PLANNING FOR NONTRADITIONAL FAMILIES

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I. Introduction

The term "non-traditional family" is a catch-all phrase that includes unmarried couples, either homosexual or heterosexual, with or without children. It may include a stepfamily, children from the prior marriages or relationships of one or both of the partners, and possibly mutual children of the couple, as well. Sociologists sometimes refer to these new family units as: The unblended family, stepfamilies whose children move in and out of the home following various custody decisions; the nesters, whose children remain in the family home, while the parents move in and out on a schedule; the partially-blended family where blended families may share a duplex so that they aren't actually living in the same household, but connected ones; and the Living Apart Togethers (or L.A.T.'s): couples who maintain entirely separate residences.

Increasingly, American adults reside in a household as members of an unmarried couple. These couples may be heterosexual or homosexual, or they may not be involved romantically in any way, such as in the case of siblings or close friends.[1] While the topic of plural or polygamous marriage is beyond the scope of this outline, it should be recognized that that many individuals espouse the idea that marriage laws should not only be changed to allow any two adults to marry, but any number of consensual adults, and that many adults live in such arrangements (while not legal), creating challenging property rights, especially in community property states.[2]

State and federal laws contain default statutes giving spouses rights, including the right to handle funeral arrangements, rights under intestacy statutes, and Social Security survivor benefits. For the most part, unmarried couples -- unlike their married counterparts -- do not have a set of laws governing the division of property or providing for support payments upon the dissolution of their relationship. Children are particularly vulnerable when unmarried relationships end because of the different application of laws to unmarried couples.

In the estate planning realm, unmarried couples cannot take advantage of transfer tax marital deductions under Sections 2056 or 2523 of the Internal Revenue Code of 1986 (referred to herein as the "Code" or "IRC"), or gift splitting under IRC §2513. Members of unmarried couples may be subject to gift tax for supporting one another or dividing shared property. Unmarried couples must prepare wills or other estate planning vehicles to assure a distribution of their assets upon death in a manner different from that provided by the intestacy statute of the decedent's

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[1] *See* Ralph C. Brashier, *Inheritance Law and the Evolving Family* (Gender, Family, and the Law Series 2004) for an excellent examination of the historical and evolving concept of family as it relates to U.S. inheritance law.

[2] *See* Diane J. Klein, *Plural Marriage and Community Property Law*, 41 Golden Gate U.L. Rev. 33 (Fall 2010) for an analysis of the various type of plural arrangements and suggestions for statutory changes to accommodate these arrangements legally and equitably.

resident state. In addition, unmarried couples, especially same-sex couples, often experience legal difficulties when arranging funerals for deceased partners.

As with estate planning for any individual or couple, the issues may be divided into five categories: (i) practices to ensure that property is distributed appropriately; (ii) methods to minimize transfer taxes; (iii) charitable gift planning; (iv) planning for personal needs such as appointment of financial and healthcare decision-makers, funeral arrangements, guardianship and custody of minors; and (v) strategies to minimize conflict. Each of these topics will be dealt with below. This paper will begin with an examination of the current state of the law with respect to same-sex marriage, and a discussion of ethical issues in connection with the representation of unmarried couples.

Estate planning for the non-traditional family is only a special application of general estate planning principles and practices. However, unmarried couples often require a more individualized and resourceful approach to their estate planning. There are also a number of techniques only available to unmarried unrelated adults, and those opportunities will also be discussed. The purpose of this paper is not to provide a detailed analysis of particular technical aspects of estate planning. Instead, it focuses on various estate planning tools and the objectives that they accomplish, with an emphasis on their use in connection with planning for the client in a non-traditional family.

II. The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010

On December 16, 2010, Congress passed the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010, Pub.L. No. 111-312, 123 Stat. 444, which was signed into law by President Obama on December 17, 2010 (the "Act"). The Act significantly changes the federal estate tax, which impacts estate planning for many unmarried clients.

A. Estate Taxes.

Before the Act, the federal estate tax was gradually reduced over several years and then eliminated for decedents dying in 2010. Prior law provided that the estate tax, with a maximum tax rate of 55% and a $1 million applicable exclusion amount, would be reinstated after 2010.

The Act reinstates the estate tax for decedents dying during 2010, but at a significantly higher applicable exclusion amount of $5 million, and a lower maximum tax rate of 35%, than under prior law. This estate tax regime continues for decedents dying in 2011 and 2012. This new regime is itself temporary and is scheduled to sunset on December 31, 2012, with the prior estate tax regime (a 55% maximum estate tax rate and a $1 million applicable exclusion amount), scheduled to be reinstated.

The Act also eliminates the modified carryover basis rules for 2010 and replaces them with the stepped-up basis rules that had applied before 2010. Property with a stepped-up basis generally receives a basis equal to the property's fair market value on the date of the decedent's death. Under the modified carryover basis rules that applied during 2010 before the Act, executors could increase the basis of estate property only by a total of $1.3 million (plus an additional $3 million for assets passing to a surviving spouse), with other estate property taking a carryover basis equal to the lesser of the decedent's basis or the property's fair market value on the decedent's death.

B. Gift Taxes.

For gifts made in 2011 and 2012, the Act limits the maximum gift tax rate to 35% and increases the applicable exclusion amount from $1 to $5 million. This change provides an opportunity to move significant amounts of wealth free of estate and gift taxes during these 2 years. The annual gift tax exclusion continues to be $13,000 per donee.

C. Generation Skipping Transfer ("GST") Tax.

The Act provides a $5 million GST exemption amount for 2010 (equal to the applicable exclusion amount for estate tax purposes) with a GST tax rate of zero percent for 2010. For transfers made after 2010, the GST tax rate would be equal to the highest estate and gift tax rate in effect for the year (35% for 2011 and 2012). The Act also extends certain technical provisions under prior law affecting the GST tax.

III. Ethical Issues of Joint Representation

Like married couples, non-married couples tend to seek estate planning together. So long as the estate planning process is limited to planning for the care of their children and the disposition of assets upon death, and planning for incapacity, the interests of the two parties are not likely to conflict. However, the process often extends to consideration of current ownership and transfer of assets, which are areas in which each party may have potentially adverse interests.

Lawyers and clients are relatively free to define the nature of their legal representation: (i) individual representation; (ii) separate simultaneous representation of both members of a couple; (iii) joint representation; or (iv) intermediary representation.[3] When determining the appropriate type of representation, state ethics laws concerning conflicts of interest with current

[3] For a thorough analysis of the various forms of representation, *see* Jennifer Tulin McGrath, *The Ethical Responsibilities of Estate Planning Attorneys in the Representation of Non-Traditional Couples*, 27 Seattle U.L. Rev. 75 (2003).

clients should be considered. ABA 2007 Model Rule of Professional Conduct ["RPC"] 1.7(b) provides, in part, that:

> Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:
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> The lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
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> the representation is not prohibited by law;
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> the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
>
> each affected client gives informed consent, confirmed in writing.

A state's rules of professional conduct concerning confidentiality affect the extent to which the lawyer for joint clients may disclose to one client relevant information that was communicated to the lawyer by the other client. The fact that the goals of the clients are not identical does not necessarily create a conflict that precludes the lawyer from representing both members of the couple.

It is important to note that federal and state marital privileges, which generally bar a spouse from testifying as to any communications between spouses without the consent of the other spouse, do not apply to unmarried couples.[4]

A. Separate Representation.

> Separate representation by different attorneys presents serious limitations on either attorney's abilities to plan for a couple. Neither attorney has access to full and complete information for both parties. Thus, effective gift and tax planning is difficult, if not impossible. However, this may be the only model of representation available if clients are unwilling to share confidences with each other and where separate representation of both individuals is not possible because the attorney determines that the parties are directly adverse.

B. Separate Simultaneous Representation.

> Separate simultaneous representation of both individuals by one attorney is possible if the attorney determines that the clients will not be adversely affected by joint representation and they consent. However, it is likely that rather than enhance an attorney's ability to represent both clients, the risks of breaching the confidentiality of either client under separate

[4] *See, e.g.*, Wash. Rev. Code ["RCW"] 5.60.060(1).

simultaneous representation may hinder the attorney from representing either client effectively.

C. Joint Representation.

By far the most common form of representation is joint representation. RPC 1.7 requires an attorney to determine whether the interests of both parties may be met with this type of representation, and the attorney must believe that the potentially conflicting interests of the parties are subordinate to their common objectives.[5] As with married couples, while the interests of the two partners may not be adverse, the partners may not be in total agreement as to whether specific assets are separate property or community property. They may choose to make different beneficiary designations, before and after the death of the surviving partner. With this model of representation, the clients must consent to the sharing of information between them and the attorney, which substantially eliminates the risk that the attorney will violate the duty of confidentiality under RPC 1.6 by revealing confidences of one member of the couple to the other.[6]

D. Intermediary Representation.

Under certain circumstances, RPC 1.7 permits an attorney to represent two clients simultaneously, as the intermediary, if the attorney reasonably believes that this form of representation will benefit both clients, and will not materially prejudice either client.[7] However, the nature of the relationship is not as an advocate for either party. It is unclear whether representation as an intermediary may be provided within the scope of RPC 1.7 in the estate planning context; between two unmarried adults, it may be difficult to distinguish business planning from estate planning. Representation in this capacity is barred where litigation is a possibility or where negotiations are likely to be hostile.

E. Documentation of Form of Representation in an Engagement Letter.

Ideally, at the initial meeting with a client, the lawyer should describe the various models of representation available and determine what type of representation will best serve the client. An agreement as to the type of representation to be used should be memorialized in writing in the form of an engagement letter. A client's expectations of confidentiality, and any agreement or understanding concerning the lawyer's ability to disclose, should also be defined in the engagement letter. The letter should be signed by the attorney and countersigned by the client or clients.

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[5] McGrath, *supra* note 3, at 121.

[6] *Id.* at 122.

[7] *Id.* at 124.

In the absence of a shared understanding of the lawyer's relationship with the clients, the lawyer should presume joint representation, and that all confidences will be shared.[8]

IV. Same-Sex Marriage and The Defense of Marriage Act

A. The Defense of Marriage Act.

1. Federal Legislation.

The federal Defense of Marriage Act ["DOMA"],[9] specifically defines marriage as a legal union between one man and one woman as husband and wife. It further provides that a state shall not be required to give effect to any public act or judicial proceeding of any other state respecting marriage between persons of the same sex if the state has determined that it will not recognize same-sex marriages.

2. State Legislation.

To date, at least 41 states have adopted statutory versions of the DOMA, or have legislation banning same-sex marriage predating the federal DOMA, and most have constitutional provisions defining marriage.[10] Washington was the 36th state to adopt the DOMA in 1998, when it passed legislation defining marriage as a civil contract between a male and a female.[11] In 2000, California passed Proposition 22, adopting DOMA.[12] Illinois passed a statutory version of the DOMA in 1996.[13]

3. Challenges to DOMA.

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[8] *See* American College of Trust and Estate Counsel, *Commentaries on the Model Rules of Professional Conduct* 76 (4th ed. 2006); *Report of the Special Study Committee on Professional Responsibility: Comments and Recommendations on the Lawyer's Duties in Representing Husband and Wife*, 28 Real Prop. Prob. & Tr. J. 765, 771 (1994).

[9] Pub. L. No. 104-199, 110 Stat. 2419 (1996) (codified at 1 U.S.C. §7 and 28 U.S.C. §1738C).

[10] National Conference of State Legislatures, Same-Sex Marriage, Civil Union and Domestic Partnerships, www.ncsl.org/programs/cyf/samesex.htm (updated July 14, 2011).

[11] RCW 26.04.010(1).

[12] Codified at Cal. Fam. Code §308.5.

[13] 750 Ill. Comp. Stat. 5/213.1. *See* www.eqil.org/civil.html (last visited July 23, 2011) for a history of analysis of the Illinois civil union, including a discussion regarding the over 600 rights and responsibilities allowed to same-sex couples in an Illinois civil union.

There have been a number of failed challenges to DOMA, too numerous to mention.[14] But, on February 23, 2011, the Obama administration announced that the Justice Department would no longer defend the constitutionality of Section 3 of DOMA, which denies recognition of same-sex marriages for purposes of administering Federal law. Until this announcement, Obama's DOJ had been arguing to preserve DOMA for two years in courts all over the nation; but, government lawyers argue that they did this based on legal precedent, not moral obligation. Attorney General Eric Holder announced that the administration had concluded that government policies that discriminate based on sexual orientation must be subject to heightened scrutiny, and it had concluded that Section 3 could not survive such scrutiny because it does not serve any important government interest.[15]

Notwithstanding the position of the Executive Branch, Congress may defend DOMA in federal courts. Unless Congress repeals it or a federal judge throws it out, Section 3 of DOMA must remain in effect unless Congress repeals it or it is struck down judicially.

In the meantime, cases will continue to be argued at the state level, which may not necessarily be affected by the repeal except as a bellwether of the changing national opinion on the topic of same-sex marriage.

4. In Re Marriage Cases; Perry v. Schwarzenegger.

One ongoing state challenge is in California. The saga began on May 15, 2008, when the California Supreme Court issued its opinion in *In re Marriage Cases*, 183 P.3d 384, 76 Cal. Rptr. 3d 683 (2008), finding that the California Constitution mandates that same-sex couples have the right to marry. The Court held that reserving marriage for opposite-sex couples, while permitting same-sex couples only to enter into domestic partnerships, violates the state Constitution. In addition, the Court found that prohibiting same-sex couples from marrying deprives them of equal protection under the law.

The decision became effective and California began permitting same-sex marriage on June 15, 2008 until November 4, 2008. On November 4, 2008, Proposition 8, also known as the California

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[14] *See* Jerry Simon Chasen, *Is DOMA Doomed?,* 25 Prob. & Prop. 22 (Jan./Feb. 2011) for an analysis of recent challenges.

[15] U.S. Dept. of Justice Office, Statement of the Attorney General on Litigation Involving the Defense of marriage Act (Feb. 23, 2011), www.justice.gov/opa/pr/2011/February/11-ag-222.html.

Marriage Protection Act, which limits marriage to one man and one woman under California law, was passed, and then upheld by the California Supreme Court on May 26, 2009 in *Strauss v. Horton*.[16] But the approximately 18,000 marriages entered into on or before November 4, 2008 in California as well as marriages validly entered into elsewhere prior to that date, are considered valid. Marriages entered into after that date are recognized as domestic partnerships.

Cal. Fam. Code §308 was amended to provide that same-sex marriages validly entered into outside of California prior to November 5, 2008 remain valid in California, but same-sex couples who entered into marriage on or after that date will instead be treated as California registered domestic partners [hereinafter "RDPs"].

Then, *Perry v. Brown*, No. 09-2292 (N.D. filed May 22, 2009), originally filed in the U.S. District Court for the Northern District of California, challenged the constitutionality of Proposition 8. The Plaintiffs were led by a high profile team, including, among others, Theodore B. Olson, former United States Solicitor General under George W. Bush, and David Boies.

On August 4, 2010, the Court found Proposition 8 unconstitutional. Judge Vaughn Walker concluded that California had no rational basis or vested interest in denying gays and lesbians marriage licenses. He further noted that Proposition 8 was based on traditional and moral disapproval of homosexuality, and that those two things are not legal grounds for discrimination. He further noted that gays and lesbians are exactly the type of minority that strict scrutiny was designed to protect.

A Notice of Appeal was filed the same day by one of the Defendants to the U.S. Court of Appeals for the Ninth Circuit.[17] On February 16, 2011, the California Supreme Court accepted the request to determine whether Proposition 8 supporters have the authority under state law to defend a ballot measure when then-Attorney General and now Governor Jerry Brown, and then-Governor Arnold Schwarzenegger have both refused to sign on to the Proposition 8 repeal. The California Supreme Court has agreed unanimously to decide this question, in the case known as *Perry v.*

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[16] 207 P.3d 48, 93 Cal. Rptr. 3d 591 (2009).

[17] *Perry v. Brown*, No. 10-16696 (9th Cir. docketed Aug. 8, 2010).

Schwarzenegger, S189476, in that Court.[18] After that decision the case will return to the federal appeals court to be heard on its merits. This may not happen until 2012.

Sorting out the procedural issues could take years. Many assume this case will go to the U.S. Supreme Court, but the constitutional analysis in this case only applies to Proposition 8 and not to any other state's laws. But, the basis of the case, that prohibition of gay marriage is rooted in disapproval of homosexuality, could provide a solid basis for other state cases, but may not necessarily bring about the uniform results from one jurisdiction to the next.

Initially Judge Walker ruled that marriages could begin again in California on August 18, 2010, but he later delayed lifting the stay until the appeals process is completed.

5. Comity.

Generally, states are required by the U.S. Constitution and by federal law to give full faith and credit to the acts, records, and proceedings of other states.[19] There is a limited exception where the strongly held public policy of a state would be violated.[20] Thus, the DOMA allows states to refuse to grant full faith and credit to same-sex marriages, even if lawful in the state entered into.[21]

Same-sex marriages are currently recognized in 10 countries, most recently Portugal, as well as Argentina, Belgium, Canada, Iceland, the Netherlands, Norway, South Africa, Spain, Sweden, as well as

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[18] Another issue was raised as to whether Judge Walker should have recused himself because he has been in a long-term same-sex relationship. Chief U.S. District Judge James Ware upheld Judge Walker's decision. In his opinion he stated: "The sole fact that a federal judge shares the same circumstances or personal characteristics with other members of the general public, and that the judge could be affected by the outcome of a proceeding in the same way that other members of the general public would be affected, is not a basis for either recusal or disqualification." Order Denying Defendant-Intervenors' Motion to Vacate, *Perry v. Schwarzenegger*, No. 09-02292 (ND. Cal. June 14, 2011) ECF No. 797.

[19] U.S. Const. art. IV, §1. ("Full faith and credit shall be given in each state to the public acts, records, and judicial proceedings of every other state. And the congress may by general laws prescribe the manner in which such acts, records, and proceedings shall be proved, and the effect thereof.") *See* Joseph W. Singer, *Same Sex Marriage, Full Faith and Credit, and the Evasion of Obligation*, 1 Stan. J.C.R. & C.L. 1 (Spring 2005) for a thorough discussion of the application of the full faith and credit clause to same-sex marriage.

[20] *Pacific Emp'rs Ins. Co. v. Indus. Accident Comm'n*, 306 U.S. 493, 501, 59 S.Ct. 629, 83 L.Ed. 940 (1939).

[21] *See Restatement (Second) of Conflicts of Laws* §283(2) (1971), providing that a marriage will be recognized as valid if legal at the time it was entered into, unless it violates the strong public policy of another jurisdiction having the most significant relationship to the couple at the time they entered into the marriage.

a number of cities and regions (most recently Mexico City) in other nations.[22] Whether foreign same-sex marriages will be recognized within the United States is a separate issue. Comity is the recognition that one nation allows to the legislative, executive, or judicial acts of another nation. Comity is discretionary when recognition of foreign law does not violate public policy.[23]

Comity implies that the U.S. should recognize a foreign same-sex marriage if entered into legally.[24] But a state may use its DOMA as its rationale for denying legal recognition of a foreign same-sex marriage as against public policy.

B. Civil Union, Domestic Partnership, Designated Beneficiaries and Reciprocal Beneficiaries.

Civil union and domestic partnership are each a type of is a separate legal status providing a range of the rights and responsibilities afforded couples under state law. Some states provide limited rights and responsibilities and some are known as "everything but marriage" statutes. Civil union is currently available in Delaware,[25] Hawaii,[26] Illinois,[27] Maryland,[28] New Hampshire,[29] New Jersey[30] and Rhode Island.[31] Civil unions were

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[22] Freedom to Marry, www.freedomtomarry.org/states.php (last accessed Jan. 5, 2011). Countries that offer broad rights to same-sex couples, but not marriage, include Denmark, Finland, Germany, Iceland, Liechtenstein, New Zealand, Sweden, the United Kingdom, and Uruguay. Countries that offer fewer marital-like rights to same-sex couples include: Andorra, Austria, Brazil, Colombia, Croatia, Czech Republic, France, Hungary, Israel, Luxembourg, Portugal, Slovenia, and Switzerland.

[23] Generally, marriages that are valid in the place entered into are valid elsewhere unless recognition of such marriage would offend a strong public policy of the jurisdiction asked to recognize it. *Restatement (Second) of Conflict of Laws* §283(2) (1971).

[24] Bernard L. McKay, *Estate Planning for the Gay and Lesbian Couple*, 6 CCH Journal of Practical Estate Planning 43, 44 (Feb./March 2004).

[25] Delaware's Civil Union and Equality Act of 2011 (codified at Del. Code ch. 2, Tit. 13) (effective Jan. 1, 2012).

[26] 31 Haw. §572C-4, which extends the same rights, benefits, protections, and responsibilities of spouses in a marriage to same-gender or opposite-gender partners in a civil union. The laws take effect Jan. 1, 2012. Passage will not repeal or modify Hawaii's Reciprocal Beneficiaries law except to the extent an individual registered as a Reciprocal Beneficiary may not also register in a civil union.

[27] S.B. 1716, 96th General Assembly, entitled "The Illinois Religious Freedom Protection and Civil Union Act," as of June 1, 2011 provides more than 650 rights and protections, including automatic hospital visitation rights and the ability to make emergency medical decisions for partners; the ability to share a room in a nursing home; adoption and parental rights; pension benefits; inheritance rights; and the right to dispose of a partner's remain.

[28] Md. Code Health –Gen. §6-101.

[29] N.H. Rev. Stat. Ann 457-A (all existing civil unions converted to marriages on Jan. 1, 2011, and couples in a civil union or a relationship that provides substantially the same rights and responsibilities as marriage from elsewhere will be treated as married in New Hampshire).

available in Vermont until September 1, 2009, but existing civil unions do *not* automatically convert to marriage and the Vermont statute is silent on recognition of relationships from other states).[32]

Domestic partnerships are recognized by many employers and municipalities. In addition, the following jurisdictions maintain domestic partnership registries: California,[33] Maine,[34] Nevada,[35] New Jersey (in addition to civil union),[36] Oregon,[37] Washington,[38] and Wisconsin.[39] The rights and responsibilities of a domestic partnership vary greatly among jurisdictions.

In addition to civil union, Hawaii recognizes reciprocal beneficiaries. This status affords any couple not eligible to marry under the law a handful of rights and responsibilities, discussed below.

As of July 1, 2009, Colorado recognizes designated beneficiaries, who may enter into written contracts ensuring certain rights and financial protections as set forth in the agreement, which must be properly recorded to be legally enforceable.[40]

C. Marriage and Recognition of Marriage.

Connecticut,[41] Iowa,[42] Massachusetts,[43] New Hampshire[44] New York,[45] Vermont[46] and the District of Columbia[47] recognize marriage for same-sex couples.

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[30] N.J. Rev. Stat. §26:8A-1.

[31] H.B. 6103, 2011 Legislative Session (codified at R.I. Gen. Laws §§15-3.1-1 – 15-3.1-11).

[32] Vt. Stat. Ann. tit. 15, ch. 23 (effective Sept. 1, 2009) no new civil unions were permitted).

[33] *See infra* notes 53 - 63.

[34] Me. Rev. Stat. tit. 22, §2710 (establishing a domestic partnership registry); Me. Rev. Stat. Ann. tit. 18-A, §1-201(10-A) (defining domestic partner).

[35] Nev. Rev. Stat. §122A.100 (does not require Nevada residence and is available to same-sex partners and opposite-sex partners of any age).

[36] N.J. Rev. Stat. §26:8A.

[37] The Oregon Family Fairness Act of 2007 (codified at Or. Rev. Stat. §106.300).

[38] *See infra* notes 72 - 88 and accompanying text.

[39] Wis. Stat. ch. 770, The Domestic Partner Registry Act.

[40] Colo. Rev. Stat. §§15-22-101 – 15-22-112. *See* www.designatedbeneficiaries.org/index.html (last accessed June 17, 2011) for a downloadable form and a link to the site where the agreement can be registered.

[41] Conn. Gen Stat. §1-1m.

[42] *Varnum v. Brien*, 763 N.W.2d 862 (Iowa 2009).

A majority of states expressly bar recognition of out-of-state same-sex marriages.[48] While not valid if contracted for in Maryland,[49] New Mexico,[50] or Rhode Island, these states have held that marriages will be recognized by state agencies if solemnized elsewhere, where it is legal. Illinois and New Jersey treat same-sex marriages as civil unions. California treats them as domestic partnerships if entered into between

D. Common Law Same-Sex Marriage.

Until now, the concept of a common law same-sex marriage was academic. However, common law marriage is only recognized in 11 states and the District of Columbia, but other states recognize common law marriages lawfully entered into in other states.[51] Three of those jurisdictions, Iowa, the District of Columbia and New Hampshire, now recognize same-sex marriage, making the possibility of same-sex common law marriage a distinct possibility. While the standards in each of the 11 states are different, they generally require: (1) intent and an express mutual agreement to be married (some states explicitly require capacity by both parties to make such an agreement), (2) cohabitation, which in some states is also described as an exclusive relationship, and (3) the parties to the marriage must hold themselves out publicly as married to each other.

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[43] *See infra* notes. 70 - 71 and accompanying text.

[44] N.H. Rev. Stat. Ann. §§457-A:1, 457-A:6 (effective Jan. 1, 2010).

[45] "The Marriage Equality Act," 2011 N.Y. Laws ch. 95, as amended by 2011 N.Y. Laws ch. 96 (effective July 24, 2011) (codified at N.Y. Dom. Rel. Law §§10-a - 10-b).

[46] An Act Relating to Civil Marriage, 2009 Vt. Acts & Resolves 3 (codified at Vt. Stat. Ann. tit. 15, §§1201-1207).

[47] The Religious Freedom and Civil Marriage Equality Amendment Act of 2009, 57 D.C. Reg. 27 (Jan. 1, 2010) (effective March 3, 2010 with a 3-day waiting period so first marriages took place on March 6, 2010) (codified at D.C. Code §46-401 – 421). The District of Columbia previously recognized civil unions, until March 6, 2010.

[48] *Op. of Att'y Gen. Gary K King 11-01* at 2 (New Mexico Jan. 4, 2011).

[49] *Marriage – Whether Out-Of-State Same-Sex Marriage That Is Valid In The State Of Celebration May Be Recognized In Maryland*, 95 Op. Att'y Gen. Md. 3 (Feb. 23, 2010).

[50] *Op. of Att'y Gen. Gary K King* at 1. Notably the opinion states that marriages should be recognized not only for couples who marry legally in another state and later move to New Mexico, but also for New Mexico residents who travel out of state to marry and return. While an Attorney General Opinion is not binding on courts, but is often persuasive.

[51] *See* Peter Nicolas, *Common Law Same-Sex Marriage*, 43 Conn. L.Rev. 932 (Feb. 2011). *See also Common-law Marriage in the United States*, www.en.wikipedia.org/wiki/Common-law_marriage_in_the_United_States for a comprehensive history of common law marriage in the United States and Common-law Marriage, www.en.wikipedia.org/wiki/Common-law_marriage for a discussion on common law marriage worldwide.

Because the definition of "legal marriage" is not contemplated in any federal statute, it appears that at least heterosexual common law marriages are "legal marriages" for the purposes of DOMA. Rev. Rul. 58-66[52] recognized that if a marriage (including one under common law) is recognized by a state, then it will be recognized for federal purposes. However, it is likely that DOMA would trump this Revenue Ruling with respect to same-sex marriages.

Once married under common law, there is no common law divorce; a couple must go through a legal dissolution to terminate the relationship.

E. Same-Sex Marriage and Legal Relationships in Selected Jurisdictions.

California, Connecticut, Hawaii, Massachusetts and Washington are discussed in more detail below.

1. California.

a. Legislation.

California's statewide domestic partnership registry became effective on January 1, 2000.[53] As discussed below, California briefly permitted same-sex marriage in 2008.

Since January 1, 2002, California has offered domestic partner benefits to state employees, as well as a domestic partner registry.[54] California's domestic partner laws grant legal rights to same-sex couples (and to unmarried heterosexual couples age 62 years and older) who file a Declaration of Domestic Partnership with the Secretary of State.[55] Couples who register need not be California residents.

As of January 1, 2005, California's Domestic Partner Rights and Responsibilities Act of 2003 expanded the rights of domestic partners to include nearly all rights and also responsibilities of spouses under state law.[56]

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[52] 1958-1 C.B. 60.

[53] 1999 Cal. Stat. 588.

[54] 1999 Cal. Stat. 588, relating to domestic partners, added Calif. Fam. Code §§297-299.6, Calif. Gov't. Code §22770 (formerly Calif. Gov't. Code §22867), and Calif. Health & Safety Code §1261.

[55] Cal. Fam. Code §297.

[56] 2003 Cal. Stat. 421.

RDPs are afforded couples the same community property rights as married couples.[57] Unless opted out of, these rights are retroactive to the date the couple registered as domestic partners.[58] Because the gift tax marital deduction of IRC §2523 does not apply to domestic partners, the creation of community property may trigger a federal gift tax liability.

The California Franchise Tax Board has issued *Publication* 776 *Tax Information for Same-Sex Married Couples* (2010), which describes how couples married in California or in a marriage recognized during that time period by California, after 5 p.m. on June 16, 2008 and before November 5, 2008, are to report their state income.[59] As of January 1, 2007, California RDPs may file their *state* income tax returns as "married filing jointly," or "married filing separate."[60] Joint federal income tax filing is discussed below.

b. Termination of a California Domestic Partnership.

On October 1, 2010, Governor Schwarzenegger signed AB 2700, entitled the Separation Equity Act,[61] providing for a simplified procedure for same-sex couples who are both married and in a registered domestic partnership to dissolve both relationships in one proceeding. The Act also clarifies that California has jurisdiction to dissolve post-Proposition 8 out-of-state same-sex marriages.

