

JURISDICTION: OKLAHOMA TAX COMMISSION - DECISION
CITE: 2004-01-20-06 / NOT PRECEDENTIAL
ID: P0000259
DATE: 01-20-04
DISPOSITION: DENIED
TAX TYPE: ESTATE
APPEAL: NO APPEAL TAKEN

FINDINGS OF FACT AND CONCLUSIONS OF LAW

1. DECEDENT died on March 22, 1999, in BIGCITY, Oklahoma. He was 81 years old at the time of his death. (Death Certificate, Exhibit "A").
2. DECEDENT was a resident of the State of Oklahoma at time of death and substantially all of his estate was located within the State of Oklahoma.
3. Before his death, the Decedent executed the "1991 Revocable Trust" (Trust, Exhibit "B").
4. Decedent's surviving spouse is the sole Trustee of Trust A and Trust B pursuant to Article I of the 1991 REVOCABLE TRUST.
5. Before his death, the Decedent executed a "Last Will and Testament" (Will, Exhibit "C").
6. Decedent's federal estate tax return was prepared and filed by the executor (Exhibit "D"). The executor did not elect out of Qualified Terminal Interest Property (QTIP) for the purposes of the federal estate tax return (Exhibit "D, Section M").
7. Decedent's Oklahoma estate tax return (Form 454-R-96) was timely filed on December 22, 1999, together with remittance to Oklahoma Tax Commission of \$X,XXX.XX, being the total amount of estate tax due on the Oklahoma return as filed (Exhibit "E").
8. The Estate Tax Division issued its Assessment Notice on March 10, 2000 (Exhibit "F"). The Assessment Notice included the following adjustments:
 - A. Marital deduction of \$XXX,XXX.XX reflecting value of Trust A has been reduced to a marital deduction amount of \$YY,YYY.YY to "reflect a life estate to surviving spouse in the QTIP Trust A as per administrative rule 710:35-5-61";
 - B. Marital deduction for value of life estate computation in Trust B in amount of \$ZZZ,ZZZ.ZZ was determined invalid due to the "invasion of principal for lineal beneficiaries before the death of the surviving spouse."
9. An extension of time to file a protest was requested by Decedent's representative and granted by the Division (Exhibits "G" and "H").
10. A protest of the assessment was timely filed on July 10, 2000 (Exhibit "I").

11. Oklahoma Tax Commission acknowledged receipt of taxpayer's protest dated July 10, 2000, and received by the Oklahoma Tax Commission on July 12, 2000, on January 2, 2001. The protest was assigned to an Administrative Law Judge on January 2, 2001 (Exhibits "J" and "K").

Additional Findings

12. Pursuant to the terms of the 1991 REVOCABLE TRUST, upon Settlor's spouse, surviving Settlor, the Trust estate was to be divided into two (2) subtrusts, Trust A (the Qualified Terminal Interest Trust [QTIP TRUST] and Trust B (the Unified Credit Trust [UC TRUST]).

13. The relevant provisions of Trust A (Qualified Terminal Interest Trust) [QTIP TRUST] are:

(a) Income. The Trustee shall and must pay at convenient intervals, at least as often as quarterly, as the same shall accrue, all of the net income to Settlor's spouse, so long as the spouse lives.

(b) Special Distributions of Principal. If at any time during the existence of Trust A [QTIP TRUST] the net income, which shall be distributed to Settlor's spouse under the terms hereof, shall not be adequate in the opinion of the Trustee for such spouse's health, maintenance and support in accordance with the spouse's accustomed manner of living, considering all other resources available to the spouse, then the Trustee may make supplemental distributions of principal out of Trust A to Settlor's spouse to the extent and in the manner that the Trustee may deem advisable. Distribution of the entire principal of Trust A is authorized if the Trustee shall determine such distribution shall be to the best interest of Settlor's spouse in accordance with the foregoing standard.

