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Choosing a Marital Deduction Formula Clause

Richard Bolte

CHOOSING A MARITAL DEDUCTION FORMULA CLAUSE

In the early years after the introduction of the Federal estate tax marital deduction in 1948, a dispute arose over whether a formula or a non-formula clause should be used to obtain this tax benefit.[1] Due to a preponderance of advantages, the formula clause has gained general acceptance[2] and the dispute has shifted to a discussion of which of the various types of formulas should be utilized.

Three general types of clauses will be examined here as applied to the hypothetical estate of Guildenstern. This article is not intended to resolve the dispute as to which is "best", however, as there is no single formula clause applicable to all situations. Rather, it is hoped that by examining the advantages and disadvantages of a few of the most commonly used clauses in relation to a given fact situation, a practical reference will be established for the practitioner who is not always able to explore the intricacies of the various formulas, and at the same time, provide citations indicating where more detailed information can be found when necessary.

BEFORE THE VOYAGE

Before his fateful voyage, Guildenstern sought estate planning advice with an estate made up at that time as follows:

Owned Solely by Guildenstern		
Life insurance (payable to his wife so as to qualify for the marital deduction)	$ 60,000	
Marketable securities	55,000	
Guildenstern Corporation stock	100,000	
Tangible personal property	10,000	
		$225,000
Owned jointly with his wife		
Bank accounts	$10,000	
Bonds	30,000	
Marketable securities	15,000	
Residence (purchased with his money)	40,000	
		95,000
Gross Estate		$320,000

The marital deduction formula clause is defined as "a provision in a will which leaves property to the surviving spouse of the testator

[1] Trachtman, *Leaping in the Dark; More Adventures with Marital Deduction Formulae,* 93 TRUSTS AND ESTATES 922 (1954); Sargent, *To Each His Own,* 93 TRUSTS AND ESTATES 933 (1954).

[2] Lovell, *Administering the Marital Deduction—a Summary of Five Years' Experience,* 92 TRUSTS AND ESTATES 812 (1953); Cantwell, *Ten Years of Experience with the Marital Deduction,* 36 DICTA 197, 201 (1959); Durand, *Draftmanship: Wills and Trusts,* 96 TRUSTS AND ESTATES 871, 872 (1957).

either directly or in trust which is so phrased that the gift (1) qualifies for the marital deduction allowed for such gift under the Federal estate tax law, and (2) is just large enough to entitle the estate to precisely the amount of the maximum marital deduction."[3] A clause that provides for an outright gift to the wife of one-half of the adjusted gross estate less those assets passing to her otherwise, would satisfy this definition. However, such a clause is not totally self-executing and must always be co-ordinated with the testator's estate.

For instance, in the estate of Guildenstern, if we estimate administration expenses to be $20,000, nothing would pass to the widow under a formula clause since property worth $155,000 (life insurance of $60,000 and joint property of $95,000), which passes automatically to her, would exceed the maximum marital deduction of $150,000. This situation, all too common when the client seeks estate planning advice, suggests, (1) that immediate adjustments must often be made in order to effectively utilize a marital deduction formula clause, and (2) that frequent review of a client's estate plan is always advisable in order to keep the clause prospectively operative in light of changes in the estate subsequent to the execution of a document containing such a clause.

The adjustments to be made here are that the life insurance will be made payable to the testamentary trustee,[4] all the joint property, except the residence, will be placed in the sole name of Guildenstern,[5] and administration expenses will be assumed to be $20,000, all of which would leave an estate comprised as follows:

Owned solely by Guildenstern		
Bank accounts	$ 10,000	
Life insurance (payable to his testamentary trustee)	60,000	
Bonds	30,000	
Marketable securities	70,000	
Guildenstern Corporation stock	100,000	
Tangible personal property	10,000	
		$280,000
Owned jointly with his wife		
Residence		40,000
Gross Estate		$320,000
less: Administration expenses		20,000
Adjusted Gross Estate		$300,000

[3] Cox, *Types of Marital Deduction Formula Clauses,* 15 N.Y.U. INST. ON FED. TAX. 911 (1957).
[4] WIS. STAT., §206.52 (2) (1959).
[5] State and Federal gift tax consequences should not be overlooked in any reshuffling at this stage in the estate plan.