For domestic partnerships of less than 5 years in duration, and not involving children, property interests or debt, and meeting a number of other requirements, the partnership may be dissolved by filing The Notice of Termination of Domestic Partnership, signed by both domestic partners, with the Secretary of State.[62] If the partnership does not meet all of the

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[57] Cal. Fam. Code §760.

[58] Opting out must be done in a written agreement similar to a premarital agreement, prior to becoming domestic partners, the form of which is governed by Cal. Fam. Code §§1600-1620. Cal. Fam. Code §297.5(k)(2).

[59] As of Oct. 11, 2009, SB 54 provides that a same-sex marriage validly entered into outside of California prior to Nov. 5, 2008 will be recognized in California; a marriage validly entered into on or after Nov. 5, 2008 will be treated as a valid marriage for all purposes under state law but will not be designated a "marriage."

[60] 2006 Cal. Stat. 802 (effective Jan. 1, 2007).

[61] Amending Cal. Fam. Code §299 & §2010, effective Jan. 1, 2011.

[62] Cal. Fam. Code §299(a). These requirements include, but are not limited to: neither of the domestic partners, to their knowledge, is pregnant; there are no unpaid obligations in excess of the amount permitted

requirements for a non-judicial dissolution, the superior courts have jurisdiction over the dissolution of a domestic partnership, as with marital dissolution.[63] As a result, all the rights and obligations that attach in marital status proceedings apply in the parallel domestic partnership status proceedings. These rights and obligations include (but are not limited to): (i) An equitable division of the partners' community property estate; (ii) a presumption that jointly titled property is community;[64] (iii) community reimbursement rights;[65] (iv) community and separate property debt liability; (v) spousal support, which includes consideration of the mandatory spousal support factors;[66] (vi) automatic temporary restraining orders; and (vii) granting, where appropriate, child custody, visitation and child support with respect to a child of the partnership or of either partner custody, and visitation and child support with respect to a child of a marriage or of either spouse.

2. Connecticut.

Connecticut was the first of a wave of northeastern states to recognize same-sex marriage. In October of 2008, the Connecticut Supreme Court ruled that same-sex couples have a constitutional right to marry.[67] The Court announced that sexual orientation is a quasi-suspect class under the Equal Protection clause of the State Constitution, and therefore it is entitled to a heightened level of scrutiny. The Court said that same-sex couples suffer a constitutional harm, and that a separate but equal scheme of civil unions did not pass constitutional muster. In its decision, the court emphasized that civil unions, permitted in that state pursuant to 2005 Conn. Acts 05-10, were not equal to marriage even though

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by Ca Fam. Code §2400(a)(6), as periodically adjusted, incurred by either or both parties after registration of the domestic partnership, excluding any unpaid automobile obligation; the total fair market value of community property assets (excluding encumbrances and automobiles), including any deferred compensation or retirement plan, is less than the amount specified in Ca Fam. Code §2400(a)(7), as periodically adjusted, and neither party has separate property assets (excluding encumbrances and automobiles) in excess of that amount; the parties have executed an agreement setting forth the division of assets and the assumption of liabilities of the community property, and have executed any documents, title certificates, bills of sale, or other evidence of transfer necessary to effectuate the agreement; the parties waive any rights to support by the other domestic partner; and both parties desire that the domestic partnership be terminated.

[63] Cal. Fam. Code §299(b).

[64] Cal. Fam. Code §2581.

[65] Cal. Fam. Code §2640.

[66] Cal. Fam. Code §§4300 – 4360.

[67] *Kerrigan v. Comm'r of Pub. Health*, 289 Conn. 135, 957 A.2d 407 (2008).

they shared all of the same rights and that the name itself was enough to offend Equal Protection. They also recognized that civil marriage has a long history in our culture, but civil unions are a recent construct. Therefore, the civil union scheme created in fact not an equal institution, but an inferior one. As of October 1, 2010, all existing civil unions automatically converted to marriages, no new civil unions are permitted, and couples in a civil union or a relationship that provides substantially the same rights and responsibilities as marriage from elsewhere will also be treated as married in Connecticut.

3. Hawaii.

While Hawaii now has a civil union statute,[68] Hawaii was the first state to adopt legislation granting equal rights to same-sex couples and their families in many areas of the law, in 1997, now known as "The Reciprocal Beneficiaries Act."[69] Additional rights have been granted since then.

Hawaii law allows same-sex couples to become "reciprocal beneficiaries." The Hawaiian legislation applicable to reciprocal beneficiaries is broken into three categories:

a. The first group conveys intangible, but great emotional, value. These include the ability to visit a partner in the hospital (Haw. Rev. Stat. §323-2), the right to make anatomical gifts on behalf of a partner (Haw. Rev. Stat. §327-3) and make medical decisions under certain circumstances (Haw. Rev. Stat. §323-2 and §327E-2).

b. The second group carries substantial value, and represents a commitment to provide rights substantially similar to those provided by marriage. These rights include equal inheritance rights (Haw. Rev. Stat. §560:2-301), rights to health insurance similar to married couples (Haw. Rev. Stat. §431:10A-601), other insurance benefits such as discounts to public workers (Haw. Rev. Stat. §87A-23(5)), general equality in many areas of retirement benefits (Haw. Rev. Stat. §88-1), the ability to bring a wrongful death lawsuit (Haw. Rev. Stat. §663-1 and

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[68] *See supra* note 26 and accompanying text.

[69] 1997 Haw. Sess. Laws 383. This Act represents the reaction of Hawaii's legislature to the decision in *Baehr v. Lewin*, 74 Haw. 530, 852 P.2d 44 (1993), in which Hawaii's Supreme Court found that there was no fundamental right to same-sex marriage under the Hawaiian Constitution, but it did determine that the marriage law denied the same-sex couples equal protection, in violation of art. 1, §5 of the Hawaii Constitution.

§663-3), the ability to own property in tenancy by the entirety (Haw. Rev. Stat. §509-2), and the same application of state estate tax as applicable to married couples (Haw. Rev. Stat. §560:3-916).

c. The third group grants rights of a more general nature with limited economic value or great value but limited application. These include the right to receive payment for saved up vacation days on behalf of a deceased public employee (Haw. Rev. Stat. §388-4), the right to paid bereavement time off for the death of a family member (Haw. Rev. Stat. §386-34), and the same eligibility for disaster loans as married couples (Haw. Rev. Stat. §209-28 & §209-29).

4. Massachusetts.

Massachusetts was the first state to recognize same-sex marriage. In *Goodridge v. Dep't of Public Health*,[70] the Massachusetts Supreme Court granted same-sex couples the right to marry as of May 2004. Massachusetts began issuing marriage licenses to same-sex couples on May 17, 2004. Those married couples have all of the rights and responsibilities of marriage under Massachusetts state law including the automatic right of inheritance, exemption from state inheritance tax, and child custody and visitation rights. On July 31, 2008 this right was extended to non-resident same-sex couples, even if their marriage would not be recognized in their state of residence. This repealed a 1913 law prohibiting marriages that would not be legal in the parties' state of residence.[71]

5. Washington.

In two cases brought by the ACLU in Washington, Washington's Defense of Marriage Act was ultimately found to be constitutional.[72] The first case, *Andersen v. King County*,[73] was brought by eight same-sex couples seeking the right to marry in Washington. Judge William L. Downing held in their favor and ruled that Washington's prohibition against same-sex marriage is

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[70] 440 Mass. 309, 798 N.E.2d 941 (Mass. 2003).

[71] Mass. Gen. Laws ch. 207, §11 (1913).

[72] Washington's DOMA defines marriage as a civil contract between a male and a female, and prohibits marriage for couples consisting of "other than a male and a female." RCW 26.04.020(1).

[73] No. 04-2-04964-4 SEA, 2004 WL 1738447 (King Cty. Super. Ct. Wash. Aug. 4, 2004), *rev'd*, 158 Wn. 2d 1, 138 P.3d 963 (2006).

an unlawful violation of the plaintiffs' constitutional rights to equality, liberty and privacy.[74]

Both sides agreed to a direct appeal to the Washington State Supreme Court, and the Order was stayed pending that review. The appeal was filed on September 1, 2004 and consolidated with *Castle v. Washington,*[75] in which the Court ruled in favor of eleven same-sex couples, and found the DOMA unconstitutional, in violation of Washington's Privileges and Immunities Clause.[76]

In the consolidated appeal, the State Supreme Court reversed the lower courts and found that the legislature is not prohibited from defining marriage as a civil union between a man and a woman, to the exclusion of same-sex couples.[77]

In response, Washington's legislature passed a domestic partner registry act that went into effect on July 22, 2007.[78] The legislature recognized that many Washington residents are in intimate, committed relationships with persons to whom they are not legally married, and many of whom are not permitted to marry. The legislature also recognized that these relationships benefit the individuals involved, and their families, by providing a source of mutual support for the financial, physical, and emotional health of those individuals and their families. The legislature concluded that the public has an interest in providing a legal framework for these relationships where the parties are unable to legally marry.

Same-sex couples did not have the same access (prior to the enactment of Washington's domestic partner registry) that married couples have to certain rights and benefits, such as those associated with hospital visitation, health care decision-making, organ donation decisions, and other issues related to illness, incapacity, and death. Furthermore, while many (but not all) of the rights granted by the 2007 bill could have been acquired by private agreement, doing so was often costly and complex.

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[74] *Id*. *Memorandum Opinion and Order on Cross Motions for Summary Judgment* at 22 (Aug. 4, 2004).

[75] No. 04-2-00614-4, 2004 WL 1985215 (Thurston Cty. Super. Ct. Wash. Sept. 7, 2004).

[76] Washington Constitution art. I, §12.

[77] *Andersen v. King County*, 158 Wn. 2d. 1, 138 P.3d 963 (2006) (*en banc*) Justice Barbara Madsen wrote for the plurality that "limiting marriage to opposite-sex couples furthers procreation, essential to survival of the human race, and furthers the well-being of children by encouraging families where children are reared in homes headed by the children's biological parents." *Id*. at 10.

[78] Laws of 2007, ch. 156, codified at RCW 26.60.

The legislature also recognized that it would benefit individuals and the public to extend domestic partnership rights to certain opposite-sex couples who are able to marry legally in Washington, but the loss of social security and pension survivor benefits make the financial cost prohibitive. For this reason, the protections of the bill were extended to these couples as well.

Accordingly, the Act allows certain same-sex couples and unmarried opposite-sex couples, one of whom is 62 or older, to register as domestic partners with the Washington Secretary of State as of July 23, 2007.[79]

Registrants must share a common residence, be over the age of 18 and members of the same gender, or one member of the couple must be over 62 for opposite-sex couples.[80] The parties cannot be married or a member of another domestic partnership.[81] The parties may not be related in a manner that would prohibit marriage and must have the mental capacity to consent.[82]

Declarations of state registered domestic partnerships are filed with the Secretary of State along with a filing fee.[83] The Secretary of State is required to post this list on the web page and send a copy of the list to partners along with the certificate of domestic partnership.[84]

Second Substitute House Bill 3104 passed March 12, 2008 and effective June 12, 2008, expanded and amended Washington's Domestic Partnership Act ["HB 3104"]. HB 3104 extended rights and responsibilities provided to spouses in various areas of law to state RDPs. These rights and responsibilities are generally in the areas of: dissolutions; community property; estate planning; taxes; court process; services to indigent veterans and other public assistance; conflicts of interest for public officials; and guardianships.

The 2008 Bill provided that a legal relationship between members of a *same-sex* couple, other than a marriage, created in a different state and that is substantially equivalent to a Washington domestic

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[79] RCW 26.60.030.

[80] RCW 26.60.030.

[81] RCW 26.60.030(3).

[82] RCW 26.60.030.

[83] RCW 26.60.040.

[84] *Id.*

partnership would be recognized in Washington.[85] This recognition does not extend to different-gender couples registered as domestic partners in another state. Accordingly, they would have to register in Washington to obtain recognition here. However, as of July 23, 2011, same-sex couples in a marriage validly formed in another jurisdiction will be recognized as a domestic partner in Washington.[86]

In 2009 the Original Act was again expanded, this time by E2SSB 5688 (the "2009 Expansion Bill"). The 2009 Expansion Bill extends the same rights and obligations to domestic partners under state law that are granted to or imposed on spouses.

Under the 2009 Expansion Bill, any privilege, immunity, right, benefit, or responsibility granted or imposed by state statute, administrative or court rule, policy, common law or any other state law to a person because he or she is a spouse, shall also be granted or imposed on equivalent terms, substantive and procedural, to a person because he or she is in a state-registered domestic partnership, to the extent not in conflict with federal law.

Language was added to the Revised Code of Washington stating that, except for RCW chapter 26.04 (marriage), the terms spouse, marriage, marital, husband, wife, widow, widower, next of kin, and family shall be interpreted to apply equally to state-RDPs and married persons, to the extent such interpretation does not conflict with federal law. The non-judicial termination process available to domestic partners is repealed.[87] Accordingly, to terminate a domestic partnership the parties must file for dissolution using the same process available to married couples under RCW ch. 26.09.

The 2009 Expansion Bill has a number of effective dates. Generally, it would have taken effect 90 days after adjournment of the session in which the bill is passed (August 1, 2009.[88] But Referendum 71, which attempted to repeal the 2009 Expansion Bill on the November 2009 statewide ballot, caused enactment to be put on hold. As a result, the effective date for the provisions scheduled to go into effect in 2009 was delayed pending the election. After passage of Referendum 71, the Act went into effect on December 3, 2009.

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[85] §1101, codified at RCW 26.60.090.

[86] RCW 26.60.090 (effective July 23, 2011).

[87] E2SSB 5688 §200.

[88] E2SSB 5688 §201.

New RCW 83.100.047(b), Washington's marital deduction statute, when effective in 2014, will provide, in part, that:

> The department shall provide by rule that a state RDP is deemed to be a surviving spouse and entitled to a deduction from the Washington taxable estate for any interest passing from the decedent to his or her domestic partner, consistent with section 2056 or 2056A of the Internal Revenue Code but regardless of whether such interest would be deductible from the federal gross estate under section 2056 or 2056A of the Internal Revenue Code.

Prior to the effective date it is likely that practical issues with the implementation of this statute are going to be uncovered.

F. Dissolution of the Same-Sex Marriage.

One of the thornier issues is how to deal with the inevitable dissolutions of same-sex marriages.[89] For some, getting divorced is fraught with more complexity than getting married.[90] The income tax issues are discussed in V below. While the couple may have, at one time resided in a state that would grant them a divorce, they may have moved since marrying, so that neither is a resident at the time they wish to end the marriage. This, in itself, is not a problem, unless their current state of residence has a DOMA that would prevent the state from recognizing the marriage, in which case they would be unable to obtain a divorce.[91]

Some states, like California, have a 6-month residence requirement for divorce for at least one member of the marriage. Most recently, Wyoming announced that while it would not recognize a same-sex marriage, it

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[89] An excellent resource for advising divorcing clients and couples is Raymond Prathers, *Considerations, Pitfalls and Opportunities That Arise When Advising Same-Sex Couples*, 24 Prob. & Prop. 24 (May/June 2010.

[90] Susan L. Pollet, *Breaking Up Is Hard[er] To Do; Same-Sex Divorce*, 83 N.Y. State Bar J. 10 at 13 (March/April 2011).

[91] *See e.g., In the Matter of the Marriage of J.B. and H.B.*, Case No. 05-09-01170-CV (consolidated with *In re State of Texas*, Case No. 05-09-01208-CV), (Texas App. – Dallas [5th Dist.] 2010) and Jamie Stengle, *Gay Divorce? Texas Says No*, Huffington Post (April 20, 2010) www.huffingtonpost.com/2010/04/20/gay-divorce-texas-says-no_n_543965.html?view=screen (last accessed Jan. 5, 2011) for a discussion of this case.

would grant a divorce.[92] New Jersey, while allowing for civil union, will recognize a marriage for the purposes of divorce, but no other purposes.

One option would be to rely on that lack of recognition, and request an annulment based on the fact that, pursuant to local law, it was never valid. This, however, would likely side-step any ability to seek spousal support as in a dissolution matter. It would also require a separate matter to be filed if there were parenting or property division issues. And it creates a new question as to whether it will be recognized as void in other states.

Another option is to obtain a legal separation, which does not have a residency requirement. This leaves the couple unable to enter into another marriage, however. Ideally, during the course of the legal separation, one member of the couple would establish residency in a state that recognizes the marriage, long enough to convert the separation to a dissolution action. There are, of course, due process limitations to this solution. So, a couple married in Massachusetts and living in Arkansas is not likely to be able to file for legal separation in California. But a couple married in California, living in Arkansas, should at least be able to file for a California legal separation. Also not clear is whether the California court would entertain a claim for spousal support in a legal separation action by a non-resident couple.

While mostly an academic issue at this point in time, some states still permit for cause divorce and 24 states and territories still have laws making adultery a crime.[93] However, it is not clear whether the definition of adultery would apply to conduct between same-sex individuals as a basis for a for cause divorce.[94]

V. Income Tax and Other Tax Ramifications of Same-Sex Marriage, Domestic Partnerships and Civil Unions

The Code essentially treats same-sex spouses as legal strangers. As a result, in many instances, but not all, same-sex couples are able to organize their financial affairs to reduce overall tax liability in ways that opposite-sex couples cannot.[95]

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[92] *Christiansen v. Christiansen*, 2011 WY 90, 2011 WL 2176486 {Wyo. Sup. Ct., June 6, 2011). In this case, involving a Canada Marriage, the Court held: "Respecting the law of Canada…for the limited purpose of accepting the existence of a condition precedent to granting a divorce, is not tantamount to state recognition of an ongoing same-sex marriage. Thus, the policy of this state against the creation of same-sex marriages is not violated" and reversed and remanded the matter to the trial court for further proceeding consistent with their opinion.

[93] Peter Nicolas, *The Lavender Letter: Applying the Law of Adultery to Same-Sex Couples and Same-Sex Conduct*, 63 Fla. L.Rev. 97, n. 19 and accompanying text (Jan. 2011).

[94] *Id.*

[95] *See* Theodore P. Seto, *The Unintended Tax Advantages of Gay Marriage*, 65 Wash. & Lee L.Rev. 1529 (2008) [hereinafter "Seto, *Unintended Tax Consequences*"].

The following is a summary of a few of the federal tax ramifications of legal stranger status.

A. Joint Return Filing.

The Code provides, in part, that "[A] husband and wife may make a single return jointly of income taxes under subtitle A."[96] In the Office of Associate Chief Counsel (Income Tax & Accounting) Chief Counsel Advice ("CCA") 200608038 (Feb. 24, 2006), the Service examined whether California domestic partners must file separate returns and report personal earnings separately, rather than 50% by each member of the couple, as with married couples in community property states. It concluded that domestic partners must file separate returns and report personal earnings separately. Then, in May 2010, the Service issued 2 rulings dealing with federal gift and income tax issues faced by same-sex couples who are RDPs under California law:

1. Chief Counsel Advice 201021050 (May 5, 2010).

On May 28, 2010, the Service released CCA 201021050 (May 5, 2010), reversing its ruling in CCA 200608038, recognizing community property rights for California RDPs.

The CCA instructs California RDPs that when filing their individual federal income tax returns each partner must report one-half of the community income on his or her federal income tax return. This CCA applies to tax returns filed for 2007 (the year California extended full community property rights to RDPs) forward and further instructs taxpayers who have filed federal tax returns for 2007, 2008 or 2009 under the previous CCA 200608038 (Feb. 24, 2006) that they may amend their prior year returns, but are not required to do so. Note that Treas. Reg. §1.31-1(a) allows prior withholding to be split but not estimated tax payments.

2. Private Letter Ruling 201021048 (May 5, 2010).

Also on May 28, 2010, the Service released PLR 201021048 (May 5, 2010), which is broader than CCA 201021050. Specifically, it provides that:

a. Taxpayer must report on his individual federal income tax return one-half of the combined income that Taxpayer and Domestic Partner earn from the performance of personal services

[96] IRC §6013(a).

and one-half of the combined income derived from their community property assets.

b. Taxpayer is entitled to half of the credits for income tax withholding from the wages of Taxpayer and Domestic Partner.

c. The requirement under California law to treat Taxpayer's earnings as community property, and thus half of Taxpayer's earnings as vested in his partner, *does not result in a transfer of property by Taxpayer to his partner for federal gift tax purposes under § 2501 of the Code*. (Emphasis added.)

Private letter rulings, technical advice memoranda, Chief Counsel Advice and similar written determinations of various divisions of the IRS hold little precedential value except with respect to the taxpayer to whom such publication was issued. Section 6110(k)(3) of the Code provides that a "written determination" may not be "used or cited as precedent." Section 6110(b)(1) of the Code defines the term "written determination" as a "ruling, determination letter, technical advice memorandum, or Chief Counsel Advice." Nevertheless, private letter rulings are often helpful in understanding the position of the IRS with respect to certain issues when a taxpayer faces a similar one but cannot rely on those rulings having any precedential value. However, a Chief Counsel advice, which is prepared by the National Office, does have weight *within* the IRS; where it is recognized by the IRS as providing correct and impartial interpretations of the internal revenue laws.[97]

In this case, the PLR and CCA are based on *Poe v. Seaborn*,[98] which since 1930 continues to be good law. In fact, some argue that a taxpayer should be able to rely on that case, without the necessity of the CCA or the PLR. On the other hand, in 2006, the Service announced in CCA 200608038, which has not been revoked, that *Poe v. Seaborn* does not apply to a state's community property law outside the context of a heterosexual married couple:

> The Supreme Court's decision in *Poe v. Seaborn* dealt with Washington's community property law, which applied to a husband and wife. We do not believe that the *Poe v. Seaborn* decision applies to the application of a state's community property law

[97] *See* IRM 33.1.3.1.1 (Definition of Chief Counsel Advice); IRM 4.46.1 (Overview of LMSB Guide for Quality Examinations).

[98] *Poe v. Seaborn*, 282 U.S. 101, 51 S.Ct. 58, 75 L.Ed. 239 (1930).

> outside the context of a husband and wife. In our view, the rights afforded domestic partners under the California Act are not "made an incident of marriage by the inveterate policy of the State." The relationship between RDPs under the California Act is not marriage under California law. Therefore, the Supreme Court's decision in *Poe v. Seaborn* does not extend to RDPs.

In December 2010, *IRS Publication 17* was amended to provide that "A registered domestic partner in California, Nevada, or Washington must report half the combined community income earned by the individual and his or her domestic partner."[99] Publication 17 refers the taxpayer to IRS Publication 555, which has also been amended to address the federal tax treatment of income subject to community property laws as applicable to RDPs domiciled in California (for tax years after 2006), Washington (where community property has also applied since June 12, 2008) and Nevada (as of 2009), as well as same-sex married couples domiciled in California in a recognized California marriage.

Attached as Exhibit A is a chart from IRS Publication 555, describing, in very general terms, the rules for allocating property as community or separate. Note that nonresident aliens may not split community property, and unemployment compensation is a wage replacement, so it should be treated as having the same character as the wages it replaces.

Unfortunately, Publication 555 contains contradictions, omissions and misinformation, a few of which are described below:

1. Publication 555 instructs RDPs to split W-2 income on line 7, the line for earned income, but doing so results in W-2 matching errors, as well as the erroneous appearance of eligibility for the earned income tax credit and IRA deductions for individuals who earned no income.

2. RDPs are being instructed to split self-employment income and taxes. Like the earned income tax credit contradiction, this can create mistakes with self-employment IRA contributions and health insurance deductions. IRC §1402(a)(5) clearly says that self-employment tax and the Social Security credits for paying that tax should be assessed solely against the person who runs the business.

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[99] IRS Pub. No. 17, at 5 (rev. Dec. 8, 2010).

3. The instructions are silent as to how to treat alimony/maintenance. In California, alimony/maintenance paid to an RDP is taxable to the recipient and deductible by the payor. But DOMA still prevents the federal government from treating same-sex couples as married, and therefore the treatment of federal rules for spousal support have not been amended to apply to same-gender couples.

4. The IRS has yet to provide clarification on the tax treatment of Social Security benefits. Social Security income is arguably community, but Publication 555 provides that earned income does not include Social Security or equivalent payments.

5. Publication 555 leaves unanswered how the same-sex couples married in other states who may have income derived from a community property state may file. Under DOMA, these relationships are not recognized, so it is not clear that these rulings would apply to them.

Form 1040 does not have a box to check to indicate that a legal relationship exists or that a partner will be filing a return reporting the other half of the earned income not reflected on that return. Therefore, it is recommended that taxpayers indicate that it is being filed pursuant to CCA 201021050. This raises another issue. The regulations at 31 CFR part 10.51, commonly known as Circular 230, governing the practice of taxpayer representatives before the IRS, have been amended by adding not e-filing to the list of "disreputable conduct."[100] Anecdotally many tax preparers are continuing to file manually along with a Form 8948 (Dec. 2010) "Preparer Explanation for Not Filing Electronically."

There are filing options married couples have taken to leave the opportunity open to amend returns at a later date as married filing jointly, if the unconstitutionality of DOMA is finally sorted out before the statute of limitations to amend has run:[101]

1. File protective refund claims.

2. Disclose their position regarding the right to file jointly on Form 8275 (Aug. 2008) or 8275-R (Aug. 2008).

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[100] TD 9527, IRB 2011-27 (July 5, 2011) regarding "¶10.51 Incompetence and Disreputable Conduct," http://www.irs.gov/irb/2011-27_IRB/ar06.html.

[101] Generally, 3 years from the date of filing. IRC §6511(a).

3. Footnote the filing single status of their Forms 1040 with the following: "The taxpayer is legally married under the laws of _____ and is reserving the right to amend the return should federal law recognize the marriage and the unconstitutionality of Section 3 of DOMA."

4. File returns as single individuals, then file an amended joint return based on the laws applicable to heterosexual couples, disclosing that they are a legally married same-sex couple and are making the claim on the basis that Section 3 of DOMA is unconstitutional. Presumably, their refund claim will be denied but they can then sue for a refund in district court.

B. Commuting Community Property to Separate.

Some couples may wish to enter into separate property agreements to avoid the requirement that community income vest equally in both members of the relationship and the associated filing requirements. However, transmutation of community property to separate property of the earning partner following registration could be treated as a gift from the non-earning partner back to the earning partner.[102] The transmutation of community income into the separate property of both partners in equal shares should not create any gift tax consequences, however.

C. State Income Tax Returns.

California, Connecticut, the District of Columbia, Iowa, Massachusetts, New Jersey, New York,[103] Oregon and Vermont allow same-sex partners to file joint income tax returns and estate tax returns where applicable.

Nevada, New Hampshire and Washington do not have individual income taxes. The Delaware, Hawaii and Illinois civil union laws were not in effect for the 2010 tax year do how these states will handle state returns is not clear.

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[102] Patricia A. Cain, *Planning for Same-Sex Couples in 2011*, 17 ALI-ABA Estate Planning Course Materials Jour. 5, 20 (June 2011) *citing* Rev. Rul. 75-551, 1975-2 C.B. 378.

[103] Same-sex married couples who are married as of Dec. 31, 2011 will be considered married for the entire year. They *must* file their returns using a married filing status starting in tax year 2011. The act is not retroactive for couples married elsewhere prior to July 24, 2011 (the first date marriage was permitted in New York). Technical Memorandum TSB-M-11(8)C, TSB-M-11(8)I, TSB-M-11(7)M, TSB-M-11(1)MCTMT, TSB-M-11(1)R, and TSB-M-11(12)S (July 29, 2011). The taxable estate of a decedent who died on or after July 24, 2011 in a marriage with a same-sex spouse must be computed in the same manner as if the decedent had been married for federal estate tax purposes. The same deductions and elections allowed for different-sex spouses are allowed for same-sex spouses, whether or not a Form 706 is filed.

Maryland, New York and Rhode Island recognize same-sex marriages performed in other states, even though they do not permit them. However, none of these states permits same-sex couples to file joint tax returns.

D. No Federal Tax Exemptions Upon Separation, Dissolution or Death.

There are generally no tax consequences for a division of property in the case of a heterosexual marital dissolution.[104] Transfers of property and payments between ex-spouses pursuant to a written settlement of marital property rights, or for support of minor children of the marriage, are deemed for adequate consideration, and therefore not a gift, even if the transferor did not actually receive adequate consideration in return for payments to the transferee.[105]

Transfers upon termination of a domestic partnership or other relationship not recognized because of the federal DOMA are not eligible for the federal tax exemptions that apply to married couples. But for the federal DOMA, these rules would apply to same-sex married couples if the relationship of the parties is legal in the jurisdiction where they reside. If the IRS does not recognize same-sex marriages, gain and loss could be recognized on the transfer of appreciated property, at the termination of the relationship.[106]

Furthermore, unlike in the marital dissolution context, at the termination of a domestic partnership maintenance payments will be taxed as ordinary income to the recipient and may not be treated as a deduction by the payor. [107] Maintenance may also be treated as a taxable gift.

Furthermore, the payment of an obligation at death to a surviving non-spouse is not deductible as a claim against the estate of the decedent partner, as it is between former spouses.[108]

E. Head-of-Household Status.

To qualify for head of household status, the following tests must be met with respect to the taxpayer:

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[104] IRC §1041.

[105] IRC §2516. The parties must divorce within the three-year period that begins one year before the agreement is executed.

[106] IRC §1001.

[107] Alimony or separate maintenance payments are included in the payee spouse's income under IRC §71(a) and the payor of the "alimony or separate maintenance payments" may claim a deduction for such payments under IRC §215.

[108] Treas. Reg. §20.2053-4(d)(5); IRC §2043(b)(2).