* * *

(e) Limitation on Discretion of Trustee. If the Personal Representative of Settlor's estate makes the election set forth in Section 2056(b)(7) of the Internal Revenue Code to treat all or any part of the property passing to Trust A [QTIP TRUST] as qualified terminable interest property in Settlor's estate, then, in determining the income payable to Settlor's spouse under the terms of Paragraph (a) hereof, and in determining the manner in which expenses are to be borne and the manner in which receipts are to be credited as between principal and income, and in determining what shall constitute income or principal, the Trustee shall make such determinations, distributions and allocations in a manner that complies with the provisions of Section 2056 of the Internal Revenue Code or the corresponding provisions of any subsequent United States revenue law or laws.

* * *

14. The relevant provisions of Trust B (Unified Credit Trust) are:

(a) Income Distributions. The Trustee shall distribute at such intervals as it may determine to Settlor's spouse, so much of the net income of Trust B as when added to resources available to Settlor's spouse from all other sources will, in the sole opinion of the Trustee, adequately provide for the Settlor's spouse's health, support and maintenance in the spouse's accustomed manner of living. The Trustee shall distribute to Settlor's children named above (who shall be treated equally), and the descendants of any deceased children of Settlor, so much of any net income of Trust B not distributed to Settlor's spouse as the Trustee may deem necessary and appropriate to provide for their health, education, including college, graduate and professional schools, maintenance and support in accordance with their accustomed manner of living, considering all other resources available to them. Any income not distributed shall be accumulated and added to the principal of Trust B. Any distributions made under this Paragraph (a) need not be equal among beneficiaries and shall not be charged against their respective shares of the Trust.

(b) Principal Distributions. If at any time during the life of Trust B [UC TRUST] the net income which is distributed under the terms hereof shall not be adequate, in the opinion of the Trustee, for the necessary and appropriate health, education, maintenance and support in accordance with the accustomed manner of living of any beneficiary of Trust B to whom income is distributable at the time of the particular supplemental distribution, considering all other resources available to such beneficiary, the Trustee, in its absolute and sole discretion, may supplement the same out of the principal of Trust B to such extent and in such manner as the Trustee may deem necessary and appropriate for said purpose, and the amount of such supplemental distribution shall not be charged against the presumptive share, if any, of the particular beneficiary of Trust B receiving the same. However, no principal distributions to or for the benefit of Settlor's spouse shall be made out of Trust B [UC TRUST] while, in the Successor Trustee's sole opinion, there are funds readily available for such purposes in Trust A [QTIP TRUST]. It is Settlor's desire that, to the extent the Successor Trustee deems it appropriate, Trust A [QTIP TRUST] be exhausted before any principal distributions are made to or for the benefit of Settlor's spouse from Trust B. Distribution of the entire principal of Trust B [UC TRUST] is authorized if the Successor Trustee shall determine such distribution shall be to the best interest of the beneficiaries in accordance with the foregoing standard.

* * *

15. After application of a previous payment made, the outstanding estate tax is \$XX,XXX.XX, consisting of tax in the amount of \$XX,XXX.XX and interest calculated to March 28, 2000, in the amount of \$X,XXX.XX.

ISSUES

- I. Whether the Division properly reduced the marital deduction in Trust A [QTIP TRUST] to reflect a life estate to the surviving spouse per *Oklahoma Administrative Code 710:35-5-61*.
- II. Whether the Division properly denied a life estate deduction for Trust B [UC TRUST] where lineal beneficiaries had a right to receive all and/or portions of the principal assets of the family trust prior to the death of the surviving spouse.

CONTENTIONS

Protestant contends regarding Trust A [QTIP TRUST] that the marital deduction should be allowed and is valid as to the entire amount of Trust A as the surviving spouse/Trustee had 100% income interest as a life estate coupled with a de facto power of appointment over 100% of the principal of said Trust A. Article V grants to the surviving spouse as sole Trustee total control and ability to appoint and distribute all of the principal to herself as surviving spouse and to remove same free of trust and to make unlimited gifts to charities and to family members. It is the position of Protestant that this power is tantamount to vesting fee simple ownership and title thereto in the surviving spouse, thereby qualifying the total amount of Trust A for a marital deduction.

