

TAX ALLOCATIONS AND APPORTIONMENT

By: Robert J. Kolasa, C.P.A., J.D., LL.M. (Tax)

**Law Offices of Robert J. Kolasa
582 N. Oakwood Avenue, Suite 200
Lake Forest, Illinois 60045
(847) 234-6262**

ESTATE PLANNING SEMINAR

**Wills Trust & Probate Committee
of the Lake County Bar Association
in Conjunction with the Taxation Committee**

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I. TAX ALLOCATIONS - LIFETIME VS. TESTAMENTARY GIVING

A. GENERAL ADVANTAGES OF LIFETIME GIFTS.

1. **Gift Tax Base is "Tax-Exclusive" and MORE Favorable.** The gift tax is imposed on the property transferred to the recipient, and *does not include* the money paid to the IRS as gift tax.
2. **Estate Tax Base is "Tax-Inclusive" and LESS Favorable.** The estate tax is imposed on both the property transferred to the recipient and the property used to pay estate taxes on the transferred property.

EXAMPLE #1: \$1 Million Testamentary Gift After \$550,000 Estate Tax Leaves \$450,000 to Daughter

Mom (in 55% estate bracket) through her will leaves a \$1,000,000 residuary bequest to Daughter. The estate tax on such transfer is \$550,000, leaving Daughter \$450,000.

EXAMPLE #2: \$1 Million Lifetime Gift After \$354,839 Gift Tax Leaves \$645,161 to Daughter

If Mom in Example #1 had used the same \$1,000,000 to make a gift and pay gift tax during her life, the gift tax would have been \$354,839 and Daughter would get \$645,161 (\$195,161 more than in Example #1).

B. CONCLUSIONS RELATING TO ABOVE EXAMPLES.

1. If Mom dies, it costs her \$550,000 to transfer \$450,000 to Daughter.
2. If Mom makes a lifetime gift, it costs her \$354,839 to transfer \$645,161 to Daughter.
3. Put another way,
 - At the 55% rate, it costs \$.55 in tax to transfer \$1.00 by gift, and \$1.22 in tax to transfer the same dollar at death;
 - Gift tax cost of transferring \$1,000,000 to Daughter is \$1,500,000 (\$1,000,000 bequest plus \$550,000 gift tax);
 - Estate tax cost of transferring \$1,000,000 to Daughter is \$2,222,222 (\$2,222,222 less 55% estate tax equals \$1,000,000 bequest).

C. CAVEATS RELATING TO LIFETIME GIFTS (or the Effect of Paying a Gift Tax Now to save Estate Taxes Later).

1. Under Code Section 2035(c), in order to realize the advantage of lifetime gifts described above, the donor must survive for three years after the gift is made.
2. In addition to the lower gift tax rate applied to the transferred property, all the income from and appreciation of the gifted property escapes any further estate and gift taxation to the donor.

EXAMPLE #3: Post-Gift Appreciation Escapes Taxation¹

A. Lifetime Gift. Mom gifts \$1,000,000 to Daughter in 1995 triggering gift tax of \$550,000, with gifted property earning 5% per year after-tax (and it is presumed Daughter does not consume any of the property or its income). Accordingly, if Daughter dies in 2015, the gifted property along with its earnings, will be worth \$2,653,298 in Daughter's hands. No further transfer tax will be due at Mom's death.

Total Cost is \$1,555,000 to transfer \$2,653,298

B. Testamentary Bequest. On the other hand, if Mom had waited until she died to transfer the property, estate taxes on the \$2,653,298 would have been \$1,459,314, leaving \$1,193,984 for Daughter.

Total Cost is \$1,459,314 to transfer \$1,193,984;

[Daughter receives \$1,459,314 LESS than Lifetime Gift in Example # 3.A.]

3. However, the lower tax rate on lifetime gifts must be weighed against;
 - The foregone earnings on the gift tax paid;
 - Loss of "stepped-up" basis upon donor's death.