1. The taxpayer may not be married or be a surviving spouse at the end of the taxable year,

2. The taxpayer must maintain a household which constitutes the principal residence of a qualifying person (defined as a child, step-child, or a descendant of a child of the taxpayer, or any other person who is a dependent of the taxpayer under IRC §152[109]), if the taxpayer is entitled to a deduction for the taxable year for such person under IRC §151; and

3. The qualifying person must have lived with the taxpayer for more than half the year.[110]

It may be possible for one partner in a domestic partnership to claim head-of-household status for purposes of federal income tax.[111] IRC §152(f)(3) precludes an individual from being "a member of the taxpayer's household if at any time during the taxable year of the taxpayer the relationship between such individual and the taxpayer is in violation of local law."[112] So, head of household status does not depend upon whether a state recognizes a civil union, domestic partnership or marriage. Rather head of household status should be available unless that status is illegal under local law (most likely because it violates a state's cohabitation restrictions, which still remain on the books in some states.)[113]

F. Dependency Exemptions.

The Internal Revenue Code allows a taxpayer to claim a dependency exemption if: (i) the cohabitant receives 50% or more of his or her support from the taxpayer; (ii) is considered a household member of the taxpayer; and the (iii) relationship of the taxpayer and the cohabitant does not violate local law.[114] For purposes of the dependency exemption, a

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[109] IRC §152 was amended by §501(d) of P.L. 110-351, The Fostering Connections to Success and Increasing Adoptions Act of 2008, effective for tax years beginning after Dec. 31, 2008.

[110] IRC §2(b)(1)(A).

[111] IRC §2(b)(1)(A)(ii).

[112] IRC §152(f)(3). *But see infra* n. 113.

[113] *See* Fla. Stat. § 798.02; Mich. Comp. Laws Serv. § 750.335; Miss. Code Ann. § 97-29-1; S.C. Code Ann. § 16-15-60 (based on definition of fornication which includes cohabitation); Va. Code Ann. § 18.2-345. However, as the Supreme Court has struck down all laws prohibiting private sexual contact between consenting adults, it appears that domestic partnerships between persons of the same or opposite sex cannot be deemed a violation of local laws. *Lawrence v. Texas*, 539 U.S. 558 (2003). Accordingly, it is not clear that this requirement is enforceable.

[114] IRC §151(c), Treas. Reg. §1.151-1(a)(iv) and IRC §152(f)(3), which precludes an individual from being a member of the taxpayer's household if at any time during the taxable year of the taxpayer the relationship between such individual and the taxpayer is in violation of local law.

dependent is generally defined by IRC §152(a); non-relative dependents may be recognized if the taxpayer provides a majority of their financial support and they are not being claimed as dependents on another taxpayer's return.[115] Like head-of-household status, dependency exemptions are only allowed to cohabitants whose relationship does not violate local law.[116]

G. Obligation of Support.

Donative transfers between non-spouses may be taxable gifts if in excess of the annual exclusion, which is still $13,000 in 2011. Yet, parties to a domestic partnership or civil union have a legal obligation to support each other under state law. "The gift tax is not applicable to a transfer for a full and adequate consideration in money or money's worth."[117] But, support in excess of the annual exclusion from one partner in excess of the value received from the other may still be characterized as a gift under IRC §2503(b) or taxable compensation under IRC §61, even if required by state law.

In TAM 8135032 (June 1, 1981), the IRS suggests that where a legally enforceable obligation to support exists pursuant to local law, certain transfers would not be treated as gifts (however, the transfers at issue in this case were found not to be pursuant to legal obligations.) And in PLR 8225091 (March 25, 1982) the IRS determined that "to the extent that current income of the trust is applied in satisfaction of the donor's legal obligation to support or maintain his parents there is no gift."

H. Adoption Credits.

Generally, an adoption tax credit is available under IRC §36C, which allows the first $13,170 (for 2010) of adoption expenses for any taxpayer with adjusted gross income not in excess of $150,000 (the credit begins to phase out at incomes above $182,520; and is phased out completely at $222,520).[118] The credit is not available for expenses incurred in the adoption of a spouse's child if the spouse does not concurrently give up

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[115] *See* IRS Notice 2008-5, 2008-2 I.R.B. 256 (allowing a dependency exemption deduction for the child of the taxpayer's unrelated friend where the "friend" was not required by IRC §6012 to file an income tax return and did not, in fact, file a return). *See also Leonard v. Comm'r*, T.C. Summary Op. 2008-141, Docket No. 12719-07S, 2008 WL 4822173 (Nov. 4, 2008), where the Tax Court permitted a *pro se* taxpayer to take dependency exemption deductions for the two grandchildren of an adult woman with whom the taxpayer had been living for 11 years.

[116] Treas. Reg. §1.152-1(b), *but see supra* note 113.

[117] Treas. Reg. §25.2511-1(g)(1).

[118] Rev. Proc. 2010-35, 2010-42 I.R.B. 438.

parental rights.[119] A married couple is limited to one credit between the two of them. Furthermore, pursuant to Notice 97-9, when an unmarried couple jointly adopts the same child, they are also limited to a single adoption credit, split between them. However, when an unmarried individual adopts a partner's child, this is not a joint adoption, and an adopting partner with a qualifying AGI, should be eligible for the full credit.[120]

I. Taxation of Domestic Partner Benefits.

When an employer provides health insurance for the spouse or dependents of an employee, federal income tax law allows the value of the health insurance coverage to be excluded from the employee's gross income.[121] When an employer provides the same health insurance coverage for the partner or the dependents of the partner of an employee, the fair market value of that coverage, including the employee's pre-tax contributions, is treated as imputed income of the employee and must be reported by the employee.[122] Additionally, employees cannot use pre-tax dollars to pay for a domestic partner's coverage, precluding them from the full benefits of an FSA or HSA.

Because the imputed income increases the employee's overall taxable income, it also increases the employer's payroll taxes - the Social Security and unemployment insurance taxes. As a result, an employer's must pay higher payroll taxes for that imputed income as well.

However, if the employee's domestic partner is a qualifying dependent, the value of the health insurance coverage should be eligible to be excluded for federal tax purposes.[123] This also appears to apply to a same-sex Massachusetts, California or foreign marriage.

If partner A receives health insurance through partner B's employer, and pays income tax on the value of the insurance, it would not be a valid self-

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[119] IRC §36C(d)(1)(C).

[120] Seto, *Unintended Tax Consequences supra* note 95 at 1580.

[121] IRC §106(a).

[122] IRC §61(a) and Treas. Regs. §§1.61-21(a)(3) and (a)(4). See Patricia A. Cain, *Taxation of Domestic Partner Benefits: The Hidden Costs*, 45 U.S.F.L. Rev. 481 (Fall 2010).

[123] Treas. Reg. §1.106-1. A qualifying dependent is one that: (i) has the same principal place of abode as the employee; (ii) receives over half of his or her support from the employee (an employed domestic partner is likely to fail this test and the community property implications of registered domestic partners in Washington, California and Nevada also affect this test;, (iii) is not anyone's qualifying child; and (iv) is a citizen or nation of the U.S., or a resident of the U.S. or a country contiguous with the U.S. IRC §152(d).

employment health insurance deduction. The insurance plan must be established under partner B's trade or business.[124]

VI. Federal Preemption, Federal Benefits and Federal Programs

A. Background.

The Employee Retirement Income Security Act ("ERISA") §514(a), 29 U.S.C. 1144(a), provides that title I of ERISA supersedes all state laws insofar as they "relate to" an ERISA plan. Federal preemption over state law applies to assets such as Treasury bonds, and to federal pensions, ERISA regulated pensions, and Medicare and Social Security benefits.[125] Accordingly, there is no federal law basis for resolving state law domestic partnership ownership issues between current and former domestic partners. State law equitable remedies will need to be relied upon instead. However, employee benefits that are not part of an ERISA plan such as unpaid family leave, family use of employer facilities, family discounts and memberships, and similar fringe benefits are subject only to state regulation.

On June 2, 2010, President Obama signed an executive memorandum directing all federal agencies to extend fringe benefits to gay and lesbian employees, to the extent permitted by DOMA.[126] These benefits include long-term care insurance and expanded sick leave for civil service employees and medical care abroad, eligibility for employment at posts, relocation expenses, cost-of-living adjustments abroad and medical evacuation for domestic partners of foreign service members. It also requires agencies that extend any new benefits to employees' opposite-sex spouses to make those benefits available on equal terms to employees' same-sex domestic partners to the extent permitted by law.

B. Non-Spouse Rollover Provision for Retirement Plans.

Before 2007, inherited retirement plan benefits could not be rolled over to an IRA on a tax-free basis if the deceased participant's beneficiary was anyone other than a spouse.

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[124] IRS Pub. No. 502, at 23 (March 3, 2011).

[125] ERISA does not apply to certain plans, such as: federal, state or local government plans, including those of certain international organizations; religious or religious-affiliated plans; plans established by employee organizations such as unions; plans maintained solely to comply with state workers' compensation, unemployment compensation or disability insurance laws; plans maintained outside the United States primarily for non-resident aliens; and unfunded excess benefit plans, which are those that are maintained solely to provide benefits or contributions in excess of those allowable for tax-qualified plans.

[126] Office of the Press Secretary, The White House, "Statement by the President on the Extension of Benefits to Same-Sex Domestic Partners of Federal Employees," 2010 WL 2211943 (June 2, 2010).

Section 829 of the Pension Protection Act of 2006[127] ("PPA") added IRC §402(c)(11)(A), effective January 1, 2007, allowing a non-spouse designated beneficiary to directly rollover qualified retirement plan benefits, via plan-to-plan transfer, to an "inherited individual retirement account" (an IRA opened after the participant's death, in the name of the deceased participant payable to the beneficiary). In IRS Notice 2007-7 the Service provided that qualified plans were not required to allow such non-spouse beneficiary rollovers.

The Worker, Retiree and Employer Recovery Act of 2008 (WRERA)[128] contained technical corrections to the PPA — as a result, as of January 1, 2010, all qualifying plans are required to permit any non-spouse beneficiary to roll over inherited retirement benefits paid in the form of a lump sum to an inherited IRA on a tax-free basis.[129]Prior to January 1, 2010, a non-spouse rollover is not required by the sponsoring employer.

The new laws affect tax-qualified retirement plans — including defined benefit plans (pensions) that pay benefits in the form of a lump sum, 401(k) plans, employee stock ownership plans (ESOPs), profit-sharing plans and money purchase plans — as well as some 403(b) plans and governmental 457(b) plans.

The law is unsettled as to whether a non-spouse beneficiary of a traditional IRA may convert that inherited account to a Roth IRA.

C. Defined Benefit Plan Survivor Annuities.

ERISA mandates that qualified defined benefit plans make benefits payable in certain forms of distributions. A death benefit must be provided for an opposite-sex surviving spouse if the participant dies prior to retirement. The default benefit distribution form under ERISA for a single or non-married individual is a single life annuity. In contrast, when a participant is married, ERISA mandates that the default benefit distribution form be a qualified joint and survivor annuity ("QJSA") or qualified pre-retirement survivor annuity ("QPSA"), which guarantees the spouse of the employee a benefit in the event of the employee's death.

Because the federal DOMA defines a "spouse" as a person of the opposite sex, plans are not required to provide a QJSA or QPSA to the same-sex domestic partner or spouse of a participant. Employers are nonetheless free to provide such benefit payments for same-sex couples.

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[127] Pub. L.No. 109-280, 120 Stat. 780 (codified as amended in scattered sections of 26 U.S.C).

[128] Pub. L.No. 110-458, 122 Stat. 5092 (codified as amended in scattered sections of 26 U.S.C.).

[129] *See* IRS Notice 2008-30, IRB 2008-12.

D. QDROs.

For domestic partners, there is no federal provision for a qualified domestic relations order ("QDRO"), an order issued by a state court in a domestic relations proceeding, dividing retirement plan benefits held by an employee pursuant to a marital dissolution.[130]

While a state court (such as those of California and Washington) may issue a QDRO that purports to require a retirement plan to make distributions to a former partner in a dissolved domestic partnership, ERISA recognizes the rights of a spouse (among other persons) to receive all or a part of a participant's interest in a retirement plan, but not a domestic partner (*but see* the discussion of the *Owens* case below).

While retirement plans are generally required to make distributions in accordance with a QDRO, ERISA plans are not bound by state-court orders that conflict with ERISA, and federal DOMA provides that ERISA preempts the application of state law to retirement plans.[131] While an ERISA plan must follow a state court domestic relations order that qualifies as a QDRO, it is not likely that a domestic partner will be able to enforce a QDRO.[132] On the other hand, not complying with the terms of a QDRO could be grounds for a state law cause of action for contempt against the plan administrator. It is not clear whether a plan can be amended to recognize the rights of a domestic partner to a QDRO.

Generally, the anti-alienation provisions of ERISA protect a plan participant's benefits from being assigned to another party, except under limited circumstances, where the party meets the definition of an "alternate payee," and the order issuing such payment meets the criteria of a QDRO. ERISA defines the term "alternate payee" as any spouse, former spouse, child, or other dependent of a participant who is recognized by a domestic relations order as having a right to receive all, or a portion of, the benefits payable under a plan with respect to such participant. Whether an individual qualifies as a dependent is based on the definition found in IRC §152(d)(2)(H). IRC §152(d)(2)(H) defines the term "dependent" as "an individual (other than the spouse of the taxpayer) who, for the taxable year of the taxpayer, has the same principal place of abode as the taxpayer and is a member of the taxpayer's household."

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[130] ERISA §206(d)(3)(C)(i)-(iv) (now codified at 29 U.S.C. 1056(d)(3)); IRC §414(p)(2)(A)-(D) contains the requirements for a valid QDRO. *See* Albert Feuer, *Who is Entitled to Survivor Benefits from ERISA Plans?*. 40 J. Marshall L. Rev. 919 (Spring 2007) for a discussion of the requirements of domestic relations orders and QDROs.

[131] ERISA §514(s) (now codified at 29 U.S.C. §1144(a)).

[132] ERISA § 206(d)(3)(B)(i) (now codified at 29 U.S.C. 1056(d)(3)); IRC § 414(p)(1)(A).

In *Owens v. Automotive Machinists Pension Trust,*[133] the Ninth Circuit held that Norma Owens, who had been in a non-marital relationship with Phillip Owens for over 30 years, was entitled to half of Mr. Owens' monthly pension benefit pursuant to a valid QDRO. The Ninth Circuit Court recognized Norma qualified as an "other dependent" under IRC §152(d)(2)(H) and therefore an "alternate payee" pursuant to 29 U.S.C. §1056(d)(3)(B)(i)(I). Note, however, because the recipient of the QDRO interest is a dependent, not a spouse, Mr. Owens would be the taxpayer for the entire payment.[134] Had Ms. Owens been a spouse she would have been the proper taxpayer.

This case raises this issue as to whether the Ninth Circuit would recognize a same-sex married couple for purposes of dividing a qualified retirement plan pursuant to a QDRO in a dissolution, in instances where the non-employee spouse may be considered a "dependent" for purposes of meeting the definition of an Alternate Payee.

Another approach that has been successfully used by some practitioners is to obtain a domestic relations order or "DRO." This is an order issued by the court that binds the employee to share a percentage of his or her post-tax retirement payment when it is actually received, but is not binding on the plan administrator. A DRO would not violate ERISA, but it also requires the non-employee partner to wait for the employee partner to begin taking payments and perhaps seek specific performance. Further, the DRO might contain a provision that if DOMA related barriers ever cease to apply that it would be converted to a QDRO.

E. COBRA.

The Consolidated Omnibus Budget Reconciliation Act of 1985 ("COBRA")[135] requires most employers to offer certain former employees, retirees, spouses, former spouses, and dependent children, the right to temporary continuation of health coverage in the event that their coverage ends due to certain events such as divorce, job termination or a reduction in work hours.[136]

The Federal DOMA prevents same-sex domestic partners and spouses from being treated as spouses under COBRA.[137] Hence, COBRA benefits do not apply to a surviving or divorced domestic partner or that domestic

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[133] 551 F.3d 1138, 1141 (9th Cir. 2009).

[134] IRC §402(e)(1)A).

[135] Pub. L. No. 99-272, 100 Stat. 82 (1986).

[136] IRC §4980B; ERISA §601, §607 (now codified at 29 U.S.C. §1161, §1167)..

[137] IRC §414(p).

partner's dependents. Because COBRA's mandate is limited to dependent children, not dependents generally, domestic partners cannot fall under that prong of the definition. However, if a plan offers coverage to the children of a domestic partner, it may be possible that these children would be viewed as dependent children for purposes of COBRA. Note also that some state COBRA plans may also provide broader coverage than federal law

F. Social Security.

For purposes of determining eligibility, the Social Security Act defines a "child" by reference to the relevant state inheritance statute.[138] Accordingly, where state law provides that parentage laws apply to same-sex couples and married couples in the same manner, so that the natural child of one member of the relationship is deemed to be the child of the other for purposes of intestacy law, then the non-biological child of a member of the relationship is eligible for social security benefits based on his or her relationship to the non-biological member of the couple.[139]

Like California,[140] Oregon and Vermont, as a result of the 2009 Act, Washington now has a presumption of parentage for domestic partners. Under RCW 26.26.116, a person is presumed to be the parent of a child if that person and the mother of the child are registered and the child is born during the term of the registration, or within 300 days of the registration's termination by death, annulment, dissolution of marriage, legal separation, or declaration of invalidity. Therefore, there is now a basis for a child to obtain benefits based on a relationship to a disabled non-biological partner.

G. Domestic Partner Employee Benefit Hardship Withdrawals.

Employee benefit plans may allow a participant to withdraw funds from the plan due to certain financial hardships, which generally include unreimbursed expenses described in Treas. Reg. §§1.401(k)-1(d)(3)(iii)(B)(1), (3), or (5) (relating to medical, tuition, and funeral expenses, respectively), incurred by the participant, the participant's

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[138] 42 U.S.C. §416(h)(2)(A). A surviving spouse for purposes of Social Security survivor benefits is also determined based on recognition under state law, 42 U.S.C. §416(h)(1)(A)(i), resulting in disparate treatment for heterosexual couples where one member of the couple has undergone gender reassignment surgery either before or after the marriage.

[139] Steven N. Engel, Deputy Assistant Attorney General, Memorandum Opinion for the Acting General Counsel Social Security Administration, *Whether the Defense of Marriage Act Precludes the Non-Biological Child of a Member of a Vermont Civil Union from Qualifying for Child's Insurance Benefits under the Social Security Act* (Oct. 16, 2007), *available at* http://www.justice.gov/olc/2007/saadomaopinion10-16-07final.pdf.

[140] Cal. Fam. Code §297.5(d).

spouse or federally-defined tax dependents. Prior to enactment of the Pension Protection Act of 2006[141] (the "PPA"), an employee benefit plan could only allow a participant to receive a hardship withdrawal due to a financial hardship affecting the participant, a spouse or dependent of the participant. Section 826 of the PPA permits hardship withdrawals from a plan for certain expenses for a "beneficiary" under the plan, beginning on August 17, 2006.

A primary beneficiary is an individual who is named as beneficiary under the plan and has a right to all or a fraction of the participant's account balance following the death of the participant.

Section 826 of the PPA applies to most retirement plans, including 401(k) plans, 403(b) plans, 457(b) plans, employee stock ownership plans (ESOPs), profit-sharing plans, and nonqualified deferred compensation plans. It does not apply to defined benefit plans (pensions) or money purchase plans. Furthermore, state and local government 457(b) plans and nonqualified deferred compensation plans may permit hardship withdrawals only to pay for expenses associated with an unforeseeable emergency.

An employer is not required to permit hardship withdrawals. If an employer's plan has not previously permitted hardship withdrawals and the employer now wishes to do so, an amendment will be needed by the end of the plan year in which hardship withdrawals are first offered.

H. Flexible Spending Accounts and Health Savings Accounts.

Flexible Spending Accounts (FSAs), permitted under IRC §125 (often referred to as "cafeteria plans"), allow employees to use pre-federal-tax dollars to pay for medical and dental as well as dependent care expenses, for themselves, spouses or qualifying dependents as defined by IRC §152.[142] Medical expenses of a non-dependent domestic partner are not eligible for tax-free reimbursement from an FSA, even if the employer offers partner health insurance benefits. Nevertheless, while a domestic partner may not be given the opportunity to select or purchase benefits offered by the plan, a domestic partner may benefit from the employee's selection of family medical insurance coverage or of coverage under a dependent care assistance program.

An FSA may provide that plan participants may change their plan elections (including revoking a prior election) if there is a "change in

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[141] Pub. L. No. 109-280, 120 Stat. 780 (2006).

[142] *See supra* note 123.

status event." A change in marital status is a "change in status event."[143] But, because of the federal DOMA, a same-sex marriage, domestic partnership or civil union will not qualify as a "change in status event."

As with an FSA, medical expenses incurred by or on behalf of domestic partners (and their children) that are not qualifying dependents under IRC §152 are not eligible for tax-free reimbursement from a Health Savings Account (HSA) used in conjunction with high deductible healthcare plans. Similar change in status event rules apply as well.

I. Family Medical Leave Act (FMLA).

Under the Family Medical Leave Act,[144] enacted by Congress in 1993, certain employers with 50 or more employees must grant eligible employees up to 12 work weeks of unpaid leave during any 12-month period to care for a family member (as defined by 29 CFR 825.122), including newborn child, or a newly placed adoption or foster child, to care for an immediate family member (spouse, child, or parent) with a serious health condition; or when the employee cannot work due to a serious health condition. Under the FMLA, the term "spouse" is defined in 29 CFR 825.122(a) as "a husband or wife" as defined or recognized under state law for purposes of marriage in the state where the employee resides. However, the Act also contains a not consistently enforced "*in loco parentis*" provision.[145]

The Office of Personnel Management has since issued final regulations making it explicit that the *in loco parentis* provision allows federal workers to take leave to care for a stepchild as well as the child of an ill domestic partner or same-sex spouse.[146] The change adds explicit language to the interpretive regulations to the FMLA regarding the list of relationships that permit a federal worker to take leave to provide care or for bereavement. The changes do not apply to the Family and Medical Leave Act itself, which only Congress can change.

Until the DOMA is repealed, it is unlikely that an employee will be eligible for FMLA leave to care for a domestic partner.

VII. Wills, Revocable Trusts, and Nonprobate Transfers

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[143] Treas. Reg. §1.125-4(c)(2)(i).

[144] *Family and Medical Leave Act of 1993*, Pub. L. No. 103-3, 107 Stat. 6 (codified as amended at 29 U.S.C. §§2601-2654).

[145] 29 U.S.C. §2611(7) (2006).

[146] 5 C.F.R. pt. 630.201.

As indicated above, state and federal laws contain default statutes giving spouses various rights to a spouse's intestate estate, the right to handle funeral arrangements, rights under intestacy statutes, and Social Security survivor benefits, as well as the right to serve as a surrogate decision-maker. For the most part, unmarried couples do not enjoy these default rights. The estate planning documents discussed below are the same as those used for opposite-sex couples, with a additional, specialized drafting, to close the legal gap and avoid potential conflict.

A. Wills.

A testamentary gift to an unmarried partner, especially a same-sex partner, is often subject to challenge by the decedent's relatives.

There are certain powers that are often statutorily limited to exercise under a will, including: the ability to name a guardian of minor children[147]; the exercise of a testamentary power of appointment;[148] and gifts of tangible personal property by separate writing.[149] Thus, in some instances, having a will is critical. Under certain circumstances, other forms of testamentary transfers, such as joint tenancy with right of survivorship or revocable living trusts, both discussed below[150], may also be used as will substitutes.

B. Revocable Trusts.

Many clients establish revocable trusts to transfer assets to a partner outside of probate. Revocable trusts are also useful as vehicles for the management of a client's assets in the event of incompetence. Some practitioners advise that if a client anticipates that his or her will may be contested, it may be prudent to establish a revocable trust, which may be more difficult to challenge on theories such as incompetence or undue influence. If the estate is not taxable, then the beneficiary need not ever report receiving the gift. But, if there is a taxable estate, estate tax apportionment between family members and a surviving partner may compromise a beneficiary's ability to keep the receipt of assets entirely confidential from a decedent's family members.

C. Beneficiary Designations.

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[147] RCW 11.88.080. However, effective July 24, 2005, RCW 11.88.080 was amended to permit the designation of a guardian for a minor child in a durable power of attorney, effective either upon the death or incapacity of the parent/principal. This designation may also authorize an agent to make health care decisions on behalf of the minor if no other parent or legal guardian is available to give consent.

[148] RCW 11.95.060(2).

[149] RCW 11.12.260.

[150] *See infra* Sections XII.A.3 and VII.B, respectively.

Clients should confirm beneficiary designations for bank accounts, investment accounts, life insurance and retirement accounts. They may also consider restating those designations in their will or revocable trust as additional evidence in the event of a challenge by hostile family members.

D. Miscellaneous Considerations and Definitions.

With any estate planning document, definitions need to be carefully considered.

1. Partner.

In Washington, RCW 11.12.051 provides for the revocation of a provision in a will for a spouse upon divorce, and RCW 11.07.010 provides for the revocation of a beneficiary designation naming a spouse as beneficiary of certain nonprobate assets. No equivalent statutes apply to a partner upon separation. Therefore, it is important to define "partner" carefully. A partner may be "the person living with me at my death," but consideration should also be given to the possibility of temporary job relocation or one person having moved to a residential care facility.[151] One option is to provide specific guidelines for the personal representative, who would make a final and binding determination as to whether an individual was a partner at the time of death.

The following is an example of a definition of life partner where the parties have entered into a legal relationship:

The term "Life Partner" shall be deemed to mean _____, unless and until one of the following circumstances should occur:

a. If our Washington State domestic partnership registration is recognized in the state in which we are residing, and either of us files for dissolution, termination or annulment of such Washington State domestic partnership registration in a state that recognizes such registration; or

b. _____ and I marry, and subsequently either of us files for dissolution, termination or annulment of the marriage in a state that recognizes such marriage; or

c. _____ and I reside in a state that does not recognize the Washington State domestic partnership registration or a subsequent marriage of _____ and me, and I deliver

[151] Gail E. Cohen, *Estate Planning for the Unique Needs of Unmarried Partners*, 30 Est. Plan. 188, 189 (April 2003).

to the Personal Representative/Trustee a signed, written instrument declaring that _____ is not my Life Partner.

If a couple is in a legally recognized relationship, it is good practice to incorporate that fact into the definition. For example:

_____ and I were legally married in California on _____. Accordingly, throughout this Will, all references to _____ shall be construed as references to my "spouse" to the fullest extent of applicable federal, state and local law"

If the parties have not entered into a legal relationship but are cohabitants, the following could be used:

The term "Life Partner" shall be deemed to mean _____, unless and until one of the following circumstances should occur:

1. A written notice of the termination of our relationship has been provided by one of us to the other.

2. We are no longer residing together and either party has no intention of resuming the committed intimate relationship.

3. If we file for legal domestic partnership, civil union, or a similar legal status, and either of us files for dissolution, termination or annulment of such legal relationship in a state that recognizes such legal relationship.

4. _____ and I marry, and subsequently either of us files for dissolution, termination or annulment of the marriage in a state that recognizes such marriage.

5. _____ and I reside in a state that does not recognize a domestic partnership registration, civil union, a similar legal status, or a subsequent marriage of _____ and me, and I deliver to the Personal Representative/Trustee a signed, written instrument declaring that _____ is not my Life Partner.

6. Either party has filed a Petition for Dissolution of Relationship, Petition to Enforce Contract or Petition to Dissolve a Registered Domestic Partnership or any like lawsuit.

If any of the foregoing occurs, _____ shall be treated as if she predeceased me.

Alternatively, an adaptation of the New York statutory definition of a domestic partner (based on criteria originally set forth in *Braschi v. Stahl Assocs. Co.,* 74 N.Y.2d 201, 543 N.E.2d 49, 544 N.Y.S.2d 784 (1989)) set forth in New York Public Health Law §4201, which defines the priority of persons entitled to make funeral arrangements for a decedent, may also provide a useful starting point for defining a domestic partner.[152] New York Public Health Law § 4201(c) provides, in part, as follows:

> "Domestic partner" means a person who, with respect to another person:
>
> i. is formally a party in a domestic partnership or similar relationship with the other person, entered into pursuant to the laws of the United States or any state, local or foreign jurisdiction, or registered as the domestic partner of the person with any registry maintained by the employer of either party or any state, municipality, or foreign jurisdiction; or
>
> ii. is formally recognized as a beneficiary or covered person under the other person's employment benefits or health insurance; or
>
> iii. is dependent or mutually interdependent on the other person for support, as evidenced by the totality of the circumstances indicating a mutual intent to be domestic partners including but not limited to: common ownership or joint leasing of real or personal property; common householding, shared income or shared expenses; children in common; signs of intent to marry or become domestic partners under subparagraph (i) or (ii) of this paragraph; or the length of the personal relationship of the persons.

2. Parent and Child.

Similarly, the terms "children" and "descendants" should be defined to include children of a partner, who are neither biologically related nor adopted, but whom the testator intends to provide for. It should also be kept in mind that anti-lapse statutes may not protect descendants of a predeceased child of a partner.[153] Furthermore, a client may still want to provide for those children even if the relationship with the partner has ended.

Assisted conception raises a number of moral, ethical as well as legal issues for clients. The definition of "parent" and "child" should also be carefully considered when science may have made

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[152] *Id*. at 1-2.