It is in regard to this estate that we shall examine three sample formula clauses, assuming (1) that the tangible personal property is specifically bequeathed to the wife, (2) that the estate is to receive the benefit of the full marital deduction, and (3) that in all cases, the executor is empowered to make distributions in cash or in kind.

AFTER THE VOYAGE

A. PECUNIARY MARITAL GIFT SATISFIED AT DATE OF DISTRIBUTION VALUES

The first clause which we shall assume to have been used in the will of Guildenstern is the pecuniary marital gift with the executor having the right to satisfy the gift with assets distributed in kind, which assets shall be valued as of the date of their distribution. The following is such a clause:

> If my wife survives me, I hearby give and bequeath unto _____, as Trustee, an amount equal to the maximum estate tax marital deduction (allowable in determining the Federal estate tax payable by reason of my death) diminished by the value for Federal estate tax purposes of all items in my gross estate which qualify for said deduction and which pass or have passed to my said wife (the words "pass or have passed" shall have the same meaning as such words shall have under the provisions of the Internal Revenue Code in effect at the time of my death) under other provisions of this will, by right of survivorship with respect to jointly owned property, under settlement arrangements relating to life insurance proceeds, or otherwise than under this bequest. In making the computations necessary to determine such amount, the final determinations in the Federal estate tax proceedings shall control.[6]

Under this clause, unless a contrary provision appears in the will, property distributed will be valued as of the date of distribution, so that Guildenstern's widow would receive $100,000 from her husband's estate at the time of its distribution, either in cash or in assets having a value at that time of $100,000, this amount being arrived at by subtracting from the maximum marital deduction of $150,000, the joint residence of $40,000 and the tangible personal property of $10,000, the latter two assets having passed to the wife otherwise than under the bequest. Such a gift is a general legacy[7] and as such, is subject to the prior payment of specific legacies but would be fully satisfied before the residuary legatees would take. A general legacy, if not in trust,

[6] Casner, *How to Use Fractional Share Marital Deduction Gifts,* 99 TRUSTS AND ESTATES 190 (1960). The last sentence of this clause does not authorize distribution at Federal estate tax values but relates only to the computations of the adjusted gross estate.

[7] *In re* Reben's Will, 115 N.Y.S. 2d 228 (1952); *In re* Lewis' Will, 115 N.Y.S. 2d 791 (1952). Such a gift would still be a general legacy even if it were to be made up out of residue. REV. RUL. 60-87; 1960-10 I.R.B. 18.

does not entitle the legatee to interest during the ordinary period of administration unless a contrary intent is manifested in the will.[8] When such a gift is made without specific provision that the gift is to receive income during administration, caution should be exercised so that the executor is not in any way "authorized or directed to delay distribution beyond the period reasonably required for administration of the decedent's estate", as such a provision may defeat the marital deduction.[9]

This form of marital gift also does not share in any appreciation or depreciation of the probate assets during the period of administration and would be paid in cash if the power to make distributions in kind were not specifically included.[10] Neither would the wife share in any appreciation or depreciation if the executor is given the power to satisfy such a legacy in kind since, as mentioned above, the assets so distributed will be valued at their values on the date of the transfer.[11]

The amount of marital gift could be altered, however, should the assets change in value during the administration and the executor elect to choose the alternate valuation date. Assuming Guildenstern's probate and trust assets of $260,000 (after expenses) increased in value, such that on the alternate valuation date they became worth $360,000, the maximum marital deduction would then be $200,000 and the widow, under the formula, would be entitled to a gift of $200,000 less $50,000, or $150,000 from the estate. Such an election, although incurring a higher Federal estate tax, is not at all unlikely, especially where the widow serves as executrix.[12]

Even though determined by a formula, the widow's claim against the estate is for a fixed and definite dollar amount and to the extent the fair market value of any property distributed in satisfaction of the claim exceeds the fair market value thereof on the date chosen for Federal estate tax purposes, capital gains would be realized by the estate.[13] In such a situation, the transferee is regarded as having acquired

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[8] 3 SCOTT, TRUSTS §234.2 (2d Ed. 1956). For the ordinary period of administration in Wisconsin, one year, see Estate of Onstad, 224 Wis. 332, 271 N.W. 652 (1937); Shupe v. Jenks, 195 Wis. 334, 218 N.W. 375 (1928); Estate of Hoehnen, 233 Wis. 645, 290 N.W. 137 (1940), and WIS. STATS., §313.13 (1) (1959).