EXAMPLE #4: Effect of Foregone Earnings on Gift Taxes Paid

Testamentary Bequest. Same as Example #3.B. above, with a 5% after-tax return on the \$550,000 gift tax paid, Mom would have \$4,112,611 at her death in 2015 (\$1,000,000 gift plus \$550,000 gift tax paid compounded at 5% for 20 years). Estate taxes of 55% of that amount would be \$2,261,936, leaving \$1,850,675 for Daughter.

Total Cost is \$1,459,314 to transfer \$1,193,984

[Daughter receives \$802,623 LESS than Lifetime Gift in Example # 3.A.]

¹Examples #3 and #4 are adapted from Kathryn G. Henkel, *ESTATE PLANNING AND WEALTH PRESERVATION*, ¶8.03 (1st ed. 1997), Warren Gorham & Lamont

4. **Other Factors to Consider:**

- a. Psychological unwillingness to pay gift taxes during the lifetime of the donor;
- b. If estate and gift taxes are repealed by Congress, the effect of paying current gift taxes now would be detrimental;
- c. Computational quagmire trying to quantify benefits of large lifetime taxable gifts where donor has a relatively good life expectancy. Analysis may be too speculative or confusing for unsophisticated clients.

II. TAX APPORTIONMENT

A. WHAT IS IT?

SOURCE OF TAX PAYMENTS - WHO will pay the dollars to the government.

1. This issue can seriously affect an estate plan;
2. Need to consider and draft tax apportionment clauses with care;
3. This area has high attorney malpractice vulnerability.

B. WHY HASN'T IT BEEN A PROBLEM FOR ME SO FAR IN MY ESTATE PLANNING PRACTICE?

1. Luck;
2. Only affects taxable estates.

C. WARNING SIGNS THAT TAX APPORTIONMENT ISSUES MAY EXIST.

1. Substantial non-probate assets pass to beneficiaries different than those receiving probate assets;
2. Substantial bequests (including assets with beneficiary designation) pass to individuals other than the residuary takers;

3. If the property passing outside the will (or to non-residuary takers) is insubstantial, then the incremental tax on such property is likely to be nominal and therefore not a problem;
4. Most often, tax apportionment problems arise in clients,
 - a. without children;
 - b. having multiple marriages with children by different marriages;
 - c. having specific assets (such as a farm or business interest) which are specifically bequested or pass outside the will to one of several children.

D. GENERAL EXAMPLES.

EXAMPLE #5 - Specific Bequest of Business to Son Adversely Affects Daughter's Residuary Share.

Dad dies in 1997, leaving a specific bequest of his \$1,000,000 business to Son. The residuary estate of \$1,000,000 goes to Daughter. The will provides that the executor shall "pay all estate and inheritance taxes without apportionment or reimbursement." Result: Daughter's share will bear the entire estate tax of \$588,000, leaving her with a net of \$412,000, while Son receives \$1,000,000.

EXAMPLE #6 - Estate Tax Borne Proportionately By Specific and Residuary Legatees.

Mom, a widow, dies with a taxable estate in 1997 of \$2,000,000 triggering estate taxes of \$588,000. Mom specifically bequests \$200,000 to A, \$800,000 to B, and leaves the residue in equal shares to C and D. None of the beneficiaries is a charity. If the taxes are borne proportionately by each recipient, the following results:²

	A	B	C	D
Pre-Tax Bequest	200,000	800,000	500,000	500,000
Estate Taxes	<u>(58,800)</u>	<u>(235,200)</u>	<u>(147,000)</u>	<u>(147,000)</u>
Property Received	141,200	564,800	353,000	353,000

EXAMPLE #7 - Taxes Borne by Residuary Legatees

²Examples #5 through #8 are generally adapted from 219-5th, page A-28, "Estate Tax Payments and Liabilities", *Tax Management, Estates, Gifts, and Trust Portfolios, BNA (1998)*

Assume the same facts as Example #6 above, except that the taxes are borne solely by the residuary legatees. The results are as follows:

	A	B	C	D
Pre-Tax Bequest	200,000	800,000	500,000	500,000
Estate Taxes	<u>0</u>	<u>0</u>	<u>(294,000)</u>	<u>(294,000)</u>
Property Received	200,000	800,000	206,000	206,000

EXAMPLE #8 - Beneficiary C is a Charity To Whom Estate Taxes Are Not Apportioned - Charitable Deduction is NOT Affected.