[153] *See, e.g.,* RCW 11.12.120.

those definitions ambiguous. One issue that must now be considered is whether any genetic material has been stored, and what the plans are to use that material to conceive children. The law is inconsistent from state to state with respect to children conceived after the death of a parent.[154]

The following is one form of provision that could be used, which takes into account the statutory presumption of parentage in the first paragraph and assisted conception in the second:

> The term "descendants" shall mean all naturally born or legally adopted descendants of the person indicated. For the purpose of this instrument, a second-parent adoption or joint adoption by a same-sex couple, or parent/child status granted by state law to children born during a domestic partnership, civil union, or marriage, shall be considered a valid legally effective parent/child relationship. For the purpose of this instrument, all children or descendants deemed children or descendants of the person indicated by a civil union, domestic partner registration or marriage entered into by the person indicated shall be considered children or descendants.
>
> My partner, _____, (sometimes referred to hereafter as "____"), and I are planning to have children through assisted reproductive technology and/or a surrogacy arrangement ["ART"]. ____ and I agree, and both intend, that any child conceived by, born to (through ART), or adopted by either or both of us at any future time shall be deemed for all purposes to be the child of both of us from the moment of conception, regardless of whether the child has yet been born, or whether we are both named as parents on the child's birth certificate, or whether any legal proceeding has been commenced or completed to have us both recognized as the legal co-parents of said child. For purposes of this instrument, any reference to "my child", "my children" or "child of mine", shall include any biological or adopted child of mine or of ____ or of both of us, even while such child is *in utero,* and all children born as a result of an IVF embryo transfer or surrogacy arrangement we may have entered into during my lifetime.

3. Tax, Debt and Expense Allocation.

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[154] Bass, *infra* note 203, at 21.

Another important component of an estate plan is the tax, debt and expense allocation clause in the will or revocable trust. Estate plans often allocate tax, debts and expenses of administration to the residue. Alternatively, a plan may rely on the state's default statutes,[155] which generally provide that each beneficiary of an asset will bear a pro rata share of taxes and expenses of administration.

The effect of the state statute regarding abatement of assets to pay tax, debts and expenses should also be considered when drafting a will or revocable trust.[156]

Even when a client elects to rely on a state's default allocation rules, because of the migratory nature of clients and the fact that the laws of multiples states may apply, the client's intent should be clearly stated in the testamentary documents.

4. Drafting for the Marital Deduction.

Consider drafting documents in anticipation of a state and federal marital deduction. It is possible to direct that, to the extent a marital deduction is *not* taken by the fiduciary, assets instead would be distributed to a credit trust, providing discretionary income provisions, or even outright, rather than to a trust containing mandatory income distribution as required in a marital trust. This is often referred to as a Clayton contingent QTIP trust.[157] Or, rather than a mandatory marital deduction, a credit trust could be drafted to qualify as a marital trust, only to the extent a marital deduction is taken.

VIII. Planning for Personal Needs

Because most unmarried partners, unless they are in another type of legally recognized relationship, do not have the benefit of a legal family relationship, it is important that they name agents to make financial and health care decisions while they are alive, and for burial decisions at death. As with the documents discussed above, each of these documents requires additional considerations not necessarily applicable to married couples.

Most states recognize a hierarchy of individuals who may make decisions for an incapacitated person in the absence of a directive.[158] For example, in

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[155] *E.g,*. RCW ch. 83.110A, Washington Uniform Estate Tax Apportionment Act.

[156] *See, e.g.*, RCW ch. 11.104A, Washington's Principal and Income Act of 2002; RCW ch. 83.110A, Washington's Uniform Estate Tax Apportionment Act; and RCW 11.10.010, Washington's general abatement scheme that applies when no other specific rule applies.

[157] In response to *Est. of Clayton v. Comm'r*, 976 F.2d 1486 (5th Cir. 1992) the Service issued regulations allowing a surviving spouse's income interest in a trust to qualify for QTIP treatment, contingent on a fiduciary's election accordingly, and allowing that portion of the property for which the QTIP election is not made to pass to the surviving spouse and/or other beneficiaries (e.g., a credit shelter trust). Treas. Reg. § 20.2056(b)-7(d)(3).

[158] *See* Rebecca K. Glatzer, *Equality at the End: Amending State Surrogacy Statutes to Honor Same-Sex Couples' End-of-Life Decisions*, 13 Elder L.J. 255 (2005) for an examination of the many statutory approaches to surrogate decision making for same-sex and unmarried couples.

Washington, in the absence of a medical power of attorney, RCW 7.70.065 provides that the following individuals may give informed consent on behalf of an individual unable to consent, which includes: (i) the patient's spouse or RDP; (ii) children of the patient who are at least eighteen years of age; (iii) parents of the patient; and (iv) adult brothers and sisters of the patient.

Few state laws to give any authority to an *unregistered* domestic partner, although some will recognize them as a "close friend" who will be called upon only when nobody else in the hierarchy is available.[159] New York is one of the few states to have adopted a surrogate decision-maker statute that recognizes individuals in an intimate (but not legally recognized) relationship to be on par with a spouse, with respect to decision-making authority involving an incapacitated partner.[160]

A. Durable Powers of Attorney and Guardianship.

The durable power of attorney grants another person (the "attorney-in-fact" or "agent") the authority to act on the principal's behalf during the principal's life, including any periods of incapacity. Generally, the principal executing the durable power of attorney would designate his partner as primary attorney-in-fact and one or more alternate attorneys-in-fact if the partner is unable or unwilling to serve. The primary advantage of this document is that it avoids the need for expensive, cumbersome guardianship proceedings in the event of disability. As with testamentary documents, clients should be aware that a durable power of attorney designation is not revoked by the termination of a relationship.

In Washington, certain powers must be specifically stated in the power of attorney in order for the attorney-in-fact to be authorized to perform such acts.[161] The powers that may be especially important for the unmarried couple, include the powers to:

1. Execute, amend or revoke any trust agreement;

2. Fund, with the principal's assets, any trust not created by the principal;

3. Make a gift from the principal;

4. Create or change survivorship interests in the principal's property or in property in which the principal may have interest;

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[159] Timothy F. Murphy, *Surrogate Health Care Decisions and Same-Sex Relationships*, 41 Hastings Ctr. Rep. No. 3, 24-27 (May-June 2011).

[160] "Surrogate Decision-Making" 2010 N.Y. Laws, Art 29-B, §2965.

[161] *See* RCW ch. 11.94 (Washington's power of attorney statute).

5. Designate or change the designation of beneficiaries to receive any property, benefit or contract right on the principal's death;

6. Give consent to an autopsy or postmortem examination of the principal;

7. Make a gift of the principal's body parts under the Uniform Anatomical Gift Act;

8. Give consent to, or prohibit, any type of health care, medical care, treatment or procedure; or

9. Direct the withholding or withdrawal of artificially supplied nutrition or hydration.

A durable power of attorney may be used to nominate a guardian and alternates, in the event the appointment of one is necessary.[162] In the absence of a power of attorney (or in the absence of a durable power of attorney nominating a guardian, if one is necessary), the court may appoint any person it finds suitable as guardian, which may not be the person the principal may have considered most suitable while still competent.[163]

A "springing" durable power of attorney (one that takes effect upon the disability or incompetence of the principal) may be problematic as a result of the HIPAA regulations concerning the confidentiality and disclosure of health care information.[164] A typical springing durable power of attorney requires an opinion of a health care professional as to disability or incompetence to be effective. However, HIPAA may prevent a physician from disclosing medical information without the authorization of the patient, who would not be able to give a valid authorization if already incompetent. To avoid this Catch-22, a durable power of attorney could be effective immediately, or the principal could either execute a separate HIPAA authorization or the durable power of attorney should contain a HIPAA authorization to allow a physician to disclose protected health information for purposes of the springing power to be effective.[165]

B. Medical Powers of Attorney.

The Medical Power of Attorney, sometimes called a Durable Power of Attorney for Health Care, is a statutory form in each state that allows

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[162] RCW 11.88.010(4).

[163] RCW 11.88.020.

[164] 45 C.F.R. §§164.500-.534.

[165] *Id.* RCW 70.02.030 sets forth the requirements for a valid authorization to disclose the health care information of the principal.

patients to select a surrogate decision-maker to make certain medical decisions when patients are temporarily or permanently unable to communicate or make such decisions. A medical power of attorney should specifically grant a partner visitation rights and the power to control other visitors, in order to eliminate visitation by hostile family members.

On April 15, 2010, President Obama issued a memorandum to the Secretary of Health and Human Services directing rulemaking to ensure that hospitals respect the right of patients to have and designate visitors. He also directed the Secretary to issue guidance that clarifies existing regulatory requirements at 42 CFR 482.13, governing the right of a patient's representatives to make informed decisions concerning the patient's care, and 42 CFR 489.102(a), concerning advance directives, such as durable powers of attorney and health care proxies.[166] On January 18, 2011, new regulations went into effect providing that hospitals participating in Medicare or Medicaid respect the rights of patients to designate visitors.[167] Hospitals are now required to have written policies and procedures detailing patients' visitation rights, as well as the circumstances under which the hospitals may restrict patient access to visitors based on reasonable clinical needs. Visitors chosen by the patient (or his or her representative) must be able to enjoy "full and equal" visitation privileges consistent with the wishes of the patient (or his or her representative). Furthermore, hospitals covered by these rules must ensure that they do not deny visitation privileges based on factors including sexual orientation or gender identity, and they must explain to all patients their right to choose who may visit them during their stay.

C. Health Care Directives.

The health care directive, also known as an advance directive or "living will," is a statutory document authorizing the withdrawal or withholding of life-sustaining procedures for a terminal condition if death is imminent.[168] It may include provisions regarding the withdrawal or withholding of hydration and intravenous nutrition, as well as intubation and cardiopulmonary resuscitation in the event of a terminal or irreversible

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[166] *See* http://www.cms.gov/SurveyCertificationGenInfo/PMSR/itemdetail.asp?filterType=none&filterByDID=0&sortByDID=3&sortOrder=descending&itemID=CMS1251864&intNumPerPage=10 for a copy of the announcement and further information.

[167] 42 CFR §482.13. The regulations have no impact on who may serve as a surrogate medical decision-maker on behalf of a patient who is unable to make decisions for him or herself.

[168] Washington Natural Death Act, RCW ch. 70.122; Wis. Stat. ch. §154; ORS 127.531. *See* www.noah-health.org/en/rights/endoflife/adforms.html (last updated Aug. 3, 2011) for printable state forms. No representation is made as to the accuracy of these forms.

condition.[169] In the absence of a directive, the wishes of the principal may not be able to be carried out, or even known.

D. Mental Health Directives.

In some states, including Washington, a medical power of attorney may also be used to allow a mentally ill person to express his or her preferences regarding mental health treatment from psychiatrists and other mental health care professionals.[170] The mental health advance directive allow individuals to bind themselves to psychiatric treatment in advance of needing it for the purpose of overcoming illness-induced refusals of treatment Between 1991 and 2006, 27 states enacted statutes authorizing psychiatric advance directives in some form.[171] Because they do not deal with end of life decisions, they are not covered in greater detail here.

E. Physicians Orders for Life Sustaining Treatment.

Many states, including Washington,[172] California[173], West Virginia[174] and New York[175] have variations of Physician Orders for Life-Sustaining Treatment ("POLST") forms, a document developed by health care professionals as a standardized method to summarize a patient's wishes regarding life-sustaining treatment. This document is meant to supplement a health care directive. The form varies from state to state, but it is generally signed by both the patient and the doctor and becomes part of the patient's medical record. It is printed on a bright colored card stock so as to be visible in a patient's file (e.g., bright green in Washington, hot pink in West Virginia).

POLST forms replace what were formally known as DNR or Do Not Resuscitate Orders. While a POLST form is typically broader than a DNR Order, it in part simply represents a paradigm shift from a discussion of withholding treatment versus a newer concept of allowing a natural death, along with an ability to provide explicit instructions for making critical

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[169] RCW 70.122.030(1).

[170] RCW 71.32.010.

[171] Breanne M. Sheetz, *The Choice to Limit Choice: Using Psychiatric Advance Directives to Manage the Effects of Mental Illness and Support Self-Responsibility*, 40 U. Mich. J.L. Reform 401, 408 (Winter 2007).

[172] RCW 43.70.480.

[173] Cal. Prob. Code §4780.

[174] W. Virginia Health Care Decisions Act §16-30-3(u), referred to as Physicians Orders for Scope of Treatment (POST).

[175] N.Y. Pub. Health L. 2994-aa – 2994-gg, referred to as Medical Orders for Life-Sustaining Treatment ("MOLST"). *See* www.nyhealth.gov/professionals/patients/patient_rights/molst/ for further information (revised Jan. 2011).

decisions concerning a patient's care.[176] The older DNR Orders were less precise. POLST, while often leading to the same outcome, offers more detail, which has the potential of relieving the burden of decision-making by others who may not know what the patient would have chosen. Studies have shown that this paradigm shift has allowed patients to, in many cases, receive the care they want and avoid unwanted treatment.[177]

The form is intended to be portable and must be on file with a particular physician in order for it to be followed. The form allows an individual to express his or her wishes with respect to resuscitation, various types of medical interventions, feeding tubes, ventilators, and antibiotics. POLST is currently used in over a dozen states and is in development in at least 20 more.

F. Burial, Cremation and Funeral Instructions, and Organ Donation.

Making advance arrangements for funerals, disposition of remains, and burial or cremation is critical for unmarried couples.

1. Disposition of Remains.

Washington law provides that "[a] valid written document expressing the decedent's wishes regarding the place or method of disposition of his or her remains, signed by the decedent in the presence of a witness, is sufficient legal authorization for the procedures to be accomplished."[178] As with the documents discussed above, in the absence of enforceable, written instructions, state law creates a hierarchy of persons who have the authority to make these decisions, and the unmarried partner of a decedent is not found in that hierarchy.[179]

Instructions regarding disposition of remains may be in a will or in a separate document. If the instructions in a will comply with the requirements for instructions regarding the disposition of remains, they are considered valid, regardless of the will's validity. Nevertheless**,** instructions separate from a will are usually preferable, because of the increased likelihood that the instructions

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[176] Paula Span, *D.N.R. by Another Name*, The New York Times, *The New Old Age Blog* (Dec. 6, 2010).

[177] Susan E. Hickman, Ph.D., et al., *A Comparison of Methods to Communicate Treatment Preferences in Nursing Facilities: Traditional Practices Versus the Physician Orders for Life-Sustaining Treatment Program*, 58 J. Am. Geriatr. Soc'y 1241 (July 2010).

[178] RCW 68.50.160(1).

[179] *See, e.g.* RCW 68.50.160(3). *See also Funeral Consumer Alliance, Who Has the Right to Make Decisions About Your Funeral*, www.funerals.org/your-legal-rights/funeral-decision-rights (last updated March 1, 2011).

will be found prior to any alternate arrangements being made. Clients should also tell their partner or other trusted friend where to find the instructions.

2. Anatomical Gifts.

The Uniform Anatomical Gift Act was passed by the United States in 1968 to harmonize the various practices related to the increasing organ transplantations.[180] It has been adopted in Washington as RCW ch. 68.64. The Uniform Anatomical Gift Act makes sure that the donations of organs are followed in an ethical manner. It covers anatomical gifts for transplantation as well as donation of donation of bodies to medical institutions and to hospitals for teaching and experimentation.

If an individual wishes to donate organs upon death, the best way to evidence that wish is through a Uniform Donor wallet card. Many states departments of licensing, including Washington and Wisconsin, provide the opportunity for residents to register their intent to donate organs on the back of their driver's license.[181]

However, many individuals may also incorporate their wishes regarding anatomical gifts into other advance directives to make sure that these wishes are known. Any written instructions should set forth the client's intentions with respect to funeral and burial arrangements, disposition of remains including disposition of anatomical parts (discussed below), and any arrangements already made and paid for.

IX. Medicare and Medicaid

Section 1917(a)(2) of the Social Security Act (the "Act") allows certain exceptions for legal spouses under Medicaid's authority to take action against the assets of a benefits recipient, either by filing a lien against real property, by seeking to void certain asset transfers, or to recover against the estate of a Medicaid beneficiary. Generally, a lien may not be filed against the real property of a Medicaid recipient where the real property is occupied by a spouse, transfer of assets to spouses are protected from Medicaid recovery, and actions to enforce a lien against an estate are precluded where there is a surviving spouse.

The Centers for Medicare & Medicaid Services of the US Department of Health and Human Services sent a letter to all state Medicaid directors on June 10, 2011 advising them as to three circumstances where HHS believes that states can

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[180] *Unif. Anatomical Gift Act* (1968) (Amended 2006), U.L.A. 109 (Supp. 2011).

[181] RCW 68.64.040(1)(a); Wis. State. §343.175(3).

voluntarily decide to recognize same-sex partners of Medicaid recipients in spite of the federal Defense of Marriage Act.

Sections 1917(b)(3) and 1917(c)(2)(D) of the Act provide certain exemptions if application of the strict rules were to create an undue hardship. An undue hardship exists when application of the transfer of assets penalty and denial of eligibility for Medicaid payment for long-term care would deprive the individual of medical care such that the individual's health or life would be endangered, or the individual would be deprived of food, clothing, shelter, or other necessities of life.[182] The letter, "Re: Same Sex Partners and Medicaid Liens, Transfers of Assets, and Estate Recovery,"[183] indicates that the exceptions previously only allowed for legal spouses may be extended to same-sex partners of Medicaid recipients under the undue hardship provision.

In its letter, HHS indicated that states have flexibility to design reasonable criteria for determining what constitutes an undue hardship and who may be afforded protection from estate recovery in such instances. At the State's discretion, HHS has indicated that this may include establishing reasonable protections applicable to the same-sex spouse or domestic partner of a deceased Medicaid recipient.

X. Cohabitation Agreements and Related Arrangements

A. Background.

Unmarried couples are able to enter into legal relationships through bilateral contracts that define the rights, duties, obligations, responsibilities, and other parameters of their relationship. Like a prenuptial agreement, the purpose of a cohabitation agreement is to create a degree of certainty for a couple with respect to how expenses will be handled, how income will be shared or separated, how assets will be acquired and under whose name, what will happen to assets in the event the relationship terminates, and how disputes are to be resolved. Unlike a prenuptial agreement, however, cohabitation agreements may bring into being rights and obligations that may not otherwise have existed. Furthermore, where a prenuptial agreement generally becomes effective upon marriage and has no effect if the marriage does not take place, cohabitation agreements generally take effect upon execution and terminate upon death or the termination of the relationship, which can be harder to define than legal dissolution.

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[182] The Deficit Reduction Act of 2005 (DRA, Pub. L. No. 109-171). The Centers for Medicare & Medicaid Services has provided guidance on undue hardship determinations in the State Medicaid Manual and in a State Medicaid Director letter, The Centers for Medicare & Medicaid Services, SMD #06-018 (July 27, 2006) emphasizing that States have considerable flexibility in determining whether undue hardship exists, and the circumstances under which they will not impose transfer of assets penalties.

[183] Center for Medicaid, CHIP and Survey Certification, SMDL # 11-006 (June 10, 2011), *available at* www.cms.gov/smdl/downloads/SMD11-006.pdf.

The parties have tremendous flexibility in deciding how comprehensive they want the agreement to be. Most courts now enforce explicit agreements between unmarried persons as long as the consideration is severable from the sexual aspect of the relationship. Consideration based on sexual services will invalidate any agreement.[184]

B. The Law in the Absence of a Written Agreement.

Whereas California confers rights of cohabitants based on an implied or an express contract,[185] Washington confers rights on cohabitants based merely on their status as such.[186] A line of cases has developed in Washington that has the effect of eliminating unjust enrichment when an unmarried couple separates with no prior agreement.[187] These cases all depend upon whether an intimate committed relationship existed.[188] Most recently, Washington State Appellate Division III ruled in *In re Long and Fregeau*, that equitable distribution principles could be applied by the court to address property division issues of terminated same-sex unregistered domestic partnership.[189]

The relevant factors for finding an intimate committed relationship in Washington include, but are not limited to: "[c]ontinuous cohabitation, duration of the relationship, purpose of the relationship, pooling of

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[184] Frank S. Berall, *Estate Planning Considerations for Unmarried Same or Opposite Sex Cohabitants*, 23 Quinnipiac L.Rev. 361, 383 (2004) [hereinafter "Berall, *Estate Planning Considerations*"]. *See also* Linda J. Ravdin, 849 Tax Mgmt. (BNA), *Marital Agreements*, A-48-49 (2003).

[185] In *Marvin v. Marvin*, 18 Cal. 3d 660, 665, 557 P.2d 106, 110 (1976), the California Supreme Court found that an implied contract for support, in return for homemaking services, could exist under some circumstances and would be enforceable. Ironically, in this case, the plaintiff, Michelle Marvin (who had legally changed her surname from Triola), was not awarded a recovery, because no such contract was found to exist. But, one of the key outcomes of the case was that California courts were authorized to enforce contracts between cohabiting couples where the requisite elements of a contract are found to exist, unless the contract was explicitly founded on sexual services as consideration.

[186] But Washington confers additional rights to persons registered pursuant to the Registered Domestic Partnership Act. *See supra* note 78-88 and accompanying text.

[187] *See, e.g., Vasquez v. Hawthorne*, 145 Wn. 2d 103, 33 P.3d 735 (2001) (the Court upheld a same-sex partner's claim against the estate of his deceased partner based on an equitable claim); *Marriage of Pennington*, 142 Wn. 2d 592, 14 P.3d 764 (2000); *Connell v. Francisco*, 127 Wn. 2d 339, 898 P.2d 831 (1995); *Marriage of Lindsey*, 101 Wn. 2d 299, 678 P.2d 328 (1984); and *Meretricious Relationship of Sutton*, 85 Wn. App. 487, 933 P.2d 1069, *rev. denied*, 133 Wn. 2d 1006 (1997).

[188] Various terms have been used to describe relationships meeting the legal standard for the just and equitable distribution of property. Earlier Washington cases used the term "meretricious relationship," which the courts defined as "a stable, marital-like relationship where both parties cohabit with knowledge that a lawful marriage between them does not exist." *Connell v. Francisco*, 127 Wn. 2d at 346, 898 P.2d at 834; *Relationship of Eggers*, 30 Wn. App. 867, 871 n.2, 638 P.2d 1267, 1270 n.2 (1982). However, because of that term's negative connotation, more recently, the Washington Supreme Court has used the phrase "committed intimate relationship." *Olver v. Fowler*, 161 Wn. 2d 655, 168 P.3d 348 (2007).

[189] *In re Long and Fregeau*, 158 Wn. App. 919, 244 P.3d 26 (2010).

resources and services for joint projects, and the intent of the parties."[190] Additional factors include whether the parties held themselves out as a couple; whether the parties named each other as beneficiaries on life insurance and employee benefits, and in their estate planning documents; and whether the couple parented children together. Not all of the factors are required but, taken as a whole, they must show the existence of a stable marital-like relationship.[191] Washington law does not distinguish between same-sex and opposite-sex unmarried couples when applying these factors.[192]

In the absence of a prior agreement, a court must examine the relationship of the parties, and the property accumulated during the relationship, and make a "just and equitable" distribution of that property.[193] Property acquired during the relationship is presumed to belong to both parties.[194] If the presumption of joint ownership is not rebutted, the court may look to RCW 26.09.080, Washington's dissolution statute, for guidance as to the fair and equitable distribution of property acquired during the relationship.[195] The distinction between marital dissolution cases and cohabitation property division cases is that property that would have been separate property had the couple been legally married is *not* subject to equitable division.[196]

C. Drafting Cohabitation Agreements.

Cohabitation agreements may be oral in some states.[197] Even when a couple is willing to rely on a state's default rules, because of the migratory nature of individuals, the potential applicability of the laws of multiple states, and difficulty in proving and enforcing oral agreements, the couple's intent should be clearly stated in a written agreement. And, because the goal of the domestic partnership agreement or cohabitation

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[190] *In re Pennington*, 142 Wn. 2d 592, 601, 14 P.3d 764, 770 (2000).

[191] *Id*. at 603, 14 P.3d at 770.

[192] *Gormley v. Robertson*, 120 Wn. App. 31, 38, 83 P.3d 1042, 1046 (2004).

[193] *Marriage of Lindsey*, 101 Wn. 2d 299, 304, 678 P.2d 328, 331 (1984) (citations omitted). *See also In re Long and Fregeau*, 158 Wn. App. 919, 244 P.3d 26 (Div. 3 2010) where the Court held that infidelity of both parties did not take away from their shared purpose in the relationship and did not preclude a finding of intimate committed relationship.

[194] *Pennington*, 142 Wn. 2d at 602, 14 P.3d at 770 (*citing Connell*, 127 Wn. 2d at 351).

[195] *Id.* at 607-608.

[196] *Connell*, 127 Wn. 2d at 351-2, 898 P.2d at 837.

[197] *See Relationship of Eggers*, 30 Wn. App. 867, 638 P.2d 1267 (1982) (the court held that express oral contracts between persons living together are enforceable), and *Whorton v. Dillingham*, 202 Cal. App. 3d 447 (1988). *See also*, Richard M. Horwood *et al.*, 813-3rd Tax Mgmt. (BNA), *Estate Planning for the Unmarried Adult*, A-48 (2010).

agreement is to eliminate any factual disputes and ambiguities about what the parties intended, a written agreement is preferable.

The following are some of the more important issues that should be addressed in the agreement.

1. Recitals. The agreement should contain recitals that document the circumstances of the parties at the time the agreement is entered into and outline their intention with respect to creating the agreement. The recitals should set forth the date the parties began living together and a brief history of the couple's relationship together. The recitals should demonstrate, based on the facts, and not on boilerplate provisions, that an enforceable contract with good and valuable consideration exists between the parties.

2. Disclosure of Assets and Liabilities. As with prenuptial agreements, both parties must disclose the nature and value of their property. Depending upon the applicable state law, it is possible that the same principles applicable to prenuptial agreements may also apply to cohabitation agreements, including the ability to set aside the agreement in the absence of full and fair disclosure.

3. Expenses While Living Together. The agreement should address how expenses will be handled during the relationship, how assets purchased will be titled, and any post-termination support commitments. Many of these issues can and should be provided for in the wills of the partners as well as in the cohabitation agreement.

4. Dispute Resolution. It is advisable to include dispute resolution provisions. If the parties agree to mediation or arbitration, the agreement should specify who would pay the mediator/arbitrator. The agreement should also indicate when the parties might abandon mediation for either arbitration or going directly to court. In addition, if attorneys or court costs are involved, it should cover how these costs will be paid for as well.

5. Parenting. Agreements regarding parenting that recognize the roles, affections and responsibilities that have developed between the child and a non-biological child, may violate public policy and therefore would not be enforceable.[198] But may be useful in establishing the terms of a parent-child relationship that has been formed if it is later called into question and may still carry some weight with the

[198] *See, e.g.,* RCW 26.09.070(3). *See also, Unif. Premarital Agreement Act* §3(b) (1983), 9C U.L.A. 35, 43 (2001) ("The right of a child to support may not be adversely affected by a premarital agreement.").

court.[199] Accordingly, the couple may want to try to agree in advance, and document, how they will handle issues such as primary parent/custody, visitation and how the children will be raised, keeping in mind that the best interest of the children, as determined by the court, will ultimately prevail.[200] Similar provisions for pets may also be documented.[201]

6. Assisted Reproductive Technology. If a couple has or plans to store genetic material it is important to deal with its use and/or disposition in a written agreement.[202] The couple should document their plans to use that material to conceive children, and whether those plans should be altered if the couple does not stay together or if one member of the couple dies.[203] If genetic material is received from a donor, the parties should agree in writing that the donor will not have any parental rights and will agree, if necessary, to having any parental rights terminated (which may not be binding, but does memorialize the intent of the parties at the time of the agreement). Exhibit B contains one form of provision that could be used to define eligible beneficiaries, in light of the various types of assisted conception, during and after the lifetime of a parent.

7. Marriage. If marriage is a legal option for a couple, they should indicate whether they intend the agreement to remain in effect should they marry. Alternatively, the agreement may terminate upon marriage, at which time the couple would be required to enter into a new agreement or rely on the state default rules applicable to married couples. If marriage would not be legal, a couple should not state an

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[199] *Tenth Annual Review of Gender and Sexuality Law: Family Law Chapter: Child Custody, Visitation & Termination of Parental Rights*, 10 Geo. J.Gender & L. 713, 740, Meredith Larson, ed. (2009) [hereinafter Larson, *Child Custody*].

[200] "The agreement may be considered by the court, in light of the circumstances and knowledge of the parties when the agreement was made, but it is not enforceable." *Marriage of Littlefield*, 133 Wn. 2d 39, 58, 940 P.2d 1362, 1372 (1997).

[201] *See* Section XI *infra* for further discussion regarding parenting issues.

[202] Washington presumes that a contract regarding the disposition of embryos is enforceable at the time it was entered into. *Litowitz v. Litowitz*, 146 Wn. 2d 514, 48 P.3d 261, 268 (2002), *cert. den.*, 537 US 1191 (2003). Washington's Uniform Parentage Act, RCW ch. 26.26 governs surrogacy contracts. *See* Dominic J. Campisi, Claudia Lowder, and Naznin Bomi Challa, *Heirs in the Freezer Bronze Age Biology Confronts Biotechnology*, 36 ACTEC J. 179, Appendix for a Model IVF Contract.