As to Trust B [UC TRUST], Protestant contends that the estate should be allowed a marital deduction for valuation of trust as a life estate pursuant to Oklahoma Statutes and Administrative Rules because Trustee has the sole power without consent of any third party to distribute the principal of Trust B either to Trustee individually in her individual capacity or to lineal issue of Trustor and at all times is subject to individual income tax on all of the income of Trust B in accordance with provisions of Internal Revenue Code.

The Division contends that it properly reduced the marital deduction for Trust A [QTIP TRUST] to reflect a life estate to the surviving spouse pursuant to *Oklahoma Administrative Code 710:35-5-61*. Further, the Division contends that it properly denied a life estate deduction for Trust B [UC TRUST] because the spouse's interest was contingent, not vested.

CONCLUSIONS OF LAW

1. The Oklahoma Tax Commission has jurisdiction of this protest. 68 O.S. 1991, § 207.
2. The value of any interest in decedent's estate, beneficial or otherwise, vesting in the surviving spouse shall be excluded in determining the value of the decedent's gross estate. 68 O.S. Supp. 1998, § 807(B)(1) and (2).

3. A federal estate tax return was filed taking a QTIP marital deduction pursuant to 26 U.S.C. § 2056(b)(7) of \$960,893.66 for "Marital deduction trust A (QTIP)". An Oklahoma estate tax return was filed on December 12, 1999, taking a marital deduction of \$XXX,XXX.XX on Schedule I-1 of the Oklahoma estate tax return for the 1991 REVOCABLE TRUST A.

4. Pursuant to the Tax Commission's authority to promulgate and enforce rules and regulations, 68 O.S. 1991, § 203, the Tax Commission promulgated 710:35-5-61, which provides as follows:

The qualified terminal interest property election provided for Federal Estate Tax use is not allowable for purposes of Oklahoma Estate Tax, except that a life estate for a surviving spouse may be deducted.

5. The Instructions to Schedule I of the Oklahoma estate tax return state that "Oklahoma does not recognize a QTIP. A life estate should be calculated for the value of the QTIP property shown on the federal return, and the remainderman taxed accordingly."

6. *Oklahoma Administrative Code 710:35-5-61* is clear and unambiguous in its terms and has the force and effect of law. The provision addresses not only the fact that the Qualified Terminal Interest Property election provided for federal purposes is not recognized for Oklahoma estate tax purposes, it goes on to plainly set out the alternative method that is to be followed where such election is made for federal purposes. The Division's treatment of Protestant's marital property claim on Oklahoma Schedule I-1 comports with the rule and was proper.

7. A vested estate or interest exists when there is an immediate right of present enjoyment, or a present fixed right of future enjoyment, in an ascertained person, and a contingent estate or interest is one in which a fixed right will arise in the future under certain specified contingencies. 96 C.J.S. *Wills* § 921. An interest is contingent when it is limited to take effect on the happening of an uncertain or doubtful event. *Id.*

8. Although a testamentary gift may be vested in interest, and the actual enjoyment postponed to a future time, where the vesting of an estate is dependent on a contingency, the estate will not vest until the happening of such contingency, a contingency being some future event which may or may not occur. 96 C.J.S. *Wills* § 925.

9. Here, the spouse's interest would vest only if Trust B [UC TRUST] remained funded. Since the terms of the trust allow for its depletion at the discretion by the Trustee, the spouse's interest is contingent and therefore the Division properly disallowed the life estate deduction for Trust B.

10. The protest should be denied.

DISPOSITION

It is the DETERMINATION of the OKLAHOMA TAX COMMISSION, based upon the specific facts and circumstances of this case, that the estate tax protest of the DECEDENT be denied.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was **NOT** deemed precedential by the Commission. This means that the legal conclusions are not generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.