

Planning for the Elective Share

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In HB 3077, the 2009 legislature passed a major revision to the elective share law in Oregon, currently at ORS 114.105 to 114.165. Although Section 23 of HB 3077 delays the effective date until deaths occurring after January 1, 2011, planning to avoid surprises created by the new law should begin now.

Under current Oregon law, defeating a surviving spouse's elective share right to a 25% interest in the decedent spouse's net probate estate has been as simple as preventing assets from passing through probate. With the proliferation of retirement plan assets and the trend toward probate avoidance in general, the current elective share statutes have become increasingly obsolete as a way to protect the rights of a surviving spouse.

As a result, HB 3077 uses an augmented estate approach that subjects to the elective share essentially all assets in which the decedent spouse and the surviving spouse have an interest at the death of the decedent spouse. Inclusion of the surviving spouse's estate in the augmented estate will prevent a wealthy surviving spouse from using the election against the estate of a less wealthy decedent spouse.

The augmented estate is defined in Section 8(1) of HB 3077 as the decedent's probate estate, the decedent's nonprobate estate, the surviving spouse's estate, and the decedent's probate and nonprobate transfers to the surviving spouse. The nonprobate estate includes revocable trusts, property held in survivorship tenancy, property subject to a pay-on-death or transfer-on-death registration, and property for which the decedent could designate a beneficiary. The nonprobate estate does not include life insurance or trusts with retained interests, except that proceeds from these assets received by the surviving spouse by reason of the decedent's death are included. The probate and nonprobate transfers to the surviving spouse are excluded from the definition of the decedent's probate and nonprobate estate to prevent double counting of those assets. *See* HB 3077, §§ 10, 11. The augmented estate is calculated net of enforceable claims and encumbrances against the property. HB 3077, § 8(2).

The surviving spouse will be able to make an election if the effect of the decedent spouse's estate plan, including beneficiary designations, trust provisions, and property passing by survivorship, is that the surviving spouse ends up with less than a stated percentage of the augmented estate. The percentage starts at 5% of the augmented estate for a marriage of less than two years and ranges up to 33% for a marriage of 15 years or longer. *See* HB 3077, § 3(2).

As with the current elective share statutes, Section 6 of HB 3077 allows spouses to relinquish their elective share rights by an agreement or waiver, entered into before or after the marriage, and signed by at least the surviving spouse. Practitioners will need to be careful to determine if a waiver of elective share rights requires that the spouses receive independent counsel.

Section 2 of HB 3077 makes clear that the elective share must be claimed while the surviving spouse is still alive, but allows the claim to be continued after the surviving spouse's death by his or her personal representative. Only the surviving spouse or an agent, conservator, or guardian of the surviving spouse may assert the elective share. HB 3077, § 7.

Note that although a conservator may assert a claim on behalf of a surviving spouse, the right to make the claim cannot be asserted by the spouse's heirs if the surviving spouse or his or her representative fails to make the claim during the surviving spouse's life. In no event may the claim be asserted more than nine months after the death of the first spouse to die. HB 3077, § 4(1).

For planning purposes, HB 3077 recognizes that QTIP and credit shelter trusts naming the surviving spouse as beneficiary will continue to be necessary elements in many estate plans as long as there is a federal estate tax and Oregon inheritance tax. Section 13(2)(b) of HB 3077 provides that such trusts will be valued, for purposes of determining the interest passing to the surviving spouse, at 100% of the principal value if there is a power to invade principal for the spouse's benefit, even if the power is limited to an ascertainable standard. A trust that provides income to the surviving spouse, but that does not allow invasion of principal, will be valued at 50% of the principal value of the trust. HB 3077, § 13(2)(c). Other assets are generally to be valued for elective share purposes at the same value as applies for federal estate tax purposes, under Section 8(4) of HB 3077.

Particularly for clients in second marriages, planning to avoid elective share surprises is likely to be a significant issue. In general, because of the favorable valuation given QTIP qualifying trusts, obtaining a good result for estate and inheritance tax purposes and a good result for elective share purposes should not be unduly burdensome.

However, for clients with large IRAs there is a trap in HB 3077. If the IRA is not left to the surviving spouse, and if the spouse makes the election, the priority rules for recovery of the surviving spouse's elective share, under Section 16 of HB 3077, will require that the named beneficiary of the IRA relinquish some portion of the IRA to the surviving spouse. There is no offset for the income taxes that the named IRA beneficiary will have to pay on withdrawals from a conventional IRA. Therefore, planners will want to be careful in advising clients on beneficiaries for IRAs.

Bequests to charity are also at risk from an assertion of a spouse's elective share rights. This may lead to problems with testamentary charitable trusts, which must meet the definition of a charitable trust from the inception. Treas Reg § 1.664-1(4). A post-inception payment to a surviving spouse in satisfaction of elective share rights would prevent the trust from qualifying for a charitable deduction.

Both the IRA and charitable issues could presumably be resolved by language in a governing document that overrides the proportional contribution requirement for payment

of the elective share contained in Section 16 of HB 3077. However, Section 16 contains no provision allowing the decedent spouse to specify an abatement of bequests to satisfy the elective share. *See also* HB 3077, § 4(2). Formula bequests to nonspouse devisees may solve this problem.

Planners may be tempted to believe that the concurrence of both spouses in a proposed plan will mean that the surviving spouse will not make an election against that plan on the death of the decedent spouse. However, if the surviving spouse is incapacitated at the death of the decedent spouse, then the conservator for the surviving spouse will likely have a duty to assert the surviving spouse's elective share rights.

Planners will need to study the new law and consider whether proposed or existing plans need adjustment to avoid an unexpected assertion of elective share rights. Formula clauses may be of assistance to prevent unexpected problems for bequests outside the marriage. Planners will also need to consider whether spouses need independent counsel if it appears, during planning, that an elective share issue must be addressed.

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