[203] *See* Kathryn Venturatos Lorio, *Conceiving the Inconceivable: Legal Recognition of the Posthumously Conceived Child*, 34 ACTEC J. 154 (Winter 2008); Carole M. Bass, *What If You Die, And Then Have Children? Know How to Plan for Offspring Who Are Born – Sometimes Even Conceived – Posthumously. A State-by-State Guide*, 145 Tr. & Est. 20 (April 2006). In some jurisdictions a non-biological parent, who has not adopted a child, may seek custody under the doctrine of *de facto* parentage. See, e.g., *Smith v. Guest*, 16 A.3d 920 (2011) and *In re Parentage of L.B.*, 155 Wn. 2d 679, 122 P.3d 161 (2005), *cert. denied*, sub nom., *Britain v. Carvin*, 547 U.S. 1143 (2006).

intent to live as husband and wife, thereby creating a possibility in certain states that the agreement will be found void because it violates public policy.[204] The following is a sample clause where the Agreement is intended to continue in effect:

The Parties intend this Agreement to continue in full force and effect in the event of a marriage between them is recognized in _____, and the parties agree to take all such action as may be necessary, appropriate and/or expedient to accomplish such purpose. In such event, the parties agree to accept the provisions of this Agreement in full and complete discharge of any and every claim and/or right he/she may hereafter have against the other party for an equitable distribution of marital property and for spousal support, maintenance and/or alimony, and the parties waive any such claims and/or rights except to the extent set forth in this Agreement.

8. Termination of the Relationship/Death. The Agreement should contemplate what the parties will provide for the other in the event the relationship terminates or one party dies.[205]

9. Choice of Law. Because of the mobile nature of couples in our society, a choice of law provision is also advisable. Confirm that the state law where the parties reside at the time of execution allows such agreements and its particular provisions.[206] Assuming that the agreement is enforceable in the state where executed, the parties may want to include a provision such as the following: "To establish reasonable certainty in their respective financial affairs, the parties agree that, without regard to where they may reside or be domiciled in the future, or where any or all of their real or personal property may be located, all property rights of the parties and their rights under this Agreement shall be determined according to the substantive laws of [state where executed], without regard to conflict of law rules applicable in [state where executed] or in any other state."

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[204] Berall, *Estate Planning Considerations*, *supra* note 184, *at* 383-384.

[205] *See supra* notes 104-108 and accompanying text for a discussion of the related federal tax consequences in these situations.

[206] Linda J. Ravdin, *Marital Agreements*, *supra* note 184, B-1101-1107, for a table by state indicating the enforceability of domestic partnership agreements regarding property and support. *See also* William A. Reppy, Jr., *Choice of Law Problems Arising When Unmarried Cohabitants Change Domicile*, 55 SMU L. Rev. 273, 275 (Winter 2002) for an examination of the issues affecting cohabitants with respect to choice of law rules after the termination of the relationship or the death of one member of the couple.

10. Severability. Because the law is so uncertain in this area, it is critical to include a severability clause allowing an unenforceable provision to be severed from the remainder of an agreement.[207]

XI. Forming a Family, Parenting Arrangements.

Same-sex couples may have children from prior marriages or relationships, foster children, adopted children (either adopted jointly or by one partner adopting the other partner's biological child), children as a result of assisted reproductive technology, including the use of preserved reproductive material for possible future use and/or children via surrogacy.[208]

A. Adoption.

Adoption can take a number of forms.[209] It may be pursued by an individual alone or by a couple jointly, or as a second-parent adoption, where one partner adopts his or her partner's biological or adopted child without terminating the original legal parent's rights is also available in some states. Same-sex adoption is not yet permitted in all states, but some have gone so far as to revise their adoption statutes to be gender-neutral, paving the way for same-sex adoptions.[210]

California law permits an adult related to the child, a person named in a deceased parent's will, a legal guardian, or a person with whom the child has been placed for adoption, to petition to adopt.[211] It also specifically provides for step-parent adoption.[212] In 2003, the California Supreme

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[207] Washington is now among the few states that allow compensation of gestational carriers. RCW 26.26.101. *See also* Ark. Code. § 9-10-201(c)(2), *In re Marriage of Buzzanca*, 61 Cal. App. 4th 1410, 72 Cal. Rptr. 2d 280 (1998), 750 Ill. Comp. Stat. 47/5 and *R.R. v. M.H.*, 426 Mass. 501, 689 N.E.2d 790 (1998).

[208] For a discussion of the issues raised by assisted reproductive technology, *see* Mary F. Radford, *Postmortem Sperm Retrieval and the Social Security Administration: How Modern Reproductive Technology Makes Strange Bedfellows*, 2 Est. Plan. & Community Prop. L.J. 33 (2009); Nancy D. Polikoff, *A Mother Should Not Have to Adopt Her Own Child: Parentage Laws for Children of Lesbian Couples in the Twenty-First Century* 5 Stan. J.C.R. & C.L. 201 (2009).

[209] *See* http://www.hrc.org/laws_and_elections/state.asp for an analysis of adoption, custody and visitation laws on a state-by-state basis; and Susan L. Pollet, *Breaking Up Is Hard[er] To Do; Same-Sex Divorce*, 83 N.Y. State Bar J. 10, 19 (Mar./April 2011) for another state-by-state chart of states permitting gay and lesbian adoption, second parent adoption and joint adoption, www.nysba.org/AM/Template.cfm?Section=Home&ContentID=47885&Template=/CM/ContentDisplay.cfm.

[210] Washington allows "Any person who is legally competent and who is eighteen years of age or older" to be an adoptive parent. RCW 26.33.140(2).

[211] Cal. Fam. Code §8802.

[212] Cal. Fam. Code §§9000-9007.

Court affirmed that a same-sex co-parent can petition to adopt his or her partner's child or child of the relationship.[213]

While the Uniform Parentage Act (UPA) deals with the donation of sperm, ova and surrogacy, the laws on these issues vary from state to state, and are in flux.[214] Any type of assisted reproduction agreement should be documented in writing that includes the intent and expectation of the parties. Donor and surrogacy agreements are beyond the scope of this outline.[215]

Note that the Uniform Probate Code (UPC) does not adopt the definitions from the UPA for determining legal parentage; rather it contains its own. Section 2-119 of the UPC does not contemplate a second-parent adoption. It allows for the genetic parent's parent-child relationship to continue when a step-parent adopts a child. But when an unmarried partner adopts the child as the second-parent, it would terminate the genetic parent's parent-child relationship for inheritance purposes. Thus, in states where this might occur it is even more critical that the parents have valid wills in place.[216]

B. De Facto Parentage.

When legal parentage has not been or cannot be established, some states, including Washington, recognize the equitable concept of the "de facto" parent, in the absence of a legal adoption.[217] The Washington Court of Appeals adopted the following four-part test to determine the existence of a *de facto* parent-child relationship, as follows:

1. the natural or legal parent consented to and fostered the parent-like relationship;

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[213] *Sharon S. v. Superior Court*, 73 P.3d 554 (Cal. 2003).

[214] *See* RCW §§26.26.700-740 (adopted in 2002), Cal Fam. Code §§7600-7606. *See also* Susan N. Gary, *We are Family: The Definition of Parent and Child for Succession Purposes*, 34 ACTEC Journal 171 (Winter 2008). *E.g*., surrogacy contracts are permitted in California, Cal. Fam. Code §7613. They are illegal in New Yew York, N.Y. Dom. Rel. Law §122, and it is a felony for an attorney to assist in the preparation of such contracts. *Id* at §123.

[215] *See* Charles P. Kindregan, Jr. & Maureen McBrien, *Assisted Reproductive Technology: A Lawyer's Guide to Emerging Law and Science* (2d ed. 2011) for sample agreements and a checklist of issues to be covered.

[216] *See* Lee-Ford Tritt, *Parent Child Property Succession*, 148 Tr. & Est. 14 (Aug. 2009) for an in-depth discussion of the Uniform Probate Code's attempt to deal with the changing definition of family caused by new types of family structures and by artificial reproductive technologies. *See also* Kristine S. Knaplund, *The New Uniform Probate Code's Surprising Gender Inequities*, Duke Journal of Gender Law & Policy (forthcoming Spring 2011); *also available at* swww.ssrn.com/abstract=1636531 (Pepperdine University Legal Studies Research Paper No. 2010/14, July 2010) for a further discussion of this topic

[217] Larson, *Child Custody supra* note 199.

2. the petitioner and the child lived together in the same household;

3. the petitioner assumed obligations of parenthood without expectation of financial compensation; and

4. the petitioner has been in a parental role for a length of time sufficient to have established with the child a bonded, dependent relationship parental in nature.[218]

While the *de facto* parent stands in legal parity with a legal parent, because it is an equitable remedy and not statutory, a written agreement would always be preferable to assuming that this remedy will be available. In the absence of either a biological parent-child relationship or a legal adoption, there is little certainty with respect to the rights and responsibilities between an adult and child.

XII. Methods to Minimize Taxes

A. Defining the Rights of Unmarried Partners to Jointly Owned Property.

1. General Federal Estate and Gift Tax Considerations.

The marital deduction, allowing most transfers between U.S. citizen spouses to avoid transfer or income taxes do not apply to unmarried couples.[219] Accordingly, any transfers between partners may be treated as taxable gifts (subject to the IRC §2503(b) annual exclusion, the donor's available applicable exclusion, and the exclusion from gift tax for tuition and medical expenses under IRC §2503(e)).[220]

2. Indirect Gifts Arising From Pooled Expenses.

The value of taxable gifts between unmarried partners becomes difficult to quantify in the context of shared living expenses. When partners pool income and one party receives more income than the other, pooling may cause a net transfer to the party with less income, resulting in a taxable gift. This result may be partially ameliorated by entering into a contractual arrangement between the partners providing for mutual and adequate consideration. The amount of the gift is the difference between the value of the

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[218] *Parentage of M.F.*, 141 Wn. App. 558, 563, 170 P.3d 601 (2007) *citing Parentage of L.B.*, 121 Wn. App. 460, 485, 89 P.3d 271 (2004).

[219] IRC §2056(a), §2523(a), and §1041.

[220] *Pascarelli v. Comm'r*, 55 T.C. 1082 (1971), *aff'd* 485 F.2d 681 (3rd Cir. 1973).

property transferred and the consideration received.[221] However, the exchange of consideration sufficient to make a promised transfer enforceable for state contract law purposes will not necessarily prevent some part of the transfer from being a gift for federal tax purposes, unless the transferor receives consideration having an economic value equal to the property transferred.

To the extent a net transfer from the greater income earner to the lower income earner is viewed as being paid in consideration for the lower income earner's love, emotional support, or other services upon which a monetary value may not be placed, the transfer is a gift.

If the contractual arrangement provides that the net transfer from the higher income earner to the lower income earner is an advance to be repaid upon the happening of some event, e.g., the lower income partner finishing school, or becoming gainfully employed, or the higher income partner retiring, the couple will be treated as being in a debtor-creditor relationship. These types of arrangements should be avoided unless the arrangement provides for adequate stated interest and the advanced sums will actually be repaid. Sections 163(h), 1274 and 7872 of the Code address below-market interest and gift loans by imputing interest income in the amount of the applicable federal rate to the creditor, taxing the creditor as making a gift of the interest, and denying the debtor's interest deductions. If the debt is never repaid, IRC §61(a)(12) treats the amount advanced as income to the debtor from the discharge of indebtedness. Section 7872(c)(2)(A) of the Code provides a *de minimis* exception for gift loans between individuals for amounts of $10,000 or less. Thus, generally, for smaller loans there is neither imputed interest nor a taxable gift.

3. Joint Tenancies.

Joint tenancy ownership of assets is one of the most popular estate planning devices for unmarried couples. When contributions by both parties are equal, and where the intentions of both parties with regard to management and disposition of the assets are identical, joint tenancy is an efficient and economical estate planning tool. Joint tenancy in the nontaxable estate may avoid the need for disclosure to family members at the time of the disposition. And if a joint tenancy is challenged, the presumption of a gift of funds in

[221] IRC §2512(b).

joint tenancy must be rebutted by clear and convincing evidence of a contrary intent, which is typically difficult to overcome.[222]

a. Joint Tenancy May Result In An Unintended Gift.

For the client with a taxable estate, joint tenancy can result in unintended consequences. When an asset, such as a house, is purchased in joint tenancy, if the parties contribute equally to the purchase, then acquiring the asset in joint tenancy is not a taxable event. However, if one partner purchases or contributes to an asset (other than a bank account or U.S. bonds), and has it conveyed to himself and his partner in joint tenancy with right of survivorship, then the purchase constitutes an immediate gift of the value of the transfer in excess of the annual exclusion.[223]

Upon the death of one joint tenant, the entire value of the jointly held property is included in the decedent's gross estate, unless it can be shown that the surviving joint owner actually contributed to the acquisition of the asset.[224] The burden of proof is on the taxpayer and may be difficult to sustain without meticulous record keeping. If clients intend to own real property in joint tenancy, they should document their intentions, their contributions to points and the down payment, mortgage payments, and home improvements.

There is an exception to the present gift rule for joint bank accounts and U.S. bonds: The transfer, and thus a completed gift, does not occur until the joint holder withdraws money from the account.[225]

b. Non-Tax Disadvantages of Joint Tenancies.

In addition to the tax disadvantages, there are other problems with joint tenancies. A joint owner of a bank account can withdraw the other party's money from the account without the party's consent

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[222] RCW 30.22.100(3).

[223] IRC §2503(b) and Treas. Reg. §25.2511-1(h)(5).

[224] IRC §2040(a) and Treas. Reg. §20.2040-1(a)(2).

[225] Treas. Reg. §25.2511-1(h)(4). The definitions in Treas. Reg. §25.2518-2(c)(4)(iii) extend the exception to the immediate gift presumption to brokerage accounts and other investment accounts, including mutual funds.

or knowledge.[226] This could be avoided by requiring two signatures on an account.

Assets titled jointly, such as real estate, stock, or a motor vehicle, cannot be sold without the consent of both joint owners. This protects the owners, but it also often results in a deadlock between partners on the appropriate disposition of an asset.

c. Drafting Recommendations.

Some practitioners recommend that partners establish a partnership or limited liability company to take title to a home, to facilitate accurate record keeping, and also to provide protection against a creditor or a partner forcing partition. Using an entity for a principal residence acquisition, however, will prevent the partners from using the exclusion for capital gain on sale under IRC §121 unless it is treated as a disregarded entity.[227] This exclusion is available to persons, but not entities.

Alternatively, legal title could be held in a revocable title holding trust with a separate schedule of beneficial interests. The trust agreement could further define how the beneficial interests are to be adjusted over time based on the relative financial contributions of the partners.

B. Adult Adoption.

1. Purpose of Adult Adoption.

One method by which same-sex couples have sought to obtain some certainty with respect to their estate planning intentions is to have one partner adopt the other.[228] There are several motivations behind this planning technique, including establishing a family

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[226] RCW 30.22.110. Washington does not have a statutory equivalent to RCW 30.22.110 applicable to securities accounts. Rev. Rul. 69-148 provides that a joint tenancy securities account constitutes a completed gift except when the account agreement allows the donor to remove assets from the account without the consent of the donee. Thus, unless an account agreement allows for a unilateral withdrawal, a securities account does not constitute a completed gift.

[227] The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788, amended IRC §121 (formerly providing a one-time exclusion of gain from sale of a principal residence by an individual who has attained age 55) and permits exclusion of up to $250,000 of gain by an individual or $500,000 by a married couple on the sale or exchange of a principal residence, if the property was a principal residence for 2 of the last 5 years.

[228] For a thorough discussion of this topic *see* Terry L. Turnipseed, *Scalia's Ship of Revulsion Has Sailed: Will Lawrence Protect Adults Who Adopt Lovers to Help Ensure Their Inheritance From Incest Prosecution*?, 32 Hamline L. Rev. 95 (2009).

relationship for purposes of entitlements and other benefits (i.e. Social Security, health insurance, survivor benefits), the desire to create a legal bond with another individual, and to establish a legal heir and secure inheritance rights.[229] Because estate intestacy laws do not allow for the distribution of a decedent partner's estate to his or her surviving partner, some unmarried couples resort to adoption, rather than rely, solely upon other more conventional estate planning techniques.

Another reason an adult may wish to adopt a partner is to bring the adoptee within the class of beneficiaries under a pre-established estate planning instrument. One partner may be a beneficiary of a trust providing for distribution of her share to her descendants upon her death, but if she has none, then to some other specified group of individuals. In this case, adoption may bring the partner into the permissible class of recipients of the trust share upon the death of the current income beneficiary.

In *Adoption of Patricia S*, 976 A.2d 966 (2009), Olive's parents established 2 trusts for her benefit and then for the benefit of her descendants. Olive had no natural descendants, so she adopted her partner, Patricia. The Trustees of the trusts filed a petition in the Maine Probate Court seeking annulment of the adoption and a declaratory judgment that the adoption is null and void. In it, they alleged that the couple obtained the adoption by fraud in that they did not disclose their relationship to the court, and because, as New York residents at the time, Patricia and Olive had not fulfilled the statutory requirements of living or residing in Maine necessary to give the Knox County Probate Court jurisdiction to issue the decree of adoption under 18-A Me. Rev. Stat. §9-315(a). The adoption was upheld on appeal.

Before reaching the conclusion that adoption will bring an individual into a class of beneficiaries, there must be a careful examination of the dispositive intent set forth in the instrument and the state law applicable to adopted heirs.[230]

Adult adoptions may provide an effective way to eliminate the status, as heirs, of the adopter's relatives, so that they no longer have standing to contest an estate plan. Considering the frequency

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[229] *See* Gwendolyn L. Snodgrass, *Creating a Family Without Marriage: The Advantages and Disadvantages of Adult Adoption Among Gay and Lesbian Partners*, 36 Brandeis J. Fam.L. 75 (1997-1998).

[230] *See* Peter T. Wendel, *The Succession Rights of Adopted Adults: Trying to Fit a Square Peg Into a Round Hole*, 43 Creighton L. Rev. 815 (2010) for an analysis of the developing law in this area.

of challenges by relatives claiming that a decedent's partner exerted undue influence over the decedent, the adoption strategy appears attractive to many unmarried partners (because it is typically more difficult to challenge an adoption than a will).[231]

The statutory treatment of adoption and its effectiveness differs from state to state. Not all states permit adult adoption, and some require the adoptee to be younger than the adopter.[232] The possibility of prosecution for incest in the applicable state should also be considered before opting for this planning method.[233] Washington's incest statute, RCW 9A.64.020, only applies to adopted descendants *under* the age of eighteen.[234]

It is important to carefully consider who will adopt whom. The partner who is likely to die first should be the adopter. Another concern is that an adoptee loses the right to inherit by intestacy from biological relatives. Adult adoption also triggers income tax considerations such as dependency exemptions and head of household status that should be considered, and clients need to understand that it is unlikely that an adoption may later be revoked or renounced once final.

2. Estate Planning Opportunities Following the Adoption of a Partner – Transfers of a Trade or Business.

Many estate planning opportunities arise once a partner has been adopted. Two particularly notable techniques are discussed below:

a. Special Valuation Rules of Section 2032A.

Section 2032A of the Code provides a special valuation rule for real property used in farming or a trade or business, with a maximum reduction in value of $1,020,000 in 2011. Section

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[231] For information concerning adoption in Washington, *see* David V. Anderson, *Adoption*, in *Washington Family Law Deskbook* ch. 60 (Wash. St. Bar. Assoc. 2d ed. 2001 & Supp. 2006).

[232] *Id*. n. 75.

[233] *Id*. at 17-24.

[234] *But see Restatement (Second) of Conflicts of Law* §290 cmt. c (1971) (providing that a state may disallow inheritance in connection with out-of-state adoption where inheritance would violate strong local public policy); *Restatement (First) of Conflict of Laws* §143 cmt. a, illus. (1934) (providing an example when adoption in one state will not be recognized for inheritance purposes in another state that does not permit such adoption). *E.g.*, Illinois' incest statute would make such adoptions illegal. 720 Ill. Comp. Stat. 5/11-11(2), and 755 Ill. Comp. Stat. 5/2-4 specifically provides that for trusts executed on or after Jan. 1, 1998, an adult adopted child is not considered a descendant. California permits adult adoption. Cal. Fam. Code §§9300-9340. Information and forms are *available at* Sacramento County Pub. Law Library, *Adult Adoption in California*, http://www.saclaw.org/pages/adult-adoption.aspx (last updated July 2011).

2032A allows the qualified real property to be valued at its actual use, rather than its highest and best use. To qualify, the "decedent or a member of the decedent's family" must have owned and used the property for the qualifying use before death, the property must pass to a "member of the decedent's family," and the property must continue to be used for the qualifying use by a "member of the decedent's family."[235] Members of the decedent's family are defined to include: (i) an ancestor; (ii) the decedent's spouse; (iii) a lineal descendant of the decedent, the decedent's spouse, or the decedent's parents; or (iv) the spouse of such lineal descendants.[236] Although the definitions of IRC §2032A are based on legal relationships, and therefore do not recognize informal relationships, they do include adopted children, stepchildren, sons- and daughters-in-law, and half-blood relations.[237] Thus, IRC §2032A may provide planning opportunities to non-traditional families in the right circumstances.

b. Section 6166 Election to Pay Estate Taxes on Qualified Businesses in Installments.

Section 6166 of the Code was passed to mitigate the pressure on an illiquid estate to sell a decedent's interest in a closely held company in order to pay estate taxes. Section 6166 allows a personal representative to pay estate tax in installments, on that portion of the estate tax for a decedent who was a U.S. citizen or resident that is attributable to a closely held business interest, over a maximum 14-year period. Section 6166 is highly technical, but some of its provisions are summarized below.[238]

The first payment of tax is due not more than five years after the date the estate tax return is due. A portion of the property ($1,360,000 in 2011 plus the applicable exclusion amount) is subject to estate tax at 2%.[239] The interest rate on deferred estate tax in excess of the 2% portion is 45% of the underpayment rate determined under IRC §6621.

Section 6166 requires that at least 35% of the adjusted gross estate must consist of an interest in a closely held business that was an

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[235] IRC §2032A(b).

[236] IRC §2032A(e)(2).

[237] *Id*.

[238] *See* Louis A. Mezzullo, 809-3rd Tax Mgmt. (BNA), *Estate Planning for Owners of Closely Held Business Interests* at Section III (2008) for an analysis of this topic.

[239] IRC §6601(j).

active trade or business in which the decedent or a member of his family holds a minimum percentage ownership interest.

An interest in a closely held business is defined, for purposes of Section 6166, as (i) an interest as a sole proprietorship carrying on a trade or business, (ii) an interest as a partner/member in a partnership/LLC carrying on a trade or business, if 20% or more of the partnership/LLC is included in the gross estate, or if the partnership/LLC had no more than 45 partners/members, and (iii) stock in a corporation carrying on a trade or business if 20% or more of the value of the corporations stock is included in the gross estate or if the corporation had no more than 15 shareholders.[240]

"Member of the family" is defined as including only brothers and sisters, spouses, ancestors, and lineal descendant, including adoptees.[241] Again, because of this restrictive definition, under the right circumstances, this may provide an excellent estate planning opportunity.

An estate will often attempt to claim the benefit of both IRC §2032A and IRC §6166. The differences between the family relationship definitions of these two sections may result in a non-traditional family qualifying for one, but not the other.

C. The Generation-Skipping Transfer Tax.

1. Background.

In addition to estate and gift taxes, there is a generation-skipping transfer ("GST") tax on transfers to grandchildren and other persons "assigned to a generation which is 2 or more generations below the generation assignment of the transferor."[242] The GST tax is a flat rate equal to the maximum estate tax rate (35% in 2011).[243] In 2011, the GST exemption $5,000,000.[244] Like the exemption equivalent sheltered by the unified credit, the GST exemption can be allocated to transfers during life, to transfers upon death, or partly to each.

a. Generation Assignment -- Family Members.

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[240] IRC §6166(b)(1).

[241] IRC §6166(D), IRC §267(c)(4).

[242] IRC §2613(a)(1).

[243] IRC §2641.

[244] The GST exemption amount is now equal to the estate tax applicable exclusion amount under IRC §2010(c) for the year in which the generation-skipping transfer is made ($5 million in 2011).

Each person is assigned to a particular generation to determine if a transfer is a generation skip.[245] Generation assignments are based on lineage for transfers to family members, and age for transfers to non-family members.[246] The age of an individual is irrelevant for generation assignments based upon family relationships.

b. Generation Assignment -- Non-Family Members.

Transfers to someone other than a family member are based on the transferee's age relative to the transferor. Any person not more than 12 ½ years younger than the transferor is assigned to the transferor's generation.[247] Any person between 12 ½ and 37 ½ years younger is assigned to the first generation below the transferor.[248] Each 25-year increment thereafter represents a new generation.[249]

Where unmarried partners are separated by a great age difference, a transfer in excess of the exemption may result in the application of the GST.

2. Adoption to Avoid the Application of the GST.

A valid adoption of an unrelated individual, who would otherwise be considered a skip-person, may avoid the generation assignment rules based on age, and allow application of the generation assignment rules based upon lineage from the transferor.

However, under regulations that went into effect on July 18, 2005, the IRS will analyze whether there is a bona fide parent/child relationship, or if the adoption was primarily for GST tax-avoidance purposes. This determination is made based upon all of the facts and circumstances, but the following requirements must be satisfied: (i) a legal adoption took place between the adoptee and the adoptive parent; (ii) the adoptee is a descendant of a parent or the adoptive parent (or the adoptive parent's spouse or former spouse); (iii) the adoptee is under the age of 18 at the time of the

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[245] IRC §2651.

[246] *Id.*

[247] IRC §2651(d)(1).

[248] IRC §2651(d)(2).

[249] IRC §2651(d)(3).

adoption; and (iv) the adoption is not primarily for GST tax-avoidance purposes.[250]

D. Partnerships and Limited Liability Companies.

One way to leverage transfers from one partner to the other is to establish a partnership or LLC for federal income tax purposes. If a couple can show they are a "syndicate, group, pool, joint venture, or other unincorporated organization through or by means of which any business, financial operation, or venture is carried on," they may establish a partnership under Subchapter K of the Code.[251] An arrangement may be classified as a partnership for federal income tax purposes even if it does not qualify as a partnership for state law purposes.[252]

Given a good faith business venture, an unmarried couple could enter into a partnership/LLC agreement, open a joint partnership/LLC account, acquire an employer's identification number from the Service, and file income tax returns for the entity. Partnership/LLC agreements allow for great flexibility and, assuming certain conditions are met, the couple can take advantage of the non-recognition provisions contained in Subchapter K, such as the ability to distribute out partnership/LLC assets without the recognition of gain or loss, so long as the value of the assets received by a partner/member do not exceed his or her basis in the entity.[253] Note, however, a joint undertaking merely to share expenses is not a partnership absent a business purpose.[254]

In addition to the opportunities discussed above, a partnership/LLC can provide asset protection. The creditor of a partner or member may receive an assignee interest in any distributions from the entity to the partner/member. But assuming the entity is treated as a partnership for income tax purposes, when income is not actually distributed, the potential for the receipt of "phantom income" often serves as a deterrent to creditors. An entity may similarly serve as a deterrent to hostile family members.

Partnerships and LLCs can be advantageous where one partner/member wants to give property to the other without giving up control over that property. Gifts of partnership or LLC interests from one partner/member to the other, if structured properly, may be discounted for lack of control

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[250] Treas. Reg. §26.2651-2(b).

[251] IRC §761(c).

[252] Treas. Reg. §301.7701-1(a)(3).

[253] IRC §731(a).

[254] Treas. Reg. §1.761-1(a).

and lack of marketability to leverage the amount of property that may be transferred within the IRC §2503(b) annual exclusion amount.[255] Furthermore, as discussed below, unmarried partners are not subject to the limitation on restrictive agreements imposed by IRC §2703.

E. Life Insurance.

Life insurance, if available, is an excellent way to: (i) provide liquidity for the payment of estate taxes; (ii) give a surviving partner the funds necessary to create a stream of income; and (iii) afford a surviving partner the funds to buy out a business partner or associate. When clients are relying on the pension and/or social security benefits of one partner for their retirement years, and neither would be available to the surviving partner, life insurance is an important consideration for replacement of that income.

By purchasing life insurance and naming a partner as beneficiary, a couple may accomplish a wealth transfer at death similar to a testamentary disposition. An advantage of life insurance is that it allows the insured to retain inter vivos power to cancel the policy or alter the beneficiary designation.

Life insurance may also afford a couple privacy and confidentiality that may not be available with other estate planning tools. If the beneficiary of a policy, instead of the insured, holds all incidents of ownership of that policy, and if there are no estate tax considerations, the beneficiary of the proceeds does not have to report the receipt of the proceeds. However, if estate tax is an issue, privacy and confidentiality will be lost: A Form 712 must be filed with the federal estate tax return indicating the recipient and amount of the proceeds.

1. Insurable Interest.

IRC §7702 requires life insurance policies to be "life insurance" under applicable state law. State insurance law generally provides that a contract of life insurance is not valid unless the policyholder has an "insurable interest" in the life of the insured.[256]

Traditionally, a policyholder is treated as having an insurable interest if any of the following exist: (i) a familial relationship with the insured; (ii) a reasonable expectation of advantage from the continuance of the insured's life; (iii) common ownership of

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[255] *See* Richard L. Lavoie, 831-3d Tax Mgmt. (BNA), *Valuation of Corporate Stock* (2006) for a discussion of valuation discounts.

[256] *See* RCW 48.18.060.

property; or (iv) a business relationship between the beneficiary and the insured.[257] The policy behind the insurable interest requirement is to discourage wagering arrangements and abusive uses of insurance.[258]

An insurable interest must exist at the time the insurance is issued.[259] Some states also require that the policyholder have an insurable interest at the time the proceeds are collected.[260] Provided that the latter rule does not apply, an insured may procure a policy on his own life and transfer it to someone who does not have an insurable interest. Where an irrevocable life insurance trust is involved (discussed below), it has been suggested that insurable interest issues may be avoided by procuring the life insurance and creating the trust under the laws of a state where an insurable interest exists.[261]

2. Income and Estate Tax Consequences of Life Insurance.

Life insurance proceeds paid by reason of the death of the insured are not generally subject to income tax.[262] Proceeds are included in an insured's gross taxable estate if they are payable to or for the benefit of the insured's estate, or if the insured retained any incidents of ownership in the policy.[263] When the owner of a life insurance policy predeceases the insured, the policy is an asset of the deceased owner's estate, and as such, is subject to estate tax like any other asset owned by the decedent at the time of his or her death. This consequence can be avoided by having a trust own a policy.