[9] "An interest is not to be regarded as failing to satisfy the conditions set forth in paragraph (a) (1) and (2) of this Section (that the spouse be entitled to all the income and that it be payable annually or more frequently) merely because the spouse is not entitled to the income from estate assets for the period before distribution of those assets by the executor, unless the executor is, by the decedent's will, authorized or directed to delay distribution beyond the period reasonably required for administration of the decedent's estate." Treas. Reg. §20.2056(b) 5 (f) (9).

[10] *In re* Lazar's Estate, 139 Misc. 261, 247 N.Y. Supp. 230 (1930).

[11] Matter v. Clark, 251 N.Y. 458, 167 N.E. 586 (1929); *In re* Estate of Kantner, 50 N.J. Super. 582, 143 A. 2d 243 (1958).

[12] The increased estate tax would be offset somewhat by the increased basis the assets would acquire for income tax purposes.

[13] Suisman v. Eaton, 83 F. 2d 1019 (2d Cir. 1936), *affirming* 15 F. Supp. 113 (D.

the property by purchase, rather than by inheritance, and would therefore take the fair market value of the property at the time of the transfer as her basis for it.[14]

By assuming Guildenstern's estate held at the time of distribution assets, valued at $75,000, but which had a Federal estate tax value of $50,000, we see that by using such assets to satisfy the claim of the widow, the estate would incur a capital gains tax on the appreciation and Guildenstern's widow would acquire as her basis for this property the $75,000 value. Conversely, satisfying the claim with depreciated assets would result in a capital loss to the estate.

It is suggested that the potential capital gains tax, a so-called disadvantage when employing such a pecuniary bequest formula clause, has perhaps been overemphasized. Although a given estate may appreciate in value as a whole, there are usually some stable or depreciated assets therein which could be used to satisfy the marital gift. Furthermore, it is usually the total taxes that the testator seeks to minimize and not just capital gains taxes.

If the widow is given a definite and certain amount of property as under this formula clause, the maximum marital deduction is obtained without any increase in the widow's potential taxable estate, at least during the period of administration, because any appreciation during this period will accrue to the non-marital share. To the extent that the widow's marital gift can be so limited, her subsequent estate will save administration expenses and death taxes, which savings might more than offset the capital gains taxes, if any, to her husband's estate.

In the event that the husband's estate depreciates in value during administration, the executor could then elect to use the alternate valuation date which would have the effect of decreasing both the taxable estate and the marital gift. The latter would again have the effect of minimizing the widow's potential settlement costs.[15]

B. Pecuniary Marital Gift Satisfied at Federal Estate Tax Values

The second clause to be examined is but a variation of the first in that the executor is empowered to satisfy legacies with property distri-

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Conn. 1935); Rev. Rul. 56-260, 1956-1 Cum. Bull. 325; Rev. Rul. 60-87 I.R.B. 1960-10, 18; 4 Tax L. Rev. 372 (1949).

[14] Comm'r. v. Brinckerhoff, 168 F. 2d 436 (2d Cir. 1948); Treas. Reg. §1.104-4 (a) (3).

[15] It would undoubtedly be advisable to satisfy the marital gift as soon as possible after the alternate valuation date in order to avoid further susceptibility to capital gains tax liability resulting from appreciation that might accrue thereafter. The feasibility of doing this will depend upon whether the adjusted gross estate can be accurately determined at this time, which in turn will depend upon whether there are still questions as to the includibility of certain items in the gross estate, the valuation of items in the gross estate, and the deductibility of the claims.

bution in kind, but valued at Federal estate tax values rather than date of distribution values. This modification evolved in an attempt to avoid the capital gains tax problem arising under the first clause, and although there apparently is no definite authority on the point, it is generally felt that no capital gain or loss would result and the distributee would take over the cost basis that the assets had in the decedent's estate.[16] The following is an example of such a clause:

