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JOINT AND MUTUAL WILLS: A MISCHIEVOUS CONCEPT

— by Neil E. Harl*

Most wills are executed by one person and may be amended, revised or revoked at any time prior to the testator's death.[1] Occasionally, use is made of wills that are "joint" in that the instrument is signed by two or more individuals (usually spouses) and contains in one document the testamentary bequests of each testator.[2] Such wills are, in effect, the separate wills of each of the testators and can be revised or revoked by any of the testators as to that person's property.[3]

Wills that are both "joint" and "mutual" contain a contractual obligation that binds the parties to dispose of their properties that are subject to the contractual obligation according to the terms of the will.[4] The contractual feature becomes binding at the death of the first testator to die; the surviving testator's interest is effectively reduced to a life estate with the remainder interest passing to the beneficiaries named in the will.[5]

Possible gift

If the ability of the surviving testator to consume, convey or dispose of the property after the death of the first testator to die is constrained by the terms of the will or by state law, the surviving testator may be deemed to have made a completed gift of the remainder interest in that surviving testator's property at the death of the first spouse to die.[6] On the other hand, if the surviving testator is subject to few constraints on disposition of the property after the death of the first testator to die, there may not be a gift of the remainder interest to the beneficiaries under the will.[7] Thus, a contractual promise to transfer an indefinite amount of property at one's death is not a gift for federal gift tax purposes.[8] If the surviving testator has a general or special power of appointment over the remainder, that may preclude a completed gift at the death of the first testator to die.

Effect on marital deduction

If the decedent wishes to claim a marital deduction, the property interest passing to the surviving spouse does not qualify for the marital deduction if the spouse is bound by contract to dispose of the interest in favor of a third person.[9] However, a marital deduction has been allowed in joint tenancy property even though subject to a joint and mutual will.[10] The courts, in general, have allowed the marital deduction for nonprobate property but not for probate property.[11] Thus, an interest bequeathed to a surviving spouse under a joint and mutual will may not be eligible for the marital deduction.[12]

In a recent letter ruling,[13] a West Virginia decedent had executed a joint will with the surviving spouse. The will provided that all real and personal property passed to the survivor who had the power to sell, convey, use or dispose of the property for any purpose and that any remaining property at the survivor's death was to pass to the children. The surviving spouse disclaimed a portion of the estate property equivalent to the amount necessary to use the unified credit and any other credits. The IRS ruled that under West Virginia law, the surviving spouse had the power to appoint the property to anyone; therefore, the estate property passing under the joint will was eligible for the marital deduction.

Inclusion in survivor's estate

Arguably, if the surviving spouse only has a "mere life estate" after the death of the first spouse to die, that spouse would have a *granted* life estate as to property previously owned by the first spouse to die and the property would not be included in the surviving spouse's estate. On the other hand, for property owned by the surviving spouse before the death of the first spouse to die, the surviving spouse would have a *retained* life estate which would be fully taxable in the survivor's estate. Property owned by the spouses in tenancy in common would appear to be subject to a retained life estate and a granted life estate in the respective portions.

Obviously, this would have important implications for provisions such as special use valuation, also.[14]

FOOTNOTES

1 See generally Note, "Recent Developments of the Iowa Law of Joint and Mutual Wills," 44 Iowa L. Rev. 523 (1959).

2 See United States v. Ford, 377 F.2d 93, 96 (8th Cir. 1967).

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[3] See note, *supra* n. 1.
[4] See, e.g., Pyle v. United States, 766 F.2d 1141 (7th Cir. 1985), *cert. denied*, 475 U.S. 1015 (1986).
[5] See Pyle v. United States, n. 4 supra.
[6] Pyle v. United States, n. 4 *supra* (significant constraints imposed on freedom of surviving spouse to dispose of property); Grimes v. Comm'r, 851 F.2d 1005 (7th Cir. 1988).
[7] Estate of Lidbury v. Comm'r, 800 F.2d 649 (7th Cir. 1986), *aff'g*, 84 T.C. 146 (1985).
[8] Hambleton v. Comm'r, 60 T.C. 558, 565 (1973), *acq. in result*, 1974-1 C.B. 1.
[9] Treas. Reg. § 20.2056(e)-2(a).
[10] Estate of Awtry v. Comm'r, 221 F.2d 749 (8th Cir. 1955). See Ford v. United States, 377 F.2d 93 (8th Cir. 1967) (joint tenancy property and life insurance proceeds).
[11] Ford v. United States, *supra* n. 10.
[12] Estate of Grimes v. Comm'r, 91-2 U.S.T.C. ¶ 60,078 (7th Cir. 1991) (under Illinois law, survivor under joint and mutual will receives only equivalent of life estate); Ltr. Rul. 9023004, February 20, 1990 (Texas law); Ltr. Rul. 9101002, September 20, 1990 (surviving spouse had mere life estate).
[13] Ltr. Rul. 94350014, June 2, 1994.
[14] See I.R.C. § 2032A.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