3. Irrevocable Life Insurance Trusts.

One technique for excluding life insurance proceeds from an insured's estate is to have a third person or trustee own all incidents of ownership in a policy. The transfer of a policy to a trust, or the purchase of a policy by a trustee, is preferable to an outright gift. An outright transfer of a policy to a domestic partner

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[257] *See* RCW 48.18.030.

[258] *See* Mary Ann Mancini & Howard M. Zaritsky, *Insurable Interests? Après Chawla, le Deluge?*, 32 ACTEC J. 194 (Winter 2006).

[259] *Id*. at 196.

[260] *See e.g.*, N.Y. Ins. Law §3205.

[261] Mancini & Zaritsky, *supra* note 258, at 224.

[262] IRC §101(a)(1).

[263] IRC §2042(1) & (2).

may be problematic if the relationship terminates. If the transferor is the one paying the premiums, he or she always has the option of allowing the policy to lapse.

The taxation of life insurance proceeds can be avoided under present law if a trust owns all incidents of ownership in a policy (*e.g.*, the right to surrender, revoke, assign, pledge or borrow against the policy or change the beneficiary).[264] A trust holding life insurance is commonly referred to as an irrevocable life insurance trust ("ILIT").

A trust may be drafted to exclude the partner as a beneficiary if the relationship terminates. Moreover, the terms of the ILIT may provide that, at the death of the insured, the proceeds may be made available to the insured's estate to create liquidity through loans between the trustee of the trust and the insured's personal representative.

In most states, a fiduciary may use trust funds to purchase life insurance on the life of a beneficiary or the life of another in whose life a beneficiary has an insurable interest.[265] In addition, an insured may obtain a policy on his or her own life and freely transfer ownership of that policy to a new owner.[266] As stated above, in some states, it is not clear whether a trust can obtain a policy that will ultimately benefit someone without an insurable interest, in all states. In those states where insurable interest is an issue, in spite of the potential estate tax consequences, it may be preferable to have the insured purchase a policy and gift it to an ILIT.

a. The Mechanics of the Irrevocable Life Insurance Trust.

An ILIT is operated as follows: Each year, the grantor transfers money to the trust in an amount slightly greater than the amount sufficient to cover the annual premium on the policy.[267] The beneficiaries are given withdrawal rights each year (the right to demand distribution of a stipulated amount of the trust corpus) for a limited period of time following the gifts to the trust, so that each

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[264] IRC §101(a)(1).

[265] *See, e.g.*, RCW 11.100.120.

[266] *See, e.g.*, RCW 48.18.360.

[267] For a more detailed explanation, *see* Howard M. Zaritsky & Stephan R. Leimberg, *Tax Planning With Life Insurance: Analysis With Forms* (2d ed. 1998) and Richard C. Baier, *Drafting Flexibility Into An Irrevocable Life Insurance Trust*, 19 Prob. & Prop. 62 (Sept./Oct. 2005) [hereinafter "Zaritsky & Leimberg"].

transfer qualifies for the gift tax annual exclusion. This right is known as a "Crummey" right of withdrawal, and its purpose is to qualify the gift as a present interest and therefore eligible for the annual exclusion from gift tax.[268] Once the beneficiary's demand power expires (assuming it goes unexercised), the funds may be accumulated in the trust. In the first year, the trustee uses the cash to purchase life insurance, typically on the life of the grantor. Thereafter, the trustee uses the cash to pay the annual premium. There are several additional technical requirements that must be observed in order for the proceeds to be excluded from estate taxation.[269]

A trust agreement may provide that the grantor's partner is to be the beneficiary of the policy proceeds, provided that the insured and her partner are in a committed relationship at the time of her death. If not, the trust agreement could provide for the proceeds to be distributed to other beneficiaries.

A potential insured can allocate a portion of his or her generation-skipping transfer tax exemption to the trust each year that is equal to the value of the year's gifts to the trust, and by these allocations, the entire trust corpus (including the insurance proceeds payable upon the insured's death) can be sheltered from the GST tax for multiple generations. The GST exemption is allocated (on a timely filed Form 709 United States Gift and Generation-Skipping Transfer Tax Return), only to the cash transferred to the trust to pay the premiums.[270] The insurance proceeds typically exceed the total premiums by a substantial amount. As a result, the life insurance trust offers an opportunity to "leverage" the use of the GST exemption.

b. The Transfer of a Preexisting Policy.

Whether the insured is expected to die within three years is a critical consideration when planning for an insurance trust. Where

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[268] In *Crummey v. Comm'r*, 397 F.2d 82 (9th Cir. 1968), the court held that by creating a window of time during which beneficiaries of certain trusts may exercise a demand power to withdraw funds that are added to the trust, the gifts subject to the withdrawal are present interests that qualify for the gift-tax annual exclusion under IRC §2503(b).

[269] *See* Zaritsky & Leimberg, *supra* note 267, at 165.

[270] Alternatively, allocation of GST exemption may be made on a late filed return, in which case GST exemption would be allocated in an amount equal to the actual value of the insurance purchased, as of the first day of the month of filing the late return, which in most cases is less than the amount of cash contributed to purchase that insurance. Treas. Reg. §26.2642-2(a)(2). *See* Kathryn G. Henkel, *Estate Planning and Wealth Preservation: Strategies and Solutions* at §5.05(2)(a) (1998). However, a late allocation cannot be made if the insured individual dies before the actual date of filing the return. *Id*.

a preexisting policy is transferred to a trust, if the insured does not survive for three years following the date of the transfer, the proceeds generally will be subject to tax in the insured's estate.[271] However, if the trustee purchases the insurance from its inception, the proceeds will be excludable from the insured's estate, without the application of the three-year rule applicable to transferred policies, provided that the insured did not retain any incidents of ownership that would cause inclusion of the trust property in his or her estate.

4. Using Partnerships and LLCs With Life Insurance.

Partnerships and LLCs can be useful for domestic partners who desire to transfer life insurance policies between themselves. Where an existing life insurance policy is transferred for valuable consideration, the transfer for value rule provides that proceeds received at the insured's death are exempt from income tax, but only to the extent of the sum of the consideration paid and the premiums subsequently paid by the purchaser of the policy.[272] The transfer for value rule does not apply, however, where the transfer is to the insured, a partner of the insured, a partnership in which the insured is a partner, or a corporation in which the insured is a shareholder. Thus, a life insurance policy may be transferred, with or without consideration, to a partnership, without causing the life insurance proceeds to lose their tax-free character.

The IRS concluded in PLR 9309021 (March 5, 1993) that a partnership could be created solely for the purpose of owning insurance. The anti-abuse rules (Treas. Reg. §1.701-2), however, are intended to eliminate the use of a partnership when the principal purpose of the partnership is to reduce substantially the partners' aggregate federal tax liability in a manner that is inconsistent with Subchapter K of the Code. In order to avoid running afoul of the anti-abuse rules, it is a good idea to use an entity that has some other purpose besides owning insurance.

5. Private Split-Dollar Life Insurance Arrangements.

Split-dollar is a method used to finance life insurance premiums where the owner of the policy and a third party agree to split the

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[271] IRC §2035(a)(2).

[272] IRC §101(a)(2). For a thorough analysis of the transfer for value rule, *see* Lawrence Brody & Stephan R. Leimberg, *Avoiding the Tax Trap of the Transfer for Value Rule*, 32 Est. Plan. 3 (Oct. 2005) and Lawrence Brody & Stephan R. Leimberg, *Using a Transactional Analysis to Avoid the Transfer for Value Rule*, 32 Est. Plan. 3 (Nov. 2005).

responsibility for paying premiums and the right to receive the policy proceeds.[273] Split-dollar insurance arrangements are commonly used in the employment context, where the employer provides the money for most or all of the premiums, but the employee's beneficiary gets most of the death benefit. In exchange for paying the premiums, the employer retains the right to a portion of the pre-maturity cash value, or the death benefit, equal to the premiums paid by the employer. Thus, the employer ultimately gets all of its money back.

Split-dollar insurance may be used in non-employment situations as well, in which case it is referred to as "private split-dollar." A common structure for this arrangement between unmarried couples is for the wealthier partner to make annual exclusion gifts to an ILIT owning a policy on his life. The less wealthy partner is named beneficiary of the trust, but has no control over the incidents of ownership in the policy. The trustee of the ILIT uses the amounts gifted to the trust to pay a portion of the premium equal to the economic benefit to the beneficiary (the value of the pure life insurance protection). The wealthier partner will pay the remainder of the premium directly. In exchange for the direct premium payments, the Trustee agrees to repay the premiums out of the policy proceeds or cash surrender value. Each year, the amount paid directly by the wealthier partner is treated as a loan to the trust. If interest is paid at or above the AFR, the imputed interest rules of IRC §7872 would not apply. If the interest is at a below-market rate, the annual forgone interest will be treated as an additional gift to the trust. Alternatively, the arrangement could be treated as an economic benefit, in which case the economic buildup in the policy would be taxed annually.[274]

It is generally recommended that the arrangement be treated as a series of loans, where interest is paid or accrued at the applicable federal rate, and not as an economic benefit arrangement, to avoid taxation on the equity buildup in the policy.[275] When an ILIT is

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[273] For a complete explanation of the income, estate and gift tax consequences of split-dollar arrangements, *see* Donald O. Jansen, *Taxation of Split Dollar Life Insurance Arrangements under the Final Regulations*, 29 ACTEC J. 285 (Spring 2004), Charles Ratner, *The Post-Split Dollar World*, 142 Tr. & Est. 18 (Dec. 2003) [hereinafter "Ratner, *The Post-Split Dollar World*"], and Charles L. Ratner & Stephan R. Leimberg, *A Planner's Guide to Split-Dollar After the Final Regulations*, 31 Est. Plan. 3 (Jan. 2004).

[274] *See also* PLR 200747011 (Nov. 23, 2007) for a discussion of private split-dollar arrangements between individuals and a revocable trust.

[275] *See* Treas. Regs. §§1.61-22(j)(1)(ii), 1.83-6(a)(5)(ii)(A), 1.301-1(q)(4)(i) & 1.7872-15(n), IRS Notice 2002-8, 2002-1 C.B. 98 (which governs the determination of the economic benefit), and Ratner, *The Post-Split Dollar World*, *supra* note 273, at 20.

structured as a grantor trust and the payments are treated as a series of loans, the grantor would typically make a gift to the trust equal to the loan interest, but the interest payments from the trust back to the grantor/insured would not be treated as income to the grantor.

Unlike in the employment situation, it has been suggested that the policy should not be assigned as collateral. This prevents the entire insurance proceeds from being included in the insured's estate under IRC §2042(2), because of a retained incident of ownership in the policy. Instead, the trust would retain all rights and interests with respect to the term insurance component of the policy. But there is a significant risk that without a collateral assignment, the plan might not qualify as a split-dollar arrangement. Treasury Regulation §1.61-22(b)(1) requires that the payor of the premiums must be able to recover those premiums from, or have them secured by, the proceeds of the life insurance policy.[276] Alternatively, it may be possible to provide a collateral assignment limited to the right of repayment to the insured in the event of surrender of the policy or death of the insured.[277]

Private split-dollar arrangements may prove useful where a wealthier partner would like to finance the purchase of a life insurance policy by the less wealthy partner, but retain a right to those premium payments. However, the best practices under the new regulations are yet to be determined.

6. Viatical Settlement.

A viatical settlement is the sale or assignment of a life insurance contract to a third party.[278] The third party then becomes the beneficiary under the policy and assumes the premium payments. Similarly, the receipt of accelerated death benefits has allowed terminally ill persons to receive a portion of their life insurance benefits prior to death. The Health Insurance Portability and Accountability Act of 1996 ("HIPAA")[279] addressed the income tax consequences of viatical settlements and accelerated death benefits.[280] Prior to the enactment of HIPAA, sale proceeds and

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[276] Donald O. Jansen, *Split Dollar Has Split – So How Do We Finance Premiums Now?*, 38 Inst. on Est. Plan. ¶1300 (2004).

[277] *Id.*

[278] *See* Damien Ríos, *An Introduction to the Use of Viatical and Life Settlements*, 31 Est. Plan. 533 (Nov. 2004) for a thorough examination of this topic.

[279] Pub.L. No. 104-191, 110 Stat. 1936, 2067.

[280] *See* Bernard Eizen & Victor S. Levy, *New and Expanded Uses of Viatical Settlements in Insurance Planning*, 26 Est. Plan. 475 (Dec. 1999).

accelerated death benefits generated taxable income to the insured. Furthermore, IRC §2035 applied to such transfers, which provides that if a life insurance policy is transferred by gift by the insured within three years of death, the policy proceeds will be included in the transferor's gross estate.

HIPAA enacted IRC §101(g), which excludes certain death benefits and payments from the insured's gross income. To qualify for this exclusion, the insured must be either "terminally ill"[281] or "chronically ill"[282] and the sale or assignment must be to a qualified "viatical settlement provider."[283]

Additional rules limit the amounts that may be received tax-free in any year under a viatical settlement arrangement. Amounts in excess of the prescribed limits are treated as follows: (i) where the policy is surrendered, the cash surrender value is treated as ordinary income; (ii) where the policy is sold the cash surrender value less the insured's investment in the contract (adjusted basis or cost of insurance) is treated as ordinary income; and (iii) where the policy is sold but has no cash surrender value the proceeds less the value of the prorated unexpired premium are treated as long-term capital gain.[284]

The purpose of the HIPAA legislation was to allow the proceeds of a viatical settlement or an accelerated death benefit to be spent on medical expenses or to maintain the insured's standard of living. However, viatical settlements can be used by healthy individuals as well to obtain cash, which can be gifted or spent. If the proceeds do not fall within the scope of IRC §101(g)(2), amounts realized will be included in gross income to the extent of gain from the

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[281] An individual who has been certified by a physician as having an illness or physical condition that can reasonably be expected to result in death within 24 months. IRC §101(g)(4)(A).

[282] An individual who is determined by a licensed health practitioner as (i) being unable to perform, without substantial assistance, at least 2 activities of daily living for at least 90 days due to a loss of functional capacity; (ii) having a similar level of disability as defined in regulations; or (iii) requiring substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment. IRC §101(g)(2)(B)(iii).

[283] A qualified viatical settlement provider is defined as a person, meeting certain licensing and disclosure requirements, regularly engaged in the business of purchasing or taking assignments of life insurance contracts on the lives on insured individuals who are terminally ill or chronically ill. IRC §101(g)(2)(B).

[284] *See* Rev. Rul. 2009-13, 2009-21 I.R.B. 1029 in which the Service considers the tax consequences to an individual who sells or surrenders a policy insuring his or her own life, and Rev. Rul. 2009-14, 2009-21 I.R.B. 1031, in which the Service addresses the tax consequences to the purchaser of a policy on the secondary market.

transaction, under IRC §1001(a).[285] Not all states permit the sale of policies by individuals who are not terminally ill.

Many states have adopted a form of the Life Settlements Model Act, developed by the National Conference of Insurance Legislators. The Act generally regulates parties who enter into life settlement contracts with insured under life insurance policies, provides a system of licensing providers and brokers of life settlement contracts, and restricts the sale of policies for the purpose of settling them or entering into loans secured by the policies.[286]

If a client anticipates taking advantage of viatical settlement or accelerated death benefits, it is important that he or she retain all of the incidents of ownership in the insurance policy to preserve these planning options.

F. Estate Freezes and Planning Under Chapter 14.

Unmarried couples are able to take advantage of planning opportunities available under Chapter 14 of the Code that are unavailable to married couples.

1. Purpose of Chapter 14.

Chapter 14 deals with transfers among traditional family members, and addresses perceived abuses in certain transactions, known as "freeze" transactions, used to pass property from one generation to the next at a reduced transfer tax cost.[287] This type of transaction essentially involved a gift by a member of the older generation to members of the younger generation to "freeze" the gift at its gift tax value. Any post-gift appreciation was removed from the donor's gross estate and shifted to the donee. Techniques, such as retaining an interest in or imposing restrictions on the property, were used to maximize the value of the retained interest or restrictions and as a result, minimize the value of the gift. The purpose of Chapter 14 is to ensure that the value assigned to a

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[285] *See* Andrew H. Hook & Thomas D. Begley, Jr., *Lawyering for Older Clients: A New Paradigm – Part 1*, 32 Est. Plan. 48, 54 (April 2005) for a discussion regarding calculation of gain in this context.

[286] The model act can be found at www.insurereinsure.com/files/upload/2005368I.pdf (adopted Nov. 2007). Adopted by Washington as RCW ch. 48.102.

[287] Chapter 14 was added to the Code as part of the Omnibus Budget Reconciliation Act of 1990, Pub.L. No. 101-508, §11602, 104 Stat. 1388, §1388-491, as amended by the Small Business Job Protection Act of 1996, Pub.L. No. 104-188, §1702f, 110 Stat. 1755, §1870, generally effective for transactions after Oct. 8, 1990.

retained interest or restriction for gift tax purposes comports with the economic reality of the transaction.[288]

Because unmarried partners are not considered family members within the definition of Chapter 14, certain techniques that are limited or no longer available to married partners under Chapter 14 remain available to unmarried couples, which are discussed below.

2. Section 2701 – Transfers of Interests in Corporations and Partnerships.

a. Types of Transactions Affected by Section 2701.

Section 2701 of the Code imposes gift tax on certain transfers of an interest in a corporation or partnership.[289] Section 2701 is triggered when: (i) the transferor makes a transfer to, or for the benefit of, "a member of the transferor's family,"[290] and (ii) "an applicable family member"[291] retains an interest immediately after the transfer.

b. Valuation of Interests Subject to Section 2701.

The value of the gift subject to IRC §2701 is equal to the transferor's entire interest before the gift, less the value of the rights and interests retained by the transferor. Unless the retained rights meet certain requirements or are otherwise excluded from the statute, the value of the retained rights will be considered zero and the value of the gift will be equal to the value of the entire interest prior to the transfer.

c. Transfers Outside of Section 2701.

Transfers between unmarried partners or transfers by one partner to the child of the other partner are not considered transfers between family members under IRC §2701 and thus the special

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[288] *See* Adena W. Testa, 835-2nd Tax Mgmt. (BNA) *Chapter 14* (1999) for a thorough discussion of Chapter 14.

[289] IRC §2701(a)(1)(B).

[290] A member of the transferor's family is defined as the transferor's spouse, lineal descendants of the transferor or the transferor's spouse, and the spouse of any such lineal descendant. IRC §2701(e)(1); Treas. Reg. §25.2701-1(d)(i). Stepchildren are included as members of the transferor's family because they are descendants of the transferor's spouse.

[291] An applicable family member includes the transferor's spouse, an ancestor of the transferor or the transferor's spouse, and the spouse of any such ancestor. IRC §2701(e)(2); Treas. Reg. §25.2701-1(d)(ii). Thus, IRC §2701 applies to a transfer when certain interests are retained by the transferor (or the transferor's spouse) or by persons who are senior to the transferor.

valuation rules should not apply with respect to valuing the interests retained by the donor and transferred to the donee. Instead, normal valuation techniques and rules are used, without taking into account the requirements of Chapter 14. Thus, the partner with greater wealth can transfer assets to a partnership, retain a non-cumulative preferred return and a preference upon liquidation, and transfer to his partner, or partner's child, a junior equity interest that carries with it the right to all future appreciation.

Presumably, the gift of the junior equity interest will be small at first, and thus it will have little value for gift tax purposes. All appreciation will accrue to the junior equity interest as the value of the entity increases, and if the rights associated with the preferred interest are not exercised, the shift of wealth is magnified even more.

3. Section 2702 – Transfers in Trust.

a. Types of Transactions Affected by Section 2702.

IRC §2702 addresses the valuation of transfers in trust where the transferor (or an applicable family member)[292] retains an interest in the trust. Suppose an individual creates a trust for the benefit of his or her family member, with the remainder to his or her children. Unless the interest in trust is a qualified interest, it will be valued under IRC §2702 at zero.[293] In most cases, this means that the entire value of property transferred to the trust would be treated as a taxable gift, even though the value of the gift to the remainder beneficiaries may actually be less (using traditional valuation rules applicable to arm's length transaction that would apply Treasury valuation tables).

If the gift in trust is instead a "qualified interest," it will be valued under IRC §7520 and subtracted from the value of the entire property to determine the value of the property gifted.[294]

b. Permissible Transfers Under Section 2702.

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[292] An applicable family member includes: (i) an individual's spouse; (ii) any ancestor or lineal descendant of the individual or the individual's spouse; (iii) any sibling of the individual; or, (iv) any spouse of any individual described in the prior categories. IRC §2702(e) (referencing IRC §2704(c)(2)).

[293] IRC §2702(a)(2).

[294] IRC §2702(a)(2)(A).

A qualified interest includes the right to receive an annuity payment from a grantor retained annuity trust (GRAT),[295] the right to receive a unitrust payment from a grantor retained unitrust (GRUT),[296] and the right to remain in a residence held in a qualified personal residence trust (QPRT).[297]

Unrelated parties are not subject to the valuation provisions of IRC §2702. Thus, it is not necessary to use a GRAT, a GRUT, or a QPRT. Instead, unrelated parties are still able to use split-interest purchases, establish common law grantor retained interest trusts (GRITs), and some of the restrictions applicable to related parties with respect to QPRTs do not apply.

(a) Grantor Retained Interest Trusts.

A grantor retained interest trust ("GRIT") is an irrevocable trust, in which the grantor retains an income interest for a term of years, and at the end of the term, the trust estate is paid to a named individual or individuals, provided that the grantor is then living.[298]

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[295] A GRAT is typically created by transferring (ideally) high-yield assets into an irrevocable trust, while retaining the right to a qualified annuity interest for a specified term. Upon the termination of the term the trust property passes to remainder beneficiaries. The amount of the taxable gift is reduced by the value of the grantor's annuity interest. The value of the retained interest is determined under IRS actuarial tables, which value the interest based on the value of the property transferred, the term of the trust, the size of the annuity, and the IRC §7520 rate in effect in the month of transfer. If the trust investments outperform the IRC §7520 rate used to value the gift, the excess inures to the benefit of the remaindermen and will not be subject to transfer tax. If the grantor dies during the retained term, the trust property is included in the grantor's gross estate. If the grantor survives the retained term the trust property, along with any appreciation, passes without further estate or gift tax.

[296] With a GRUT the grantor transfers income-producing assets into an irrevocable trust. The grantor retains the right to receive payments equal to a percentage of the value of the assets, revalued annually. A GRUT is also a qualified interest under IRC §2702(b), but has little estate planning utility.

[297] The QPRT is a type of irrevocable trust that is used to transfer an interest in a residence at a discounted value at the end of a defined term. Treas. Reg. §25.2702-5. The trust lasts for a term of years (no more than 20), during which time the grantor can retain ownership of the house. At the end of the term the house would pass to the remainderman (presumably, the grantor's partner), shifting any appreciation during the trust term to the remainderman. If properly structured, the value of the gift to the remainderman escapes the valuation provisions of IRC §2702, and instead the gift is valued under valuation rules applicable to third-party transactions. The tax advantages of a QPRT depend on the grantor surviving the trust term. If the grantor does not survive the trust term, the entire value of the trust's interest in the residence at the grantor's death will be included in the grantor's estate for estate tax purposes. Therefore, the estate and gift tax advantages will be lost, but the effect will usually be the same as if the QPRT had not been established. When the grantor establishes the QPRT there is an immediate taxable gift of the remainder interest in the residence, the value of which is less than the value of the residence, because the value of the grantor's right to use the residence for the trust term is subtracted from the fair market value of the residence. The longer the trust term, the lower the value of the reportable gift to the remaindermen.

[298] *See* Mark W. Smith, *Reconsider the GRIT*, 144 Tr. & Est. 24 (Dec. 2005)

GRITs were very popular prior to the enactment of Chapter 14. But Chapter 14 eliminated their use if the remainder beneficiary was a "family member." Because an unmarried partner does not fall within the definition of family member as defined in IRC §2702(e), a GRIT can be an excellent way to allow a wealthier partner to provide an income stream during the retained trust term and allow the principal to pass at a reduced transfer tax value at the expiration of the term.

The grantor of a GRIT places property in an irrevocable trust and retains the right to income for a specified term. Ideally, highly appreciating property will be used to fund the trust and the growth and therefore the amount passing to the remainder beneficiary or beneficiaries will exceed the projections for gift tax purposes.[299]At the end of the term, the property may remain in trust or be distributed outright for designated beneficiaries (typically the grantor's partner or the partner's children). If the grantor survives the term, then the property is excluded from the grantor's gross estate. If the grantor dies before the end of the term, the corpus would be includable in the grantor's estate.[300]

The benefit of the GRIT is that the fair market value of the property transferred is reduced by the value of the grantor's retained interest in determining the gift tax value of the transfer.[301] The value of the retained income interest, like the value of a GRAT's annuity interest, is based on the actuarial value of the remainder interest (the value of the property transferred, the length of the retained term, the grantor's age (if the grantor retains a contingent reversionary interest), and the IRC §7520 rate in effect in the month of the transfer). Any appreciation in the trust property is transferred to the remainder beneficiaries, provided the grantor survives the trust term.

(b) Qualified Personal Residence Trusts.

If one partner establishes a qualified personal residence trust ("QPRT") for the benefit of an unrelated party, they are not subject to the sale prohibitions otherwise applicable to QPRTs.[302] Thus, the opportunity for a sale between a grantor and a trust holding the grantor's personal residence remains available. The grantor may purchase the residence from the trust just prior to the expiration of the grantor's retained term so that cash or other assets pass to the remaindermen in place of the residence. Because this is a transaction between a grantor and his or her wholly owned grantor trust, no gain or loss is recognized by the grantor.[303] Moreover, if the grantor owns the residence at death, the

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[299] Mark W. Smith, *supra* note 298, at 26.

[300] IRC §2036(a).

[301] Treas. Reg. §25.2512-5(d)(2).

[302] *See* Jeremy T. Ware, *Using QPRTs to Maximum Advantage for Wealthy Clients*, 32 Est. Plan. 34 (Nov. 2005) for a general discussion concerning QPRTs. For trusts created after May 16, 1996, Treas. Reg. §25.2702-5(c)(9) requires a QPRT's governing instrument to prohibit the trust from selling or transferring the residence, directly or indirectly, to the grantor, the grantor's spouse, or an entity controlled by the grantor or the grantor's spouse, at any time during the original retained term and at any time after the original term interest during which the trust is a grantor trust.

[303] IRC §671 and Treas. Reg. §1.671-2(b). *See also*, Rev. Rul. 85-13, 1985-1 C.B. 184.

grantor's estate, and the ultimate beneficiary, will receive the benefit of a step-up in basis under IRC §1041 to the date-of-death value of the residence.

It is also important to note that it is not entirely clear whether unrelated parties may establish QPRTs with cotenancy interests in a residence. The issue arises because: (i) the property must have its primary use as the grantor's residence, (ii) the grantor must have the exclusive right of occupancy, and (iii) the property may not be used other than as a residence when the grantor is not there.[304] Shared occupancy is permissible, so long as it is at the sufferance of the grantor. There are no rulings concerning QPRTs established by cotenants that are not also spouses.[305] Therefore, the regulations suggest that the exclusive right of occupancy requirement precludes the establishment of QPRTs with cotenancy interests if the cotenants/donors are not also spouses.[306]

Where a cotenant with a non-spouse wishes to establish a QPRT, one approach to accomplish the exclusive occupancy requirement is to have that cotenant lease the property from the other co-tenants during the QPRT term.[307]

(c) Split-Interest Purchases.

Because of the disadvantages of a QPRT, clients may want to consider some of the alternatives. One is the split-interest purchase. A split-interest purchase involves the division of the total purchase price: One person contributes an amount equal to his or her life interest value or an interest for a term of years, while the other person contributes an amount equal to the value of the remainder interest following the termination of the term interest. If the joint purchasers are applicable family members for purposes of IRC §2702, the person acquiring the term interest is treated as acquiring the entire property and then transferring the remainder interest to the other purchaser, and the retained interest (generally a life estate) is valued at zero unless the retained interest constitutes a qualified interest.[308]

If the joint purchasers are not applicable family members, the valuation rules of IRC §2702 do not apply to the transaction. Again, all appreciation in the purchase is shifted to the survivor at the end of the term of years.[309]

(d) Sale of a Remainder Interest.

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[304] Treas. Reg. §25.2702-5(b)(2)(iii).

[305] Natalie B. Choate, *The QPRT Manual: The Estate Planner's Guide to Qualified Personal Residence Trusts* ¶2.3.02 (2004).

[306] John A. Hartog, *QPRTs for Co-Tenancy Interests – Do they Work?*, 6 Cal. Tr. and Est. Q. 4 (Fall 2000).

[307] Natalie B. Choate, *supra* note 305, at ¶2.3.02.

[308] IRC §2702(c)(2).

[309] *See* Robert S. Schwartz, *IRS Approves Split-Purchase Qualified Personal Residence Trust*, 13 Prob. & Prop. 54, 55 (March/April 1999) for an analysis of this topic.

Another QPRT alternative is the sale of a remainder interest. The sale of a remainder interest may also be preferable to a QPRT because the seller may retain use of the residence for life, instead of a term of years, rent-free. It also avoids the concern that the grantor might not survive the QPRT term.