> If my wife survives me, I give to _____ _____, as Trustee, an amount equal to fifty per cent (50%) of the value of my adjusted gross estate as finally determined for Federal estate tax purposes, less the aggregate amount of marital deductions, if any, allowed for such tax purposes by reason of property or interests in property passing or which have passed to my said wife otherwise than by the terms of this Article of my Will.
>
> My executor may satisfy said bequest wholly or partly in cash or kind, and select and designate, and assign and convey to the Trustee of said trust fund, the cash, securities, or other assets including real estate and interests therein, which shall constitute said trust fund. Any property so assigned or conveyed in kind to satisfy said bequest shall be valued for that purpose at the value thereof as finally determined for Federal estate tax purposes. No asset or proceeds of any asset shall be included in the trust fund as to which a marital deduction is not allowable if included. Said bequest shall abate to the extent that it cannot be satisfied in the manner hereinabove provided. The exercise by my executor of the authority and discretion given hereunder shall not be subject to question by any person.

The effect of the marital gift is that it may or may not share in any fluctuation of value in the property during the administration because, as the proponents of this clause suggest, the executor could satisfy the marital gift by distributing in kind assets which exceed in value the amount of the claim. For instance, if Guildenstern's estate at the time of distribution held property worth $150,000, but having a Federal estate tax value of only $100,000, the executor could satisfy the gift by giving this property to the widow. On the other hand, he could just as well distribute $100,000 in cash to her, or even property which had depreciated since the time it was valued for Federal estate tax purposes.[17] But whether the court having jurisdiction over the estate would allow an executor to make such an unequal distribution is still questionable. New York, at least, would not, since it has already held in the *Bush* case,[18] that where the executor had such a power, the allocation

[16] CASNER, ESTATE PLANNING 650 (2d ed. 1956).
[17] *Id.* at 649; Cox, *supra* note 3, at 930.
[18] *In re* Bush's Will, 2 A.D. 2d 526, 156 N.Y.S. 2d 897 (1956), *aff'd*, 3 N.Y. 2d 908, 145 N.E. 2d 872 (1957).

and distribution of the property to the marital deduction gift and the residuary trust had to be made in such a manner that each would share proportionally in any appreciation or depreciation of the several securities. The power in the Bush will was decided to be contrary to a particular New York Statute,[19] but even without such a statute, an executor is essentially a trustee[20] and must act impartially for the interests of all the beneficiaries.[21] The allocation of depreciated property to the marital portion would have the advantage, as mentioned above, of tending to reduce the amount of assets susceptible to more taxes at the death of the widow, and perhaps to an even greater extent than under the first clause examined above. If, however, such an allocation is allowable, it is apparent that the ultimate amount of the gift the widow is to receive here depends not only upon the wishes of her deceased husband, but also upon those of his executor.

Assuming, that by giving the executor this power to distribute at Federal estate tax values, the capital gains issue is resolved, the question remains whether more problems are raised than cured thereby. Is the executor in effect given the power to fix values? If so, there is the possibility that this will be deemed a power of appointment, perhaps incurring gift and estate taxes.[22] There is the further complication that the marital deduction gift may be disqualified if the executor is deemed to have the power to divert property from the spouse.[23] Presumably, such questions would not arise where the executor must make a pro rata allocation of the several securities as in the *Bush* case.

Apart from the tax problems, such a clause might very well place the executor in a position whereby he must act somewhat like an octopus, using many arms to hold off bickering beneficiaries whose interests are conflicting, and in many cases, making a final decision satisfactory to none. A not so uncommon example which emphasizes the above is where the widow is a second wife and the residuary legatees are the testator's children of a prior marriage. This situation would be further compounded where a relative is serving as executor or co-executor.[24]

The question now arises that with all the above-mentioned uncertainties, many of which disappear when the fractional share of the residue formula clause is used, why does a pecuniary formula clause remain so very popular with draftsmen? Perhaps the most logical answer is that it is a comparatively simple and uncomplicated formula clause, both for the attorney to draft and the client to understand. In

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[19] NEW YORK DECEDENT ESTATE LAW, §125-2.
[20] Shupe v. Jenks, *supra* note 8.
[21] Will of Rice, 150 Wis. 401, 137 N.W. 778 (1912).
[22] CASNER, *supra* note 16, at 648-650.
[23] Treas. Reg. §20.2056(5)-5 (a)(5).
[24] Kiley and Golden, *A Residue Formula for Maximum Marital Deduction,* 89 TRUSTS AND ESTATES 744, 746 (1950).

the day to day practice of law, the attorney does not usually have the time to originate his own marital deduction clause and is reluctant to just "boilerplate" a complex clause suggested by one of the noted authorities in the field. Furthermore, a formula fractional share of the residue clause such as that which shall be examined next, often evokes the comment of a client that the complicated language therein is used only to justify the attorney's fee.