Assume the same facts in Example #6 except that C is a charity and all taxes are borne by D as the nonresiduary remainderman (the taxable estate is thus \$1,500,000). The results are as follows:

	A	B	C	D
Pre-Tax Bequest	200,000	800,000	500,000	500,000
Estate Taxes	<u>0</u>	<u>0</u>	<u>0</u>	<u>(363,000)</u>
Property Received	200,000	800,000	500,000	137,000

EXAMPLE #9 - Beneficiary C is a Charity To Whom Estate Taxes Are Apportioned - Charitable Deduction is Decreased.

Assume the same facts in Example #6 except that charity C bears 50% of the tax burden. In such case, the computation of the charitable deduction is interrelated with the computation of the estate tax. Final results - the charitable deduction is decreased from \$500,000 to \$265,806. This causes the estate tax to increase from \$363,000 to \$468,387. The results are as follows:

	A	B	C	D
Pre-Tax Bequest	200,000	800,000	500,000	500,000
Estate Taxes	<u>0</u>	<u>0</u>	<u>(234,193)</u>	<u>(234,193)</u>
Property Received	200,000	800,000	265,807	265,807

OBSERVATION - REDUCTION OF CHARITABLE & MARITAL

DEDUCTIONS DUE TO TAX APPORTIONMENT. The same “problem” exists with regard to the marital deduction. Whenever a beneficiary is a spouse or charity, the method of apportioning estate taxes may affect the amount of the marital or charitable deduction and the estate tax itself. Simply put, if the amount which the spouse (or charity) receives bears a portion of the estate taxes, then the deductible amount is decreased as it is based on the net after-tax amount received.

EXAMPLE #10 - “Proportionate” vs. “Incremental” Apportionment

Mom dies in 1997 leaving \$1,000,000 through her will to Daughter. Son is named as the primary beneficiary of a \$1,000,000 insurance policy on Mom's life. Estate taxes on the \$2,000,000 taxable estate are \$588,000. There are three likely apportionment results attributable to this example:

1. **Executor to pay all taxes from residue without apportionment:**

\$588,000 is paid from Daughter’s residuary share (receives \$412,000);

\$0 is paid from Son’s share (receives \$1,000,000).

2. **Tax clause provides for "proportionate reimbursement"**

\$294,000 is paid from Daughter's residuary share (receives \$706,000);

\$294,000 is paid from Son’s share (receives \$706,000).

3. **Tax clause provides for "incremental reimbursement"**

\$153,000 is paid from Daughter's residuary share (receives \$847,000)
[Estate taxes generated on 1st \$1 million];

\$435,000 is paid from Son's share (receives \$565,000)
[Estate taxes generated on 2nd \$1 million].

E. FEDERAL APPORTIONMENT STATUTES

1. **IRC Section 2206 - Life Insurance**

SEC. 2206. LIABILITY OF LIFE INSURANCE BENEFICIARIES.

Unless the decedent directs otherwise in his will, if any part of the gross estate on which tax has been paid consists of proceeds of policies of insurance on the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds of such policies bear to the taxable estate. If there is more than one such beneficiary, the executor shall be entitled to recover from such beneficiaries in the same ratio. In the case of such proceeds receivable by the surviving spouse of the decedent for which a deduction is allowed under section 2056 (relating to marital deduction), this section shall not apply to such proceeds except as to the amount thereof in excess of the aggregate amount of the marital deductions allowed under such section.

- Will or trust may waive apportionment or reimbursement rights;
- This statute provides for proportional reimbursement;
- Property qualifying for marital deduction excepted.

2. **IRC Section 2207 - General Power of Appointment**

SEC. 2207. LIABILITY OF RECIPIENT OF PROPERTY OVER WHICH DECEDENT HAD POWER OF APPOINTMENT.