This technique is not without risk. Undervaluation of the remainder interest could cause the remainder interest to be brought back into a life tenant's estate under IRC §2036. To withstand scrutiny, the purchasers of the remainder interest should use funds held for some time and not merely received as a gift just prior to the transaction. The sale of a remainder interest also needs to comply with the personal residence trust and qualified personal residence trust regulations set forth in Treas. Reg. §25.2702-5(a).[310]

If the residence is sold during the lifetime of the life tenant(s) and the proceeds are not reinvested in a replacement residence, or converted to a qualified annuity trust, the proceeds must be paid to the life tenant. One alternative would be to provide in the purchase and sale agreement of the remainder interest that the sale of the residence during the lifetime of the life tenant(s) is prohibited.

With a QPRT or life estate, the life estate or primary beneficiary of the trust must pay for maintenance, utilities, insurance, taxes and repairs. Where the remainder interest has been sold, the payment for improvements by the life tenant is treated as an additional gift.

Mortgage interest is the responsibility of the life tenant. Principal payments are considered additional gifts, however, unless the debt is secured by property other than the residence prior to the sale of the remainder or transfer to the QPRT. Or the grantor could retain the obligation and enter into an indemnification agreement with the trust or remainder beneficiary in the event the lender attempts to realize on the security interest.

4. Section 2703 – Valuation of Restrictive Agreements.

a. Types of Transactions Affected by Section 2703.

Section 2703 of the Code applies to buy-sell agreements and other options and restrictions on the right to acquire or use property. IRC §2703 provides that certain restrictive agreements will not be considered in valuing corporate or partnership interests for estate and gift tax purposes.

Unlike the other sections of Chapter 14, IRC §2703 applies to all restrictive arrangements, regardless of the identity of the parties. An arrangement covered by IRC §2703 may be contained in a partnership agreement, articles of incorporation, bylaws, or a

[310] *See* PLR 200840038 (Oct. 3, 2008).

shareholder agreement.[311] A right or restriction "implicit in the capital structure of the entity" may also trigger the application of IRC §2703.[312] Section 2703 treats the lapse of certain rights, such as voting and liquidation rights, as a gift by, or includible in the gross estate of, the owner of the lapsed right.

The definition of "member of the family" under IRC §2703 is considerably broader than under the other Chapter 14 sections. A "member of the family" includes family members as defined in Treas. Reg. §25.2701-1(d): The transferor's spouse; lineal descendants of the transferor or the transferor's spouse; and the spouse of any such lineal descendant. Thus, nieces, nephews, stepchildren, and siblings-in-law are included in this definition. A "family member" may also be any other individual who is a natural object of the transferor's bounty.[313]

The regulations do not define "natural objects of the transferor's bounty."[314] Accordingly, it is not clear whether domestic partners may escape the application of IRC §2703, or whether the Service will attempt to use this language to extend this section's coverage.

b. Valuation Under Section 2703.

Generally, a right, option or agreement that restricts the sale or use of property is disregarded for valuation purposes, unless: (i) it is a bona fide business arrangement; (ii) it is not a device to transfer such property to members of the decedent's family for less than full and adequate consideration in money or money's worth; and (iii) its terms are comparable to similar arrangements entered into by persons in an arm's-length transaction.[315] If an agreement meets all three tests, then the IRS will consider the agreement in determining value. Furthermore, if unrelated individuals own more than 50% of the interests in the business, the tests are deemed to be satisfied.[316]

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[311] Treas. Reg. §25.2703-1(a)(3). *See* Edward A. Renn & N. Todd Angkatavanich, *Sabotaged: Don't Let a Buy-Sell Agreement Blow Up an Estate Plan*, 145 Tr. & Est. 52 (April 2006) for an analysis of buy-sell agreements in the estate planning context.

[312] *Id.*

[313] Treas. Reg. §25.2703-1(b)(3).

[314] *See* Richard M. Horwood, *et al.*, 813-3rd Tax Mgmt. (BNA), *Estate Planning for the Unmarried Adult* at A-27 (2010) for a discussion of the meaning of this phrase.

[315] IRC §2703(a) & (b).

[316] Treas. Reg. §25.2703-1(b)(3).

Failure to meet all three of the tests may subject the arrangement to IRC §2703(a). Thus, even non-family members may need to show that a business arrangement was the result of an arm's-length negotiation for full and adequate consideration.[317] But the IRS generally presumes that a person's own self-interest will prevent that person from entering into agreements to transfer property to non-family members for less than full and fair value.

A right or restriction is considered to meet each of the three tests if more than 50% by value of the property subject to the right or restriction is owned directly or indirectly by individuals who are not members of the transferor's family.[318] Thus, the issue as to whether the transferee is a family member will most likely be determinative of whether the restriction will be respected for valuation purposes.

An agreement meeting all three tests may be used to freeze the value of preferred interests, pay out income to the preferred partner/member and deflect future growth to the other class of interests, typically the poorer partner, and/or that partner's children, in this context.

5. Section 2704 – Lapsing Rights and Restrictions.

IRC §2704 treats the lapse of certain rights as a taxable transfer. Between family members, if a lapse occurs at death, the value of the right -- in addition to the individual's interest in the corporation or partnership -- is included in the individual's estate. IRC §2704 also disregards for gift tax purposes "applicable restrictions"[319] on the ability of an entity to liquidate if family members possess the power to remove the applicable restriction.[320]

In certain family-controlled LLCs and partnerships, valuation discounts obtained through restrictions on liquidation may be disregarded for purposes of valuing the transferred interest under IRC §2704(b). Under that provision, if there is a transfer of an interest in a partnership/LLC among family members, and the transferor and members of the transferor's family control the

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[317] Treas. Reg. §25.2703-1(b)(2).

[318] Treas. Reg. §25.2703-1(b)(3).

[319] An applicable restriction is one that limits the ability of an entity to liquidate if: (i) the restriction lapses, in whole or in part, after a transfer of an interest to or for the benefit of the transferor's family; or (ii) after the transfer, the transferor or any member of the transferor's family has the right to remove the restriction. IRC §2704(b)(2); Treas. Reg. §25.2704-2(b).

[320] IRC §2704(b)(1).

partnership/LLC, then restrictions on the transferor's liquidation rights that are more restrictive than the state law default provision will be disregarded, resulting in a higher transfer tax value.

The restrictions under IRC §2704 should not apply to lapsing rights and restrictions between non-family members.[321]

For example, a restriction on a member's ability to withdraw from an LLC, which lapses upon the death of a certain member, would be ignored for valuation purposes if the LLC were among family members. Similarly, a lapsing right to liquidate the entity, to receive a guaranteed liquidation value, and/or to receive a preferred return, would also be ignored if applied to family members. However, those restrictions will be recognized for purposes of applying discounts when valuing an unrelated partner's interest in the entity for estate tax purposes.

Unmarried partners should be able to take advantage of substantial discounting opportunities through the use of partnerships, LLCs, and other entities with restrictive provisions, allowing interests in these entities to be transferred between partners at death or during their lifetimes at a reduced transfer tax cost.

G. Miscellaneous Strategies To Transfer Wealth Between Partners.

The following strategies, some of which are prohibited between family members, can be used to transfer wealth to the less wealthy partner.

1. Annual Exclusion and Similar Gifts.

In addition to annual exclusion gifts from the wealthier partner to the less wealthy one, unmarried couples can take advantage of the exclusion for the payment of educational, health and dental expenses (including health insurance premiums), so long as they are made directly to the provider.[322] Educational expenses may include tuition (but not books, supplies, room, board or other living expenses) and medical expenses may include doctor and hospital bills, medically necessary home improvements, costs of necessary home health care providers and anything else that an individual would be allowed to deduct on an income tax return as an unreimbursed medical expense under IRC §213. One person can

[321] IRC §2704(c)(2) defines the term "member of the family" with respect to any individual as: (i) the individual's spouse; (ii) any ancestor or lineal descendant of the individual or the individual's spouse; (iii) any sibling of the individual; and (iv) any spouse of any individual described in the prior categories.

[322] IRC §2503(e).

also pay another's long-term health care insurance provided that the "eligible long-term care premiums" limits of IRC §213(d)(10)(B) are not exceeded.

2. Sale to Recognize Loss.

The disallowance of losses on sale or exchange of property to another family member under IRC §267 does not apply. Thus partners may sell stock to each other to recognize losses so long as there is adequate consideration. As a result, the purchase price becomes the transferee's basis.

3. Hiring a Partner as an Employee.

One partner may own a professional services corporation that the other partner provides services for. This avoids the high tax rate professional service corporations are subject to when the services are provided by an owner. In many instances, one partner may be able to employ the other for services for which they would otherwise have to pay an outside party. Of course, the income received must be reported by the recipient partner.

Business owners who hire their partner can deduct a portion of the cost of health insurance and long-term care insurance as a fringe benefit.

4. Installment Sales.

To create a stream of income for the wealthier partner and transfer assets to the less wealthy partner, one partner may sell rental property to the other in return for a promissory note under IRC §453. This has the effect of transferring income from one partner to the other, while preserving a stream of income to the former owner of the rental property in the form of interest income on a note, which may be recognized over time.

5. Private Annuities.

Another way to create a stream of income for the wealthier partner and transfer assets to the less wealthy one is to have one partner sell property to the other in exchange for a private annuity. A private annuity is a contract that provides for specified payments to the named annuitant during the annuitant's lifetime.[323] This is similar to the installment note arrangement, but under a private

[323] *See* Edward P. Wojnaroski, 805-4th Tax Mgmt. (BNA), *Private Annuities and Self-Canceling Installment Notes* (2010).

annuity, the payments never cease so long as the annuitant is alive, even if the annuitant outlives his or her life expectancy. The disadvantage of the private annuity is that, unlike promissory notes used with installment sales, private annuities cannot be secured, putting the annuitant at risk that the buyer may default. Furthermore, gain or loss must be recognized at the time of the exchange rather than deferred.[324]

6. Stock Redemptions.

IRC §302(a) provides that a redemption of stock "shall be treated as a distribution in part or full payment in exchange for the stock," if any of the exceptions set forth in IRC §§302(b)(1)-(4) apply. The exceptions apply if the redemption is not essentially equivalent to a dividend (with no reduction for basis), and the redemption proceeds will therefore be taxed as ordinary income, rather than capital gain.[325]

Typically, a complete redemption of a shareholder's interest in a company will fall under the exception of IRC §302(b)(3), and result in the proceeds of the redemption being subject to capital gain treatment. Where a member of a family group is redeemed, and other members of the group of related parties owns stock in the company, the attribution of stock ownership rules under IRC §318 prevent the exiting shareholder from falling under the exception of IRC §302(b)(1) (because the redeemed shareholder's stock will continue to be attributed back to the exiting shareholder).

But, where unrelated partners own a closely held business together, the attribution of stock ownership rules do not apply. Thus, the ability to accomplish a substantially disproportionate redemption of stock or a complete liquidation of a shareholder's interest under IRC §302(b) may be available. As a result, the value of the stock redeemed may be treated as capital gain, rather than a dividend.

7. Retirement Benefits.

Most pension plans cease payments at the death of an unmarried employee. However, some plans may provide for a "term certain" form of benefit payout, which allows a set amount to be paid out to the employee, and if not then living, named beneficiaries, over a predetermined number of years. This election is typically less favorable as one for an employee and a surviving spouse. But, it

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[324] Treas. Reg. §1.72-6.

[325] IRC §302(b)(1).

can provide some benefit to an unmarried surviving partner where no other benefits would be available if the employee partner were to die earlier than expected.

8. Transfer on Death Accounts/Deeds and Community Property Agreements.

Transfer on death security registration has been widely adopted, and allows for the transfer of a security or brokerage account by beneficiary designation.[326] To date, 13 states have adopted transfer on death deed statutes[327] modeled on the Uniform Real Property Transfer on Death Act, passed by the National Conference of Commissioners on Uniform State Laws in July 2009.[328] These forms of property ownership avoid probate, do not require an immediate transfer, and one partner may continue to control his or her property during life.

In states where RDPs may use a community property agreement effective at death to transfer property to the survivor, such as California and Washington, these should be considered.

It is also important to keep in mind that clients who move from a community property state to one that has adopted the Uniform Disposition of Community Property Rights at Death Act ("UDCPRDA")[329] could benefit by preserving the community property treatment of any property traceable to community property. To that end, property placed in a joint trust should reflect the factors set forth in Rev. Rul. 66-283, describing a joint trust holding community property of a California husband and wife. Notwithstanding the Act, rights to real property are typically determined by the law of the state in which it is located.[330]

XIII. Charitable Planning

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[326] Adopted as Cal. Prob. Code §§5500-5512 in California, RCW ch. 21.35 in Washington, and ORS 708A.495 in Oregon.

[327] *See* Dennis M. Horn & Susan N. Gary, *Death Without Probate: TOD Deeds – The Latest Tool in the Toolbox*, 24 Prob. & Prop. 13 (March/April 2010); David Major, *Revocable Transfer On Death Deeds: Cheap, Simple, and Has California's Trusts & Estates Attorneys Heading For the Hills*, 49 Santa Clara L. Rev. 285 (2009) for background on, and history of, the transfer on death deed.

[328] 8B U.L.A. 125 (Supp. 2011).

[329] States that have adopted the UDCPRDA are: Alaska, Arkansas, Colorado, Connecticut, Florida, Hawaii, Kentucky, Michigan, Montana, New York, North Carolina, Oregon, Virginia, and Wyoming, 8A U.L.A. 213 (Supp. 2011).

[330] Terrance J. Mullin, *Understanding the Testamentary Effects of Community Property Rules*, 79 Fla. Bar J. 49 (Jan. 1, 2005).

When unmarried partners share the same intent with respect to their charitable giving (although conceivably even when they do not), a number of planning opportunities exist. Because they are unable to take advantage of the marital deduction, unmarried couples often perceive that there is less available to give to charity. Some of the vehicles described below may actually allow one partner to transfer more wealth to a partner than he or she would be able to transfer otherwise. Most of the vehicles discussed below also have the benefit of avoiding probate, which often reduces the likelihood of challenges from family members or other individuals who may be hostile to the surviving partner.[331]

A. Charitable Remainder Trusts.

In general, a charitable remainder trust ("CRT") is an irrevocable trust that makes payments – at least annually – to one or more beneficiaries, at least one of which is not a charitable entity, for a term of not more than 20 years, or for the life or lives of the individual beneficiaries.[332] It is also possible, to a certain extent, to define the trust term with respect to both a term of years and one or more lives.[333] When the non-charitable interest or interests terminate, the remainder interest passes to one or more qualified charitable organizations.[334]

A CRT may be structured as either a charitable remainder annuity trust ("CRAT") or a charitable remainder unitrust ("CRUT"). A CRAT pays the non-charitable beneficiary a fixed dollar amount that is specified in the trust agreement and that is neither less than 5% nor more than 50% of the initial value of the trust's assets. Thus, the payout from a CRAT does not vary from year to year. A CRUT pays a fixed percentage (no less than 5% and no more than 50%[335]) of the value of the trust property as valued annually, meaning distributions can fluctuate based on the increase or decrease in value of the trust. Because the distributions from a CRAT cannot increase over time, it is less frequently used than is a CRUT.

A CRT is exempt from income tax unless it has unrelated business taxable

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[331] Chris J. Yates, *The Unmarried Penalty: Gift, Estate Tax, and Other Considerations for Unmarrieds*, Gift Planner's Digest (Sept. 26, 2000).

[332] *See* Robert J. Rosepink, *Charitable Remainder Trusts and Pooled Income Funds*, 865-2d Tax Mgmt. Portfolio (2008) and Sanford J. Schlesinger & Martin R. Goodman, *Back to Basics: A Primer for Charitable Remainder Trusts*, 32 Est. Plan. 9 (March 2005) for a thorough discussion of this topic. Another useful planning tool, but one beyond the scope of this article, is the nonqualified CRT. *See* J. Michael Pusey, *What if the Estate Tax is Repealed? Part I*, http://www.pgdc.com/pgdc/what-if-estate-tax-repealed-part-i (posted June 23, 2003), and the footnotes thereunder for a discussion of this technique.

[333] IRC §664(d).

[334] IRC §§664(d)(1) & (2).

[335] IRC §664(d)(1)(A).

income, which is taxed at a rate of 100%.[336] Tax is paid by each annuity or unitrust beneficiary as distributions are received, according to the four-tier system set forth in IRC §664(b). As a result, the trustee may receive appreciated assets and then liquidate them and reinvest the proceeds, without immediate capital gain tax consequences.

In the year of funding, the grantor of an *inter vivos* CRT may claim an income tax charitable deduction for the present value of the remainder interest that will pass to charity, subject to certain restrictions.[337] One of those restrictions is that, to qualify as a CRT, the actuarial value of the remainder eventually passing to charity must be at least 10% of the value of the trust estate at the date the trust is funded.[338] A CRT may have multiple beneficiaries, either concurrently or serially, although additional recipients reduce the likelihood that the trust will meet the 10% threshold. Similarly, a CRT is rarely available for use with very young beneficiaries (unless the trust term is limited to a period of years), because their longer life expectancies will also tend to cause the amount actuarially anticipated to pass to charity to fall below the 10% threshold.

A testamentary CRT can be a useful tool, especially in planning for large retirement accounts. Estate and income tax costs can be mitigated by leaving a retirement plan to a testamentary CRT rather than outright to a surviving partner. Using a CRT will allow the surviving partner to receive income from the retirement account, subject to income tax only upon receipt. The estate of the deceased partner will receive a charitable deduction for the present value of what will eventually pass to charity.

An *inter vivos* CRT created by one partner for the benefit of other partner may give rise to gift tax consequences upon formation. A gift on formation can be avoided by having the grantor create a CRT for the grantor's life, followed by the life of the partner, with a retained right to terminate the survivorship interest.[339] The resulting gift will be the same if the partner survives the grantor and if the grantor did not exercise the right, but the present value of the survivorship income interest will be included in the grantor's taxable estate.[340]

Some commentators have suggested that the retained right to terminate could be further limited to situations where the relationship has

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[336] IRC §664(c).

[337] IRC §170(f)(2) and IRC §2522(c)(2).

[338] IRC §664(d)(1)(D) & IRC §664(d)(2)(D).

[339] Treas. Reg. §1.664-2(a)(4) & Treas. Reg. §1.664-3(a)(4).

[340] Treas. Reg. §25.2511-2(c).

terminated.[341] Alternatively, the named surviving partner might want more security against termination. In this case, instead of a reserved testamentary power to terminate the surviving partner's interests, the grantor partner may agree to make a completed gift but build into the trust a provision that if the relationship terminates, so does the surviving partner's interest. In any event, this kind of plan can lead to some insecurity on the part of the potential surviving beneficiary. On the other hand, it can create some security for the grantor, who may not necessarily feel comfortable with the otherwise irrevocable nature of the CRT.

Creation of a CRT may have gift or estate tax consequences because the marital deduction is not available.[342] However, the charitable deduction for the value of the remainder passing to charity will lessen the tax due as a result of conferring a benefit on the other partner.

CRTs with unrelated grantors should generally be avoided. The IRS determined, in PLR 9547004 (August 9, 1995) that a CRT established by a husband, wife and 6 grandchildren qualified as an association, rather than a trust, under Treas. Reg. §301.7701-2(a)(1), and thus could not qualify as a CRT.[343]

B. Charitable Lead Trusts.

A charitable lead trust ("CLT") could be used to provide a stream of income to one or more charities for a term of years or for the life or lives of one or more individuals, and thereafter provide support for a partner. At the end of the charitable lead term, the trust terminates and the trust estate can be paid to the partner, as well as to children. Like a CRT, a CLT may be structured to pay a unitrust amount or an annuity, although the payment, as a percentage of the initial value of trust assets (annuity trust) or of the value of trust assets as it may change from year to year

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[341] Jerry Simon Chasen & Elizabeth F. Schwartz, *Estate and Gift Tax Planning for Nontraditional Families*, 15 Prob. & Prop. 6, 10 (Jan./Feb. 2001). In a similar situation involving a heterosexual divorce, the IRS ruled that a CRT containing a termination provision if the parties divorced, as well as a provision that one spouse could terminate the interest of the survivor by will, was permissible. PLR 9511029 (March 17, 1995). *See also* PLR 200430012 (July 23, 2004) in which the IRS ruled that a contingency to terminate a CRAT upon the earlier of the surviving spouse's death or remarriage was a qualified contingency.

[342] In addition, if an inter vivos CRT is established by a donor for the benefit of his or her partner, and if the donor dies before the partner and has retained the right to change charitable beneficiaries, one commentator has asserted that under certain circumstances, the overall transfer tax cost might be higher than if the right to change charitable beneficiaries had not been retained by the donor. Alan F. Rothschild, Jr., *Designing and Documenting Charitable Gifts*, http://www.pgdc.com/pgdc/designing-and-documenting-charitable-gifts (posted Oct. 27, 2005).

[343] *See also* PLR 200203034 (Jan. 18, 2002). Note, however, that the IRS, in its safe-harbor CRUT and CRAT revenue procedures stated that it is permissible to have multiple grantors if they are spouses. Rev. Proc. 2003-53 through Rev. Proc. 2003-60, Rev. Proc. 2005-52 through Rev. Proc. 2005-59.

(unitrust) can be less than 5% or more than 50%. In addition, if the trust is to last for a term of years, the period may be longer than 20 years. Finally, whereas CRTs are tax-exempt entities when administered properly, CLTs are taxable trusts.

If structured as a grantor trust (usually as a result of the donor reserving a reversionary interest, in which case nothing is distributed to a partner or to children when the trust ends), the grantor would receive an income tax deduction in the year the trust is funded, for the present value of the payments made to charity. No gift tax is due because a gift tax charitable deduction applies to the present value of the payments to charity, with the balance reverting to the donor and therefore not being treated as a gift. During the term of the grantor CLT, the donor is taxed on the income but does not receive a further charitable contribution deduction for the payments to charity.

More typically, however, *inter vivos* CLTs are structured as non-grantor trusts, in which case the grantor receives at the time of transfer a gift tax charitable deduction for the present value of the payments to charity during the trust term. This means he or she is treated as having made a taxable gift equal to the present value of the non-charitable remainder interest. Nevertheless, the trust, not the grantor, will be taxed on the income passing to charity during the term of the trust. Interestingly, if the trust lasts long enough or has a high enough payout rate, the amount subject to gift tax can be reduced to zero.

Care should be devoted to determining which scenario makes sense for a particular client, based, in part, on whether he or she would benefit from the immediate income tax charitable deduction for the grantor CLT, or if the client would prefer a non-grantor CLT in order to pass wealth on to others and to avoid the annual income tax liability of the grantor CLT. Particularly if a non-grantor CLT is being contemplated, the client should give thought to funding it with assets that are likely to increase in value significantly, thereby leveraging the impact of the gift tax charitable deduction.[344]

It is important to take into consideration the rules regarding permissible measuring lives when a charitable lead trust is established for the life of one or more individuals.[345] Each remainder beneficiary must be a lineal

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[344] Of course, when assets are distributed to the remainder beneficiaries, those assets retain the donor's cost basis, even if the donor has since died. In other words, there is no step-up in basis in connection with the donor's death, and a beneficiary could recognize substantial gain upon sale of an asset that had been in the trust.

[345] Treas. Reg. §1.170A-6(c)(2)(i) & (ii). There must be less than a 15% probability that persons who are not lineal descendants of the measuring individuals will receive any portion of the trust corpus.

descendant or spouse of a descendant of the individual lives used as measuring lives, which would include stepchildren and step-grandchildren. Thus, the measuring lives must be chosen carefully.

The testamentary CLT may be used as a substitute for a marital deduction type trust. In this situation, the gift to the remaindermen would be included in the donor's estate, but the gift to charity would qualify for the estate tax charitable deduction. A testamentary CLT is generally used when children and/or the surviving partner do not need immediate access to the funds (perhaps because a CRT has been established concurrently to provide a stream of income during the term of the CLT), as the non-charitable beneficiaries will not receive their interest until the CLT terminates.

Because the individual beneficiary of a CLT does not receive distributions until the term of the trust has expired, and then only if he or she survives the charitable term, this vehicle works best for younger individual beneficiaries, particularly children and grandchildren.

CLTs are far less common than CRTs, likely due to the relatively larger value of assets needed for a CLT to be applicable. Still, in the proper circumstances, a CLT can be useful, often in combination with a CRT.

C. Charitable Gift Annuities.

Couples may also consider using a charitable gift annuity ("CGA") to satisfy their charitable intentions while securing a stream of payments that benefit one or both members of the couple for life. A CGA is like a CRT in that the donor receives in the year the payments are arranged an income tax charitable deduction for part of the value of the assets contributed. Unlike a CRT, however, payments may be made to no more than two persons (whether consecutively or on a joint-and-survivor basis), and they may not be made for a term of years.

Thus, a CGA involves a gift to a specific charity, in exchange for the charity's promise to pay an annuity. By contrast, a CRT is indeed a trust arrangement and can potentially benefit many charities. A CGA could be for the life or lives of *any* two persons, although typically it would be for the life of the donor, the life of the partner, or both lives.

An unmarried couple's use of a CGA presents potential disadvantages. For example, if appreciated property is used to fund the annuity, the taxable gain, calculated under the bargain sale rules, must be fully recognized by the donor in the year the annuity is created (unless the donor is the sole or initial annuitant, in which case the gain may be

prorated over the donor's life expectancy calculated as of the time payments begin).[346]

In addition, if the annuity is created by one member of the couple and payable to the other, there are very likely to be gift tax consequences upon formation. If the annuity is paid first to the donor and then to the partner, or if the partner is an annuitant of a deferred payment gift annuity, then the gift tax annual exclusion – which applies only to gifts of present interests – will not be available to offset any portion of the present value of the payments. Therefore, in certain cases, the donor might consider retaining in the gift annuity contract a right to revoke the partner's annuity interest, either on a testamentary basis or during the lifetime of the donor.[347]

In lieu of establishing a CGA during life to benefit a partner, a donor could do so through his or her will.[348] Alternatively, the donor could arrange now for a CGA to be funded upon death with a distribution from his or her IRA.[349] Finally, even though technically a CGA could be funded with assets owned jointly by both members of a couple,[350] the simpler and preferable approach would be to create separate CGAs established by each of the partners with his or her own assets.

D. Pooled Income Funds.

A pooled income fund ("PIF") is a taxable trust established and administered by a public charity.[351] A donor to a PIF irrevocably transfers assets (usually cash or publicly-traded securities other than municipal bonds) to a trustee. The assets of all donors who have contributed to the PIF are commingled and invested like a mutual fund. Donors to the fund receive units of participation in the fund based on the pro rata value of their contributions relative to the total value of the fund. Each year for life, a variable share of the total income from the fund is paid to the donor and/or other beneficiaries designated by the donor. The term of the non-charitable interest may not be for a period of years. It must be for the life

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[346] Treas. Reg. §1.1011-2(a)(4).

[347] Frank Minton, Edith Matulka and J. William Zook, Jr. *Charitable Gift Annuities: The Complete Resource Manual* 2:11-22 (2003).

[348] *Id*. at 20:17-19.

[349] *Id* at 16:17-20 and PLR 200230018 (July 26, 2002).

[350] Minton, *supra* note 347, at 2:14.

[351] The technical requirements for a pooled income fund are set forth at IRC §642(c)(5). *See* John H. Clymer, *Pooled Income Funds: A Good Vehicle for Smaller Charitable Gifts*, 24 Est. Plan. 310 (Aug./Sept. 1997) and *Pooled Income Fund*, http://www.pgdc.com/pgdc/pooled-income-fund (posted May 3, 2003) for a comprehensive analysis of pooled income funds.

of the beneficiary or beneficiaries.[352] Qualified contingencies are not specifically authorized to be used to terminate a beneficiary's interest, nor are they prohibited.[353] At the death of the beneficiary or beneficiaries of the units associated with the donor's contribution, a proportionate share of the assets of the PIF is conveyed to the charity.

For an *inter vivos* transfer of assets to a PIF, a donor is entitled to both income and gift tax charitable deductions in the year of the gift, based on the present value of the remainder interest passing to charity.[354] Likewise, a testamentary contribution to a PIF results in an estate tax charitable deduction for the present value of the remainder interest. A donor does not generally recognize gain or loss on the transfer of property to a pooled income fund.[355] Instead, the fund takes on the basis and holding period of the assets transferred. However, where the gift is to someone other than the charity and the donor, he or she makes a taxable gift of the income interest (or the applicable portion thereof) that benefits the other person or persons.

A donor can postpone a taxable transfer to another individual recipient by retaining a testamentary right to revoke that interest, causing the gift to be incomplete.[356] However, the donor should not retain a lifetime right to revoke.[357] If a power to revoke has not been retained, then the present value of the future income payments to be received by the non-spouse/non-donor recipient is considered a present interest gift.

A PIF can be an attractive charitable giving vehicle for a donor with certain highly appreciated assets because neither the donor nor the PIF is taxed on any of the gain, so long as the PIF always pays out all of its income. Nevertheless, the payments made by a PIF are fully taxable as ordinary income to the recipient, whereas the payments made by a CRT or a CGA are often taxed more favorably. Finally, relatively few charities maintain PIFs, and those PIFs that do exist often make payments at

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[352] Treas. Reg. §1.642(c)-5(b).

[353] There is no equivalent to the qualified contingency provision under IRC §664(f) for charitable remainder trusts, applicable to pooled income funds.

[354] Inter vivos gifts are covered by IRC §170(f)(2)(A) & IRC §2522(c)(2), and testamentary gifts by IRC §2055(e)(2).

[355] Treas. Reg. §1.642(c)-5(a)(3). There is an exception, however, for debt-encumbered property, the transfer of which is treated as a bargain sale. IRC §1011-2.