The most widely acclaimed reason for using the pecuniary formula clause satisfied at estate tax values is because it allows for post-mortem tax planning.[25] The executor is able to allocate assets in such a way as to obtain the maximum tax benefits in the estates of both the husband and the wife, usually by diverting from the marital gift those assets in which appreciation is anticipated or has already accrued. This, of course, presupposes that an unequal allocation of property is allowable under the applicable local law, but this in itself might not be an unmixed blessing if the questions raised by Mr. Casner are valid.[26]

C. FRACTIONAL SHARE OF THE RESIDUE

Professor Casner suggests the following as a fractional share formula clause:

> If my wife survives me, I hereby give, devise and bequeath unto _____, as Trustee, the following described fractional share of my residuary estate:
>
> The numerator of the fraction shall be the maximum estate tax marital deduction (allowable in determining the Federal estate tax payable by reason of my death) minus the value for Federal tax purposes of all items in my gross estate which qualify for said deduction and which pass or have passed to my said wife (the words 'pass or have passed' shall have the same meaning as such words shall have under the provisions of the Internal Revenue Code in effect at the time of my death) under other provisions of this will, by right of surviorship with respect to jointly owned property, under settlement arrangements relating to life insurance proceeds, or otherwise than under this bequest and devise (in computing the numerator, the values as finally determined in the Federal estate tax proceedings shall control); and the denominator of the fraction shall be the value of my residuary estate, and to the extent that items in my residuary estate are included in my gross estate, the value at which they are included in my gross estate shall control in determining the denominator, and to the extent they are not to included, their value at the time they would have been valued if they had been so included, shall control in determining the denominator.[27]

Applying the suggested fractional share of the residue clause to

[25] COX, *supra* note 3, at 931.
[26] See CASNER, *supra* note 16, at 648-650.
[27] CASNER, *supra* note 6, at 190.

Guildenstern's estate, the numerator of the fraction would be $100,000, derived by subtracting from the "maximum estate tax marital deduction" of $150,000, the value of all items "which pass or have passed to my said wife . . . otherwise than under this bequest," which under the assumed facts would be $50,000. The denominator would be the value of the residuary estate, or $250,000. This fraction, 100,000/250,000 or 2/5, as applied to the distributive assets would produce a marital gift of $100,000 (2/5 of $250,000) which, when added to the other assets passing to the widow, $50,000, would equal the maximum marital deduction. If, however, the residuary estate increased in value to $300,000, two-fifths thereof would be $120,000 and the ultimate amount of property received by the wife then would be $170,000; conversely, a decrease to $200,000 would make her total share only $130,000. Under each of these three conditions, the residuary legatees would take the balance of the estate less taxes of about $30,000 (approximate Federal estate tax of $17,500, Wisconsin inheritance taxes of $12,500), their shares being $120,000, $150,000 and $90,000 respectively. This same proportionate sharing of the distributive property *might* occur under the pecuniary bequest formula using Federal estate tax values, but so far, only New York has interpreted the executor's power to distribute at Federal estate tax values as being a mandatory direction for a pro rata allocation, whereas under this fractional share of the residue formula, it is mandatory by the terms of the will itself.[28]

The fractional share of the residue formula clause apparently removes virtually all of the objections raised against the pecuniary bequest formulas:

1. The assets received by the widow are acquired through inheritance so that unquestionably there is no capital gain or loss upon distribution when the assets are distributed on an aliquot basis and the distributee acquires the estate's basis for the property.[29]

2. The widow automatically shares in any increase or decrease in value of the probate assets during the administration.[30]

3. Some of the temptation to elect a high valuation date in order to increase the marital deduction is removed because the marital and non-marital portions share ratably in any accretions.

4. The executor cannot be deemed to possess a power of appointment as there is no necessity for any provision requiring the distribution of assets at Federal estate tax values. Neither can the executor be considered as having the power to divert assets from the spouse, as distributions under a fractional share formula must be made according to the fraction so as to at least provide dollar proration.