Unless the decedent directs otherwise in his will, if any part of the gross estate on which the tax has been paid consists of the value of property included in the gross estate under section 2041, the executor shall be entitled to recover from the person receiving such property by reason of the exercise, nonexercise, or release of a power of appointment such portion of the total tax paid as the value of such property bears to the taxable estate. If there is more than one such person, the executor shall be entitled to recover from such persons in the same ratio. In the case of such property received by the surviving spouse of the decedent for which a deduction is allowed under section 2056 (relating to marital deduction), this section shall not apply to such property except as to the value thereof reduced by an amount equal to the excess of the aggregate amount of the marital deductions allowed under section 2056 over the amount of proceeds of insurance upon the life of the decedent receivable by the surviving spouse for which proceeds a marital deduction is allowed under such section.

- Will or trust may waive apportionment or reimbursement rights;
- This statute provides for proportional reimbursement;
- Property qualifying for marital deduction excepted.

3. **IRC Section 2207A - "QTIP" Marital Property**

SEC.2207A. RIGHT OF RECOVERY IN THE CASE OF CERTAIN MARITAL DEDUCTION PROPERTY.

(a) RECOVERY WITH RESPECT TO ESTATE TAX.—

(1) IN GENERAL.— If any part of the gross estate consists of property the value of which is includible in the gross estate by reason of section 2044 (relating to certain property for which marital deduction was previously allowed), the decedent's estate shall be entitled to recover from the person receiving the property the amount by which—

(A) the total tax under this chapter which has been paid, exceeds

(B) the total tax under this chapter which would have been payable if the value of such property had not been included in the gross estate.

(2) DECEDENT MAY OTHERWISE DIRECT.— Paragraph (1) shall not apply with respect to any property to the extent that the decedent in his will (or a revocable trust) specifically indicates an intent to waive any right of recovery under this subchapter with respect to such property.

- Relates to QTIP marital trust where trust is established by 1st to die's estate plan, but trust value is included in surviving spouse's estate, thereby triggering estate taxes for surviving spouse's estate;
- This statute provides for incremental reimbursement;
- Section 2207A(a)(2) was amended by the Tax Relief Act of 1997 to mandate that the surviving spouse must specifically waive QTIP reimbursement rights. Previously this right of reimbursement was often accidentally waived by boilerplate language in surviving spouse's will or trust that taxes be paid from his or her estate.

4. IRC Section 2207B - Retained Interests

SEC.2207B. RIGHT OF RECOVERY WHERE DECEDENT RETAINED INTEREST

(a) ESTATE TAX.—

(1) IN GENERAL.— If any part of the gross estate on which tax has been paid consists of the value of property included in the gross estate by reason of section 2036 (relating to transfers with retained life estate), the decedent's estate shall be entitled to recover from the person receiving the property the amount which bears the same ratio to the total tax under this chapter which has been paid as --

(A) the value of such property, bears to

(B) the taxable estate.

(2) DECEDENT MAY OTHERWISE DIRECT.— Paragraph (1) shall not apply with respect to any property to the extent that the decedent in his will (or a revocable trust) specifically indicates an intent to waive any right of recovery under this subchapter with respect to such property.

- Will or trust may waive apportionment or reimbursement rights;
- This statute provides for proportional reimbursement;

- As in Section 2207A, surviving spouse must specifically waive reimbursement rights.

5. Apportionment of Generation Skipping Tax (“GST”) - Sections 2603, 2621-2623.

- TAXABLE DISTRIBUTION - GST paid by the transferee on value of property received by the transferee (tax inclusive);
- TAXABLE TERMINATION - GST paid by the trustee on the value of all property with respect to which the taxable termination has occurred;
- DIRECT SKIP - GST paid by the transferor on the value of the property received by the transferor.

a. Section 2603(b) states that the GST shall be charged to the property constituting such transfer unless the governing instrument provides otherwise by specific reference to the GST tax (i.e., \$1 million specific bequest to grandchild generating \$550,000 GST tax is charged against that property [grandchild receives \$450,000] unless will or trust specifically provides that the residue is to pay the GST tax);

b. The distinct methods of computing the GST make taxable distributions and taxable terminations more expensive than direct skips.

F. ILLINOIS LAW RELATING TO APPORTIONMENT.

1. **Equitable Apportionment.** Equitable apportionment is the term which is used to describe the process of distributing the burden