[356] Treas. Reg. §1.642(c)-5(b)(2).

[357] *See* Mary C. Hester & Lizbeth A. Turner, *Retaining a Right to Revoke an Interest in a Charitable Plan*, 32 Est. Plan. 26, 27 (June 2005) for a complete discussion of the tax consequences of a retained right to revoke.

relatively modest rates (i.e., below 5%), so this technique will be an option only in a limited number of cases.

E. Gifts of Remainder Interests in Personal Residences and Farms.

A couple may benefit from giving a personal residence or farm to a charity, subject to the reservation of a life estate. Where a home is involved, it must be a personal residence, but need not be the primary residence.[358] Reasonable surrounding grounds, determined by the customary lot size in the area, may also be included in the charitable gift. The gift of the remainder interest could take effect at the end of one or two lives, or a term of years.[359]

While the gift itself is made by means of a simple deed, there should also be separate documentation regarding the rights and responsibilities of the charity and of the life tenant or tenants. Customarily, life tenants will be required to pay property taxes, utilities, liability and casualty insurance, maintenance expenses, and similar costs.

If the donor makes the gift during life, he or she receives income and gift tax charitable deductions for the present value of the charity's remainder interest. In addition, if the property is appreciated the donor does not recognize any capital gain. If the gift is made on a testamentary basis, the donor's estate is entitled to an estate tax charitable deduction for the present value of the charity's remainder interest.

This arrangement is most useful with a residence that is not subject to a mortgage and for couples that do not intend to pass the property on to further generations or heirs. If one partner makes the gift, it might be possible for the other partner to re-acquire the gifted property from the charity at a later date, as only the remainder interest will need to be purchased. Additional options exist if the life tenant – whether the donor or the partner – wants or needs to move out of the residence. He or she can rent the property to another tenant; contribute the remaining life interest to the charity (perhaps for a CGA) and receive a deduction for the present value of the remaining life interest; or agree with the charity to sell the property and divide the proceeds according to the respective interests of the parties.

F. Simple Wills and Disclaimer Planning.

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[358] A farm is defined as land that is used for the production of agricultural products, including crops or timber. Treas. Reg. §1.170A-7(b)(4).

[359] Treas. Reg. §1.170A-7(b).

Even though subject to probate, and therefore to challenge by disapproving family members, basic wills can make sense for unmarried couples with estates modest enough in size that they likely will not be subject to transfer taxes. A basic will that is suitable for many married couples can also work well for people who are not married, provided they agree on the ultimate beneficiaries of their estates. Naturally, if there are children or other descendants to be considered, one partner's will may need to differ from the other's. Yet in many cases, an "all to my partner if she survives me but otherwise all to charity" disposition will be practical.

For a couple with charitable intent, qualified disclaimers can be used to further that intent. A qualified disclaimer allows the disclaimed interest to be treated for federal tax purposes as if it had never been transferred to the individual disclaiming, thus avoiding gift or estate tax.[360]

A disclaimer must be completed within nine months of the interest being created and it must be in writing. As a result of the disclaimer, the property must pass to an individual or organization other than the disclaimant without any direction by the disclaimant (exceptions apply with respect to disclaimers resulting in property passing to an opposite-sex spouse but not yet to a same-sex spouse or partner).[361] As a result, a disclaimer to a charitable vehicle where the disclaimant would possess a life income interest, such as a CRT or CGA, would not be qualified, and therefore ineligible for an estate tax deduction.

Nevertheless, in the unmarried couple context a disclaimer provision could provide that disclaimed assets are to pass to a particular charity. As a result, the asset will be treated as if it passed directly from the decedent to charity, eligible for an estate tax charitable deduction equal to the value of the property disclaimed.

XIV. Estate Planning for the Transgender Client

While planning for the transgender client is beyond the scope of this paper, there are a few issues that are discussed below.[362]

A. Name Change.

Legal recognition of sex and name change is an important step for a transgender adult, for self determination as well as safety and the ability to

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[360] IRC §2046 & §2518.

[361] IRC 2518(b)(4), Treas. Reg. §25.2518-2(e)(1)(ii).

[362] For a thorough and thoughtful analysis of this topic, *see* A. Spencer Bergstedt, *Symposium: Issues in Estate Planning for Same-Sex and Transgender Couple. Estate Planning and the Transgender Client*, 30 W. New Eng. L.Rev. 675 (2008). This section is based, in part, on his materials.

work, travel and function in society. Each state has a different procedure by which this may be accomplished.[363] In some states this is permitted by common law, in others there is a statutory procedure.

In Washington this is done in district court and may be completed in one day.[364] Illinois law allows an Illinois resident to change his or her name by filing a petition in the circuit court of the county in which he or she resides.[365] Similarly, in California a name change may be obtained by filing a petition in superior court in the county where the person whose name is to be changed resides.[366]

Some states simply deny a transgender person's name change, and, a legal change in one state might be denied recognition in another.[367]

B. Change of Gender Identifier on Various Documents.

Next, a client is likely to change the gender on government issued documentation such as a driver's license, birth certificate, green card, military identification, selective service registration, professional licenses, pilot license and other federal or state issued identification. In our mobile economy, legal photo identification is crucial.[368] It is important that photo identification match the current identification of a client. Without this identification, an individual's ability to travel, drive, have access to financial institutions and credit, obtain employment and security clearances, make certain purchases, obtain medical treatment, enter

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[363] *See* Becky Allison, M.D., *U.S. States and Canadian Provinces: Instructions for Changing Name and Sex on Birth Certificates* www.drbecky.com/birthcert.html (last update 2011) for a summary of name change rules and procedures in the U.S. and Canada.

[364] RCW 4.24.130.

[365] 735 Ill. Comp. Stat. 5/21-101. *See* the Illinois State web site for the procedure and contact information: Illinois Vital Records: Gender Reassignment, www.idph.state.il.us/vitalrecords/gender.htm (last updated 2011).

[366] California Code of Civil Procedure §1275.

[367] *In re Estate of Gardiner*, 273 Kan. 191, 42 P.3d 120, *cert. denied Gardiner v. Gardiner*, 537 U.S. 825 (2002); (the Wisconsin court ordered a new birth certificate with changed name and sex to be issued, the transgender plaintiff argued unsuccessfully that Kansas must give full faith and credit to a Wisconsin court order and birth certificate; instead, Kansas Supreme Court held that the marriage of a transwoman and man violated its policy against same-sex marriage.) *In re Marriage License for Nash*, Nos. 2002-T-0149, 2002-T-0179, 2003 WL 23097095 (Ohio Ct. App. Dec. 31, 2003) (an amended Massachusetts birth certificate is considered by Massachusetts to be *prima facie* evidence, but not conclusive proof, of the facts recorded therein; full faith and credit is not violated when granting full faith and credit to another state's record that would violate Massachusetts' public policy (here, Ohio's policy against same-sex marriage).)

[368] *See, e.g.*, California Health and Safety Code §103425 regarding the modification of a birth certificate in California. For further information on California law *see* Transgender Law Center, www.transgenderlawcenter.org/ (last updated 2011).

government buildings and engage in a whole host of other activities will be severely limited.

Each state sets its own procedure for name and gender changes on identification documents. For changing a driver's license, typically some type of evidence of adoption of a different gender is required. Birth certificates are harder to change. Some states provide by statute how they may be changed and some states do not allow changes. Those that allow amendment may issue new birth certificates or simply strike out the old information and write in the new.[369] Under California law, the old birth certificate is sealed and a new one issued.

The Social Security Administration[370] requires evidence of sexual reassignment before allowing a change of gender identification, and until recently the Department of Homeland Security (for U.S. Passports[371]) followed the same rule, which limits the ability of most transgender individuals to change these documents (since reassignment surgery is not necessarily opted for by all transgender adults).

As of June 10, 2010, the U.S. Department of State announced that when a passport applicant presents a certification from an attending physician that the applicant has undergone appropriate clinical treatment for gender transition, the passport will reflect the new gender. It is also possible to obtain a limited-validity passport if the physician's statement shows the applicant is in the process of gender transition. No additional medical records are now required and sexual-reassignment surgery is no longer a prerequisite for passport issuance. The new policy and procedures are based on standards and recommendations of the World Professional Association for Transgender Health, recognized by the American Medical Association as the authority in this area of medicine.[372] The new policies and procedures contain a model letter for licensed physicians to certify to an applicant's gender change.[373] It also provides guidelines where an

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[369] California law permits a transgender individual born there, and who has undergone sex-reassignment surgery to obtain a new birth certificate, at which point the old birth certificate is sealed. Cal. Health & Saf. Code §103425. *See* http://www.courts.ca.gov/1105.htm (last visited Sept. 15, 2011) for California name and gender change forms.

[370] The Social Security Act is codified at Chapter 7 of Title 42 of the U.S. Code. *See generally* 42 U.S.C. §§301-1399..

[371] The Secretary of State has the authority to grant and issue passports under 22 U.S.C. §211a.

[372] The U.S. Department of States passport rules regarding gender change are found at 7 U.S. Department of State Foreign Affairs Manual (FAM) – Volume 7 Consular Affairs §1320 Appendix M, Documents to be Submitted with Passport Application, www.state.gov/documents/organization/143160.pdf (Jan. 20. 2011).

[373] *Id.*

applicant's original passport gender marker was incorrect, and other situations that arise from time to time.[374]

While a passport and social security card are not as important as a driver's license, on a daily basis, they may lead to a gender mismatch, which could be brought to the attention of an employer and other agencies requesting various legal documents. The Social Security Administration in the past, notified an employer with a "No-Match Letter" if the information they had on file associated for an employee did not match the information provided by the employer.[375] As of September 2011, The Social Security Administration (SSA) announced that it will no longer allow gender to be matched in its Social Security Number Verification System (SSNVS). This will result in the immediate cessation of SSA sending notifications that alert employers when the gender marker on an employee's W-2 does not match Social Security records.[376]

Female to male transgender adults need not register for selective service. The Selective Service has a form to elect out of registering entitled "Request for Status Information Letter" found at www.sss.gov/PDFs/SilForm_Instructions.pdf (Aug. 4, 2009). This letter can be requested from the Selective service at (847) 688-6888. The applicant should not make any of the automated choices and wait for a representative.

C. Tax Considerations.

In a remarkable 69-page opinion with 70 pages of concurring and dissenting opinions, the Tax Court ruled in *O'Donnabhain v. Comm'r*,[377] that a male to female gender reassignment surgery qualifies as a deductible medical expense under IRC §213, in part (contrary to the Service's position in Chief Counsel Advice 200603025). Specifically, the court held that hormone therapy and sexual reassignment surgery costs are deductible medical expenses but that breast augmentation surgery costs are not deductible. The Tax Court acknowledged that the taxpayer had been diagnosed with gender identity disorder, a medically recognized "disease" within the meaning of IRC §213(d)(1)(A) and that the taxpayer's hormone therapy and sex reassignment surgery treated this

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[374] *Id.*

[375] For more on No-Match Letters, see www.nctequality.org/Resources/NoMatch_employees.pdf and http://transequality.org/Resources/NCTE_SSA_2011.pdf.

[376] Nan Hunter, *Social Security Ends No Match Letters for Gender Difference*, Hunter of Justice, http://hunterforjustice.typepad.com/hunter_of_justice/2011/09/ss-ends-no-match-.html?utm_source=feedburner&utm_medium=email&utm_campaign=Feed%3A+HunterOfJustice+%28hunter+of+justice%29 (posted Sept. 16, 2011).

[377] 134 T.C. No. 4 (Feb. 2, 2010).

disease. The court concluded, however, that breast augmentation procedure served only to improve her appearance, so this expense was nondeductible as cosmetic surgery.

D. Marriage.

The validity of a marriage is determined by the couple's status at the time the marriage is performed. If a couple was legally able to marry under state law when (and where) they entered into the marriage, they remain married until death or divorce. As a result, transgender individuals may be able to enter into heterosexual marriages after undergoing sexual reassignment surgery. Furthermore, if spouses were of different genders at the time of their marriage, the marriage should remain valid even if one spouse later transitions to become the same sex as his or her spouse.

Some states take the position that gender is determined at birth and that reassignment surgery will not be recognized.[378] However, many other states recognize as valid a heterosexual marriage where, prior to the marriage, one member of the couple changed genders.[379]

Another issue beyond the scope of this paper is whether DOMA can be used to bar foreign transgender individuals from obtaining legal

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[378] The following are just a few of the cases demonstrating the disparate treatment from state to state: *In re Marriage of Simmons*, 355 Ill. App. 3d 942, 825 N.E.2d 303 *appeal denied*, 216 Ill. 2d 734 (2005) (pursuant to Illinois Vital Records Act, 410 ILCS 535, the State Registrar issued a new birth certificate with changed name and sex, but the court held that "the mere issuance of a new birth certificate cannot, legally speaking, make petitioner a male;" issuance of birth certificate is "ministerial act" that generally does not involve fact-finding. Therefore a male birth certificate was found to be not conclusive of male sex and as a result, the individual's marriage was deemed invalid. *Littleton v. Prange*, 9 S.W.3d 223 (Tex. App. 1999), *cert. denied*, 531 U.S. 872 (2000) (the court held that it is not bound by an amended birth certificate except to allow corrections to information that was inaccurate at the time of birth). *In re Ladrach*, 32 Ohio Misc. 2d 6, 513 N.E.2d 828 (Prob. Ct. 1987) (an Ohio birth certificate statute only authorizes corrections if there was an error in the original entry). *K. v. Health Division*, 277 Or. 371, 560 P.2d 1070 (1977) (this case reversed a Court of Appeals order granting new birth certificate changing sex based on statutory interpretation, and held that a statutory change is a matter of public policy to be decided by the legislature, until which issuing a new birth certificate will not be permitted.) *Darnell v. Lloyd*, 395 F.Supp. 1210 (D. Conn. 1975) (the State Commission of Health violated Connecticut's equal protection clause by denying some requests for birth certificate changes and must show a substantial state interest for its policy of refusing to change birth certificates to reflect sex change.) *In re Heilig*, 372 Md. 692, 816 A.2d 68 (2003) (the petitioner sought a court order to change name and sex, but not birth certificate because the petitioner was born out of state; the Court of Appeals held that jurisdiction exists to determine and declare that a person has changed gender, but that the petitioner did not sufficiently establish a gender change, remanded to the lower court where the petitioner has the burden to present sufficient medical evidence of relevant criteria for determining gender and of the fact that, based on that criteria, he has completed a permanent and irreversible change from male to female.)

[379] *In re Anonymous (Anonymous II)*, 293 N.Y.S.2d 834, 835, (N.Y. Civ. Ct. 1968); *In re Lovo-Lara*, 23 I.& N. Dec. 746, 753 (B.I.A. 2005) in which the BIA found a North Carolina marriage between a post-operative transsexual female and a foreign male to be valid because North Carolina allows a person to amend his or her birth certificate following gender-reassignment surgery.

immigration status as a spouse of a U.S. citizen, in order to reside in the U.S.[380]

E. Practice Pointers.

When drafting legal documents, in addition to the other provisions that might be included, it is important to make statements about the principal's identity, using names and pronouns consistent with the principal's identity that he or she is to be identified by, unless inconsistent with the client's wishes. It is also advisable to give the fiduciary the right and the directive to preserve that identity postmortem.

XV. Strategies to Minimize Conflict

The practitioner and the testator should understand the grounds for contesting a will, such as improper execution, incompetence of the testator, duress, undue influence, and fraud. Family members, especially those unhappy or surprised about learning that a loved one was gay or lesbian, or unwilling to accept that a relationship existed between partners who never married, may challenge a will, alleging fraud, duress, undue influence, or mental incapacity of the decedent. The possibility of disgruntled family members disputing an estate plan is far greater with unmarried couples.[381]

To deter will contests, practitioners use a number of strategies discussed below:[382]

A. *In Terrorem* Clauses.

In states where permitted, *in terrorem* clauses are only useful if a potential contestant is actually in danger of losing something.[383] As of January 1, 2010, California permits contests in very limited circumstances as set forth in Cal. Prob. Code 21311,[384] applicable to instruments that became

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[380] *See* Rachel Duffy Lorenz, *Comment: Transgender Immigration: Legal Same-Sex Marriages and Their Implications for the Defense of Marriage Act*, 53 UCLA L.Rev. 523 (Dec. 2005).

[381] Kathleen Ford Bay, *Estate Planning for Unmarried Couples: What's Different and What's the Same?*, 2004 Am. College of Tr. and Est. Counsel Annual Meeting, at 3.

[382] For additional drafting recommendations to avoid conflict over an estate plan, *see* Bruce Stone & Bruce S. Ross, *Bombproofing the Estate Plan to Anticipate and Avoid Litigation 2.0*, 44th Ann. Philip E. Heckerling Inst. on Est. Pl., U. of Miami Law Center (2010).

[383] Bay, *supra* note 381, at 7.

[384] (a) A no contest clause shall only be enforced against the following types of contests:

(1) A direct contest that is brought without probable cause.

(2) A pleading to challenge a transfer of property on the grounds that it was not the transferor's property at the time of the transfer. A no contest clause shall only be enforced under this paragraph if the no contest clause expressly provides for that application.

irrevocable on or after January 1, 2001.[385] The safe harbor provided by Cal. Prob. Code §21320, which previously allowed a beneficiary to obtain an advance ruling as to whether a proposed legal action would be considered a "contest" for purposes of a no contest clause, is no longer available.

Unless a client is willing to give a potential contestant a gift, such a clause may only create a false sense of security.[386] If a client insists on including an *in terrorem* clause, and they are willing to make a gift to the person or persons they are concerned about, below is a sample clause to consider:

> If any beneficiary hereunder shall in any way, directly or indirectly, contest or object to the probate of this Will, or dispute any provision hereof, or exercise or attempt to exercise any right to take a share of my estate against the provisions of this Will, or institute or prosecute, or be in any way, directly or indirectly, interested or instrumental in the institution, or prosecution, of any action, proceeding, contest or objection, or give any notice for the purpose of setting aside or invalidating this Will, or any provision hereof, then all provisions for such beneficiary or for his or her descendants contained herein shall be void, and I give the property or share of my estate to which such beneficiary or his or her descendants would have been entitled hereunder in like manner as if such beneficiary and all his or her descendants were then deceased, or if such beneficiary is a corporation or other entity, that it had ceased to exist prior to my death. No provision of this article shall apply to Article ___ or to any religious, charitable, scientific, literary or educational organization, a bequest to which is deductible for federal estate tax purposes.

B. Statement That Omission of a Family Member Is Intentional.

It is generally not recommended to make statements in a will as to why certain individuals have not been provided for. Such statements may incite an individual to contest a plan where, in the absence of such a

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(3) The filing of a creditor's claim or prosecution of an action based on it. A no contest clause shall only be enforced under this paragraph if the no contest clause expressly provides for that application.

(b) For the purposes of this section, probable cause exists if, at the time of filing a contest, the facts known to the contestant would cause a reasonable person to believe that there is a reasonable likelihood that the requested relief will be granted after an opportunity for further investigation or discovery.

[385] Cal. Prob. Code §21315.

[386] *Id.*

statement, that person might not have.[387] Worse, it might be grounds for a testamentary libel claim.[388] Alternatively, a client might consider making positive statements about why the client has chosen to benefit his or her partner over others.[389]

C. Evidence of the Client's Capacity at the Time of Execution.

It is also strongly recommended that the attorney extensively interview the client, in the presence of the witnesses, regarding his or her intent, his or her assets, and the objects of his or her bounty.[390] The attorney should keep detailed notes of this meeting, signed and dated by the witnesses.[391] Witnesses should be articulate, and likely to make a good impression if asked to testify.[392] The attorney may also obtain a statement from the client's physician as to the client's capacity.

Some attorneys videotape the execution. However, this might well be used as evidence supporting a lack of competency. While tempting because it seems like a good idea at the time, taping or videotaping should only be used with extreme caution. "Many people do not come across well on videotape and if you rehearse the ceremony on film, the other side will undoubtedly want to see the entire video, not just the polished product."[393] Similarly, tape recording should be avoided. In *Discipline of Miller*,[394] the drafting attorney recorded the signing ceremony in a failed attempt to demonstrate his client's testamentary intent. At the drafting attorney's malpractice trial, the Court relied on the tape recording as evidence that the testator did not understand the scope of the gift that she made (to the drafting attorney in violation of Washington's RPC 1.8(c)).

For those who can't be dissuaded from their wish to video record the will execution ceremony, Gerry W. Beyer has written a step-by-step guide for

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[387] Bay, *supra* note 381, at 8.

[388] *Id*. *See also* Paul T. Whitcombe, *Defamation by Will: Theories and Liabilities*, 27 J. Marshall L. Rev. 749 (1994).

[389] *Id*.

[390] An excellent resource for approaches to determine and document capacity is the ABA Comm'n. on L. & Aging & Am. Psychological Assn., *Assessment of Older Adults with Diminished Capacity: A Handbook for Lawyers* (2005) *available at* http://www.apa.org/pi/aging/resources/guides/diminished-capacity.pdf.

[391] *Id*.

[392] Bay, *supra* note 381, at 6.

[393] *See* Gerry W. Beyer, *Video-Recording the Will Execution Ceremony*, Estate Planning Studies (April 1, 2010), www.ssrn.com/abstract=1609462, for a thorough discussion of the benefits and risks of videotaping.

[394] 149 Wn. 2d 262, 269, 66 P.3d 1069 (2003).

taking of advantage of this option in a manner most beneficial to the client.[395]

D. Periodic Re-Execution of Estate Planning Documents.

When competency is likely to be an issue, and even when it is not, it is recommended that the client re-sign the same estate planning documents periodically, without destroying prior versions, even if the content changes little from one version to the next, so that a contestant would need to set aside a series of documents rather than just one to bring a successful contest.[396] Repetition also provides evidence of a client's intent.

E. Maintain Standardized Procedures.

It is important to have standardized procedures for execution of any documents. If irregularities in the execution of a particular document are later alleged, the fact that all documents are executed according to the same procedure may be sufficient to overcome the allegation, even if the witnesses are unable to recall the details of the event. Execution of documents outside of the presence of the drafting attorney should be strongly discouraged. But when this is not possible, a standardized memorandum of instructions should be delivered to the client along with the documents to be signed. If possible, it is recommended that the attorney request that after the execution, the client sign and return the instructions to indicate that they were complied with. The signed instructions should be retained in the client file.

F. Confirm Intent With Respect to Nonprobate Transfers.

Unhappy family members may also challenge nonprobate transfers. Accordingly, attorneys may want to consider placing a statement in a will that any nonprobate transfers were intended by the decedent, and were not for mere convenience while the decedent was living.

XVI. Conclusion

Even in states where same-sex marriage and civil quasi-marital relationships are permitted, the DOMA makes it unclear how federal law will apply. As states are persuaded to adopt same-sex marriage or some form of quasi-marital relationship, it will be necessary to develop a new body of law to define the rights and responsibilities that come with it. Until parity is brought to the laws applicable to unmarried couples, the bias in favor of married couples that is inherent in the

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[395] *See* Beyer, *supra* note 393.

[396] *Id.*

transfer tax laws means that unmarried couples will often bear a heavier estate and gift tax burden.

The estate plans of unmarried partners, and partners in marriages not legally recognized, needs special attention to insure that their objectives are met with a minimum of income, gift, and estate tax liabilities, as well as a minimum of conflict. Unmarried partners need to understand that no default legal structure exists in the absence of an estate plan, as there is for married couples. Their advisors need to understand the disparities in the law relative to unmarried couples, and need to be able to recommend steps, if any, to mitigate the lack of parity with married couples. Furthermore, family dynamics and hostile family members often play a large role in shaping the plan of an unmarried couple. It is critical to consider this when recommending a plan, and to take steps to reduce the risks.

EXHIBIT A[397]

Table 1. General Rules — Property and Income: Community or Separate?

Community property is property:	**Separate property** is:
• That you, your spouse (or RDP/California same-sex spouse), or both acquire during your marriage (or registered domestic partnership/same-sex marriage in California) while you are domiciled in a community property state. (Includes the part of property bought with community property funds if part was bought with community funds and part with separate funds.) • That you and your spouse (or RDP/California same-sex spouse) agreed to convert from separate to community property. • That cannot be identified as separate property.	• Property that you or your spouse (or RDP/California same-sex spouse) owned separately before your marriage (or registered domestic partnership/same-sex marriage in California). • Money earned while domiciled in a noncommunity property state. • Property either of you received as a gift or inherited separately during your marriage (or registered domestic partnership/same-sex marriage in California). • Property bought with separate funds, or exchanged for separate property, during your marriage (or registered domestic partnership/same-sex marriage in California). • Property that you and your spouse (or RDP/California same-sex spouse) agreed to convert from community to separate property through an agreement valid under state law. • The part of property bought with separate funds, if part was bought with community funds and part with separate funds.
Community income [1,2,3] is income from: • Community property. • Salaries, wages, or pay for services of you, your spouse (or RDP/California same-sex spouse), or both during your marriage (or registered domestic partnership/same-sex marriage in California). • Real estate that is treated as community property under the laws of the state where the property is located.	**Separate income** [1,2] is income from: • Separate property. Separate income belongs to the spouse (or RDP/California same-sex spouse) who owns the property.

[1] **Caution:** In Idaho, Louisiana, Texas, and Wisconsin, income from most separate property is community income.

[2] **Caution:** Check your state law if you are separated but do not meet the conditions discussed in *Spouses living apart all year*. In some states, the income you earn after you are separated and before a divorce decree is issued continues to be community income. In other states, it is separate income.

[3] **Caution:** Under special rules, income that can otherwise be characterized as community income may not be treated as community income for federal income tax purposes in certain situations.

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[397] *IRS Publication 555* (Dec. 2010) Table 1.

EXHIBIT B

Drafting for Assisted and Collaborative Conception and Posthumously Conceived Children.

1. A child born as a result of assisted conception shall be considered a child of the individual whose status as such child's parent determines whether such child becomes a beneficiary under this instrument. An individual shall be considered the natural parent of a child:

   i. If such child was conceived using (a) such individual's ovum or sperm and the ovum or sperm of such individual's spouse, (b) such individual's ovum or sperm and the ovum or sperm of a donor other than such individual's spouse, or (c) the ovum or sperm of a donor and the ovum or sperm of such individual's spouse;

   ii. Regardless of whether such ovum was fertilized *in utero;*

   iii. Regardless of whether the fetus was carried to term by such individual or such individual's spouse; and

   iv. Regardless of whether such child has been legally adopted by such individual if such adoption is required under applicable law at the time of such child's birth to establish that such individual is such child's parent.

2. Any individual who may be considered a natural parent of a child solely because of having donated ovum or sperm or having acted as a gestational carrier and who would not otherwise be a beneficiary under this instrument, and any other individual who is related to such individual by consanguinity or affinity, shall not be a beneficiary under this instrument.

3. A genetic child of a parent who was deceased at the time of such individual's conception shall be deemed to be a descendant of such parent only if:

   i. such individual was born within the Three Hundred (300) day[398] period after such parent's death;

   ii. such parent gave permission for the use of his or her genetic material to the surviving parent in connection with the conception of such individual by such parents in an instrument that was signed by the deceased parent; and

   iii. such deceased parent would have had legal rights and obligations as a parent of such child upon his or her birth under local law.

4. A child, where such child was in the process of being adopted before the adopting parent's death (i.e., the child has been "placed" with the adopting parent), if the adoption is legally completed by the (deceased) person's spouse within two (2) years after such death (provided the adopted child is under the age of eighteen (18) at the date of adoption), shall be deemed accomplished prior to death.

[398] Pursuant to RCW 26.26.116, Washington's statute regarding the presumption of paternity in the context of marriage.

EXHIBIT C

Bibliography of Internet Resources

1. LAMBDA Legal – Gay Rights By State: www.lambdalegal.org/our-work/states/.

2. Legal Marriage Court Cases – A Timeline – U.S. Constitutional cases from 1971 – Present: www.buddybuddy.com/t-line-1.html.

3. Same-Sex Marriage – a Selective Bibliography of Legal Literature: www.law-library.rutgers.edu/resources/SSM.html.

4. Compilations of links for transgender legal resources can be found at National Center for Transgender Equality: www.nctequality.org/Resources/index.html, The Transgender Law & Policy Institute: www.transgenderlaw.org/,the ACLU: www.aclu.org/lgbt-rights/transgender, the Transgender Legal Defense Fund: www.transgenderlegal.org/, and the Transgender Law Center: www.transgenderlawcenter.org/ (which also includes many resources specific to California).

5. Immigration Equality – An organization seeking equal application of U.S. Immigration laws and for those facing discrimination due to sexual orientation: www.immigrationequality.org/.

6. ABA AIDS Coordination Project – a Committee of the ABA to Educate the Bench, Bar and Public about Legal Issues Concerning HIV/AIDS: http://www.americanbar.org/groups/individual_rights/projects/aids_coordinating_project.html.

7. Human Rights Campaign – A comprehensive web site dealing with a wide range of legal issues, including marriage, for the gay, lesbian and transgender community, and a section providing information concerning state adoption laws: www.hrc.org/.

8. Wikipedia contains entries on several topics including same-sex marriage, the history of legislation and the status of legislation worldwide: www.en.wikipedia.org/wiki/Same-sex_marriage.

9. Same-Sex Marriage, Civil Unions and Domestic Partnership stories collected news and commentary at The New York Times: http://topics.nytimes.com/top/reference/timestopics/subjects/s/same_sex_marriage/index.html.

10. Same-Sex Marriage and Domestic Partnership collected articles at Open Directory Project: http://www.dmoz.org/Society/Gay,_Lesbian,_and_Bisexual/Law/Marriage_and_Domestic_Partnership/.