[28] See *In re* Bush's Will, *supra* note 18.
[29] KILEY AND GOLDEN, *supra* note 24, at 747.
[30] *Ibid.*

5. Because the marital and non-marital portions share ratably dollarwise when residuary property does appreciate, the executor is not placed in the uncomfortable position which might occur when the executor distributes at Federal estate tax values under a pecuniary bequest clause and thereby has the ability to favor one share over another.

6. The intent of the testator cannot be frustrated by the actions of the executor.

Although the fractional share clause seems to have these distinct advantages over a pecuniary bequest clause, it may not be without its own failings. One of the arguments against the use of such a clause is its inflexibility because it removes the possibility of post-mortem planning as the executor is unable to alter the amounts of the respective shares or even the assets therein as each item in the residue apparently should be divided on a pro rata basis.[31]

Professor Casner suggests two methods of overcoming the last objection. The testator can make a specific bequest of property he decides should not be split between the marital and non-marital shares, but if the property is likely to increase significantly in value before his death, such a bequest might hinder the operation of the formula. In such a case, as an alternative, the executor could be given the "discretion on distribution to allocate such property to the non-marital share and to transfer to the marital share from the non-marital share property of equivalent value in place thereof."[32]

Such a discretionary power, and also a mandatory power to exclude from the marital share those assets appearing in the gross estate which would not qualify for the marital deduction if so included, might cause a new complication, however. The problem is this—if the executor should allocate one asset to the marital share, and another asset having an equal value at that time, but a different basis to the estate, to the non-marital share, perhaps it will be considered a taxable exchange.[33]

To illustrate, if Guildenstern's executor allocated to the marital share a block of GM stock worth $36,000 and having a basis of $30,000, and IBM stock to the non-marital share also worth $36,000 at the time of allocation, but with only a $24,000 basis, the Commissioner might claim that this was a taxable exchange. This is because the beneficiaries would not receive equal benefits in that if we assume that each issue is then sold and a 25% capital gains tax subtracted therefrom, the net to the widow would be $34,500 whereby the non-marital legatees would realize only $33,000.

[31] Peeler, *Unsuspected Realization of Profit in Estates and Trusts*, 98 TRUSTS AND ESTATES 1191, 1193 (1959); CASNER, ESTATE PLANNING 1960 SUPPLEMENT 201 (2d ed. 1956).
[32] CASNER, *Id.* at 209.
[33] PEELER, *Supra* note 31, at 1192.

According to the Regulations,[34] a distribution in kind may result in taxable gain if (1) in satisfaction of a right to receive a distribution in a specific dollar amount or (2) in satisfaction of a right to receive specific property other than that actually distributed. We have already seen an example of the first in connection with a distribution under the first clause examined above. The second seems to assume in effect that there is something like an "exchange of property for other property differing materially either in kind or in extent"[35] which is a realizing taxable event under Section 1001 (a) of the Code.[36] But whether an unequal allocation of assets by an executor can be treated as either a taxable exchange or a dollar claim[37] from one share in favor of the other, depends in part upon what interest the beneficiaries had in the property prior to its allocation.[38]

Real estate, in Wisconsin, descends to the heirs or devisees upon the decedent's death[39] whereas legal title to personalty passes to the executor.[40] Whether the beneficiaries acquire sufficient interests in personalty to constitute a claim before distribution seems uncertain.

In one Wisconsin decision, the court required a personal representative to convey his legal title in certain personalty in accordance with the beneficiary's prior dealings with her equitable interests in that property.[41] On the other hand, the court has also held that residuary legatees take as tenants in common[42] but did not go on to decide whether each tenant in common has an undivided interest in each of the assets of the residue.

Two other authorities would seem to indicate that a non-aliquot distribution would not create a taxable capital gain. In O.D. 667, 3 CUM. BULL. 52, there was a residuary bequest in equal portions to three legatees. Cash and securities were distributed unevenly, but it was held that the distribution created no capital gain to the estate and the distributees acquired the estate's basis for the property. In the *Long* case, it was decided that a joint partition deed which divided residuary realty and personalty nonratably was not a taxable exchange.[43] It has been suggested, however, that these decisions might not still be healthy "in light of their age."[44]

"Until and unless this question has been resolved favorably, it is

[34] Treas. Reg. §1.661 (a) -2 (f).
[35] Treas. Reg. §1.1001-1 (a).
[36] INT. REV. CODE of 1954, §1001(a).
[37] CASNER, *supra* note 31, at 209; Kenan v. Comm'r. 114 F. 2d 217 (2d Cir. 1940).
[38] PEELER, *supra* note 31, at 1192.
[39] Estate of Rieman, 272 Wis. 378, 75 N.W. 2d 564 (1956).
[40] Will of Krause, 240 Wis. 72, 2 N.W. 2d 733 (1942); Shupe v. Jenks, *supra* note 8.
[41] McKeigue v. Chicago & N.W.R. Co., 130 Wis. 543, 110 N.W. 384 (1907).
[42] Estate of Hoermann, 234 Wis. 130, 290 N.W. 608 (1940).
[43] Long v. Comm'r., 35 B.T.A. 95 (1936).
[44] CASNER, *supra* note 31, at 210.

advisable to make distributions on an aliquot basis to the fullest extent possible,"[45] which in fact is feasible in the majority of estates and limits the significance of this question to unusual fact situations.

A number of variations of the fractional share of the residue formula clause have been suggested which should be considered here. Perhaps the most refined of these variations from the standpoint of its actual operation is that clause suggested in the early days of the marital deduction by Messrs. Kiley and Golden which reads as follows:

> I give the entire residue of my estate remaining after the payment of all taxes as provided under Article One of my will to my trustee hereinafter named as trustee of separate trusts to be designated as Trust A and Trust B. If my wife survive me, Trust A shall be comprised of that fractional share of the residuary estate passing under this Article which will equal one-half of my adjusted gross estate as finally determined under the Internal Revenue Code for Federal estate tax purposes, less the aggregate marital deduction allowable for property or interests in property which pass or have already passed to my said wife under any other Article of this will, by operation of law, through insurance contracts or otherwise. Trust B shall be comprised of the remaining fractional share of the residuary estate or of the entire residue if my wife does not survive me. Such fractional shares of residue shall be determined on the basis of final Federal estate tax values.[46]

When using this clause, the authors suggest that a direction be made that all estate, inheritance and succession taxes be paid as administration expenses (note the reference in the clause to Article One), and that any property, which if left to the widow would not qualify for the marital deduction, be specifically bequeathed to the non-marital trust. It is further suggested that any assets which might be unsuitable to splitting between the trusts be specifically bequeathed to one trust or the other.

The main difference between this clause and others is in its definition of the residue. Defining the residue as an "after-tax" residue seems most logical in that the fraction is then applied at distribution to the true residue held by the executor. The division could also be made by the trustee after the executor has placed the final residuary estate in his hands. This seems particularly logical in Wisconsin where the trustee is likely to already be holding unallocated life insurance proceeds.[47]

Mathematically, the "after-tax" clause in effect allows the widow to share in any appreciation which might occur in the assets in fact used to pay taxes during or at the end of the administration of the es-

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[45] PEELER, *supra* note 31, at 1193.
[46] KILEY AND GOLDEN, *supra* note 24, at 794.
[47] WIS. STATS. §206.52(2) (1959).

tate.[48] In most cases, this mathematical factor should not be too significant.

By also excluding non-qualifying assets from the defined residue, the possibility of a dollar claim in favor of the marital share, as a result of a mandatory direction, is removed.[49] But the problem raised above in regard to certain assets which do not readily lend themselves to division between the two portions, such as real estate or stock in a close corporation, where the fluctuating values of the property are likely to distort the formula, may not be cured by making a specific bequest thereof. In such a case, the draftsman must decide for himself as to the advisability of allowing an executor to allocate property in his discretion to the share best suited to receive it.

It should be observed that the fractional share clause suggested herein differs from that drafted by Messrs. Kiley and Golden in that it employs the numerator-denominator method of defining the fraction. As can be seen by working through the Kiley and Golden clause, it is somewhat difficult to actually come up with a definite fraction, although the clause must operate in terms thereof. With Guildenstern, Trust A would receive a fractional share equal to one-half of the adjusted gross estate, $150,000, less the property passing otherwise to the wife, $50,000, or $150,000 minus $50,000. This seems more like an amount than a fraction whereas under the numerator-denominator method, there is no doubt but that the language spells out an actual fraction to be used by the executor. Perhaps, therefore, it would be advisable to combine the "after-tax", "after undesirable items" clause with the numerator-denominator language in order to come up with as refined a fractional share of the residue clause as possible. An additional wrinkle which might be added for use in the State of Wisconsin is to have the trustee make the division after he has received the true residuary estate from the executor. A clause embodying these many elements might read as follows:

[48] In the "before tax" example used above on page 540, when the assets appreciated in value, the computations were as follows:

Marital share: $\frac{\$150,000-\$50,000}{\$250,000}$	× $300,000	=	$120,000
Non-marital share:			
Residuary estate			$300,000
Less: Marital share	$120,000		
Taxes	30,000		−150,000
			$150,000

Similar computations under an after-tax formula would be:

Marital share: $\frac{\$150,000-\$50,000}{\$220,000}$	× $270,000	=	$122,727
Non-marital share:			
Residuary estate			$270,000
Less: Marital share			−122,727
			$147,273

[49] CASNER, *supra* note 31, at 208.

I devise and bequeath all of my residuary estate (being all property, wherever situated, in which I may have any interest at the time of my death not otherwise effectively disposed of by my will or codicil, but not including any property over which I may have power of appointment) remaining after payment of all taxes as directed in Article I to my trustees hereinafter named, upon the following trusts:

1. If my wife survives me, my trustees shall divide my said residuary estate, together with the proceeds of insurance on my life and any other death benefit payable (without specific reference to either of said trusts) to my said trustees (all of which property shall be known as my trust estate), remaining after payment of all taxes as directed in Article I, into two trusts, each of which shall be held and administered as a separate trust:

(a) One trust, called the Marital Trust, shall comprise that share of my said trust estate required to obtain for my estate a full marital deduction after taxes, which share shall be determined by a fraction—

(i) The numerator of which shall be the value of the maximum marital deduction allowable in determining the Federal estate tax payable by my estate under the laws in effect at the time of my death diminished by the value of all other property included in my estate for Federal estate tax purposes which qualifies for the said marital deduction and which passes or has passed to my wife and to the Marital Trust either under any other provisions of this will or in any other manner, and

(ii) The denominator of which shall be the value of my trust estate.

(b) The other trust, called the Family Trust, shall comprise the remaining share of my said trust estate.

(c) In computing the numerator and denominator of said fraction, the values as finally determined in the final Federal estate tax proceedings shall control. The assets distributed pursuant to the provisions of this Article, however, shall be valued for distribution purposes at their fair market values at the time or times of actual distribution to the respective trusts. My trustees, in their sole discretion, shall determine the assets to be transferred to the Marital Trust.

2. If my wife shall not survive me, the Family Trust shall comprise my entire said trust estate.[50]

CONCLUSION

The main differences between the above clauses seem to be in their effect upon appreciation or depreciation of estate property and the capital gains tax liability resulting therefrom. The pecuniary gift, satisfied at date of distribution values, definitely incurs a capital gain or loss to the estate when the assets fluctuate in value, but what would

[50] This clause was composed by the author and Charles G. Carpenter, Assistant Cashier in the Trust Department of Marshall & Ilsley Bank and member of Wisconsin Bar.

appear to be the best argument for its use, namely the overall savings in the estates of both spouses, is a very persuasive one. The fractional share of the residue clause, on the other hand, does not incur any capital gains taxes (except possibly where a non-aliquot distribution is made) but does allow the widow to share in any increase or decrease in value of the property in the hands of the fiduciary. The pecuniary bequest, satisfied at Federal estate tax values, is somewhat of a hybrid in that it is purported not to require pro rata allocation of increments or decrements, nor to incur any capital gains taxes, but it rests on an uncertain legal foundation in both respects.

One point is certain, however. The use of any one of the formula clauses requires first, a careful analysis of the total estate of the client in light of his testamentary desires, and second, a thorough knowledge of the effect each type of clause would produce in that estate. Expert assistance is suggested wherever an uncertainty arises as mistakes in this area are irreparable.

RICHARD BOLTE*

*Senior law student at Maruette University and associated with the Estate Planning Division of the Trust Department of Marshall & Ilsley Bank, Milwaukee.