim of the Second Codicil.*

*Even assuming that the Second Codicil could mean what the Majority opinion reads it to mean -which is far from clear -we ordinarily resolve textual ambiguities in favor of consistency, not inconsistency. Where there are two possible interpretations of a provision of a codicil, one which conflicts with the original will and one which does not, our precedents favor adoption of the interpretation that does not conflict. Thus, even if the Second*

*were ambiguous, it ought to be interpreted to be consistent with the original will rather than to contradict it.*

## COMMENT:

The Orphans' Court unnecessary statement at the outset of its opinion that the Will was inartfully drafted was uncalled for, conflicts with many of the Orphans' Court's own conclusions in its opinion and, in my opinion, simply is not true. In my opinion, both Maryland courts got this one wrong. In my opinion, the majority opinion out of Maryland's highest court is very intellectually soft, especially one coming from a state's highest court. The dissenting opinion simply and elegantly blows the majority's arguments and conclusion out of the water. This is, in my opinion, the most pernicious form of judicial meddling.

The majority's rationale of Clancy wanting to avoid double taxation as justification for its conclusion is dubious to say the very least. Just because the testator who creates a trust that is QTIPable doesn't require or otherwise mandate that the executor make the QTIP election over all or any part of it. The testator who creates a QTIPable trust actually cedes to his executor the discretion of whether or not to make the QTIP election. I fail to see much more sign of intent here.

The executor has to evaluate the totality of the circumstances in the QTIP *vel non* decision. While the QTIP election was in fact made over the Family Trust, in probable part because Alexandra was 21 years younger than Clancy, suppose that the executor in this case had decided not to make a QTIP election over the Family Trust. In that case, there doesn't seem to be any doubt that the Family Trust would have been burdened by its share of the federal estate tax.

So how is it that making the QTIP election automatically relieves it from **all** of its federal estate tax burden pursuant to the Will, especially where the Will expressly burdened the residue with the federal estate tax? The majority failed to address this critical point.

I distinctly recall a number of very similar situations, i.e., large taxable estates and blended families, where my clients in **every** such situation **expressly** favored paying **more** federal estate tax in order to **equally**

divide the estate between a subsequent spouse and the children from the prior relationship. The focus should have been on Clancy's **intent** rather than on a tortured reading of the Will.

Sadly, both courts seemed to overlook any extrinsic evidence of Clancy's **actual** intent. I doubt very seriously that he intended to slight his Older Children just two months prior to his death by skewing the distribution in favor of Alexandra and the minor child to such a significant degree. Clancy could have simply written the Older Children out before his death, but he didn't, indeed not changing their legacies one iota. In my opinion, Tom Clancy is probably turning over in his grave with this result.

There are important lessons to be learned from this case. Estate tax apportionment provisions often are included in the so-called boilerplate legalese in the document, but they might be the most important provision in that document, particularly with blended families. If you don't address estate tax apportionment in the client's will or trust, the state provides default estate tax apportionment rules, and **you must know them!**

This means that your client must describe his or her intentions to you relative to estate tax apportionment. You also can and should provide for whose share is charged with the expenses of administering the estate or trust, since those expenses can be significant. Again, client intent is critical here. After making some assumptions about tax rates and applicable exclusion amounts, there could be a significant multi-million dollar swing in what the surviving spouse and children would receive: the children or the surviving spouse will likely both fight each other and the executor and pursue your E&O carrier for that kind of change.

In this case, the will scrivener testified in favor of the Older Children's position, i.e., equal division and higher estate taxes, which should have borne much more weight than the courts ascribed to it. Yet the courts seemingly disregarded that testimony in favor of a very tortured reading of the Savings Clause, ascribing testamentary meaning to it since the effect of the Savings Clause changed the sharing ratios, which, in my opinion, is preposterous.

In blended families, it is not unusual for people to choose **higher** estate taxes over giving the surviving spouse more and their children less. In fact, it was my experience that this occurred often. Get clients to sign off on this.

Consider an example: suppose Al dies in 2016 with a \$50,000,000 estate in Ohio, a state with no death tax, and a federal estate tax rate of 40%, leaving 1/2 to his surviving spouse, Beatrice, and 1/2 to his children of a prior marriage, having \$100,000 in administrative expenses.

After the effect of the applicable exclusion amount, which in 2016 sheltered \$5,450,000 of assets from federal estate tax, if taxes come off the top, Beatrice and Al's children will each take \$20,075,000 and \$9,750,000 will go to estate taxes.

If taxes and administrative expenses come only out of the children's share instead, Beatrice will take \$25 million, Al's children will take \$17,120,000, and \$7,780,000 will go to estate taxes. As you can see, the total amount of federal estate tax goes down, but it dramatically impacts the sharing ratios. In this example, there is a negative swing of \$4,999,250 in what Beatrice takes, a positive swing of \$2,888,750 in what Al's children take, and an additional \$1,970,000 in estate taxes paid, just depending upon how the estate taxes are apportioned. (Numbers courtesy of NumberCruncher. [www.leimberg.com](http://www.leimberg.com)).

In large estates such as this one, the use of examples with real numbers in the estate planning documents themselves (as well as in the explanations) assuming a death today is helpful. It also can provide clear illumination of the testator's intent as well as ample CYA for the estate planner after a death, should either the surviving spouse or the children feel that they got slighted by the federal estate tax apportionment. And this is exactly how I drafted those particular estate planning documents in these situations.

However, in light of both courts' fixation on the Savings Clause, which all prudent estate planners include, query whether we should modify saving clauses to clarify that the testator's intent elsewhere **specifically** expressed, i.e., how federal estate tax is to be apportioned, is not somehow subordinated by the savings clause? This, in my opinion, would be too cute by half and should be unnecessary. However, you might run into misguided courts like these that might not see it that way.

An expression directly of **exactly** how federal estate tax is to be apportioned, together with numerical examples of its operation and a statement that the testator is aware that his direction will increase the total

amount of federal estate tax due, clearly, in my opinion, should override a general savings clause, which usually only is inserted out of an abundance of caution anyway. It strains credulity to consider that a marital deduction savings clause would have a substantive divisional impact, yet that is exactly what happened in the Clancy case, which is sad.

**HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!**

*Paul Hood*

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**CITES:**

*Bandy v. Clancy*, 144 A.3d 802, 449 Md. 577 (2016); *In the Matter of the Estate of Thomas L. Clancy, Jr.*, Estate Number 101962 (Orphans' Court for the City of Baltimore), August 21, 2015; Rev. Rul. 75-440; *Northeastern Pennsylvania Nat. Bank & Trust Co. v. U.S.*, 360 F.Supp. 116 (M.D. Pa.1973).