BANKRUPTCY

GENERAL-*ALM* § 13.03.*

EXEMPTIONS

AMENDMENTS. At the time of the bankruptcy petition, the debtor was a plaintiff in a personal injury action but the debtor did not list the action on the bankruptcy asset schedules nor did the debtor claim the action as an exemption. Once the trustee learned about the action, the trustee retained counsel to litigate the action and eventually settled the case for a cash award. The debtor then filed an amendment to the exemptions to include the proceeds of the settlement as exempt. The trustee argued that once the trustee had liquidated an estate asset, the debtor could not claim the asset as exempt. The court held that the debtor could claim the proceeds of the settlement as exempt but that the trustee would be allowed to deduct the cost of procuring the settlement. ***In re* Fournier, 169 B.R. 282 (Bankr. D. Conn. 1994)**.

CHAPTER 12-*ALM* § 13.03[8].*

PLAN. The debtor owned a one-fourth interest in a ranch as a tenant in common. The other interests were held by nondebtors, the debtor's mother and sister. The ranch was operated by the owners as a partnership. The owners were comakers of a loan from the SBA, secured by two mortgages on the ranch which did not exceed the fair market value of the entire ranch. The SBA filed a claim in the debtor's case for the entire amount owed. The Chapter 12 plan provided for the SBA to retain its first lien position on a portion of the land but subordinated the lien as to another portion of the land to a judgment lien held by another creditor. The debtor argued that the SBA loan was oversecured because the value of the claim was only one-third of the fair market value of the ranch. The court held that the determination of the secured status of the SBA claim was to be made using only the value of the debtor's interest in the ranch. Because the claim was at least equal to the debtor's interest in the ranch, the SBA claim was not oversecured and any change in the SBA claim made by the plan would impair the claim impermissably under Section 1225(a)(5). ***In re* Beach, 169 B.R. 201 (D. Kan. 1994)**.

CHAPTER 13-*ALM* § 13.03.*

PROPERTY TAXES. The Chapter 13 debtor owned real property in Maryland against which real estate taxes became first due during the bankruptcy case. The real estate taxes were prospective, i.e., the 1994-1995 taxes became first due on July 1, 1994. The debtor's plan did not provide for payment of the taxes and had not been confirmed when the county filed a claim for the taxes after July 1, 1994. The court noted that had no claim been filed, the taxes were a post-petition claim not required to be paid under the plan and would not be dischargeable. In addition, the court noted that if the tax claim had not been filed, the taxes could have been assessed against the debtor as soon as the plan was confirmed and the real property reverted to the debtor. However, because the county filed a claim for taxes arising post-petition, under Section 1305, the tax claim was to be treated as having arisen pre-petition and allowed as a claim, was subject to the automatic stay and was subject to discharge. Baffled as to why the county would subject its tax claim to these limitations, the court allowed the county to clarify its filing or withdraw it. ***In re* Reamy, 169 B.R. 352 (Bankr. D. Md. 1994)**.

FEDERAL TAXATION-*ALM* § 13.03[7].*

CLAIMS. The IRS filed a priority claim for employment taxes and an unsecured claim for penalties nine months after the bar date for filing claims in the Chapter 7 case. The trustee objected to the claims as untimely filed. The court held that priority tax claims need only be filed pre-distribution to be allowed in Chapter 7 cases unless the claimant was guilty of inequitable conduct but that the unsecured claim would not be allowed because it was untimely filed. The court also held that the failure of the IRS to timely file the claim was not inequitable because the debtor did not provide its employment identification number with the notice of the case to the IRS. ***In re* Bunce, 169 B.R. 355 (Bankr. E.D. N.C. 1994)**.

The debtor filed a Chapter 7 case and listed federal employment tax claims. Notice of the case and the bar date for filing claims was sent to the IRS but not the U.S. Attorney's office. The IRS failed to file a claim until after the claims bar date and the trustee sought to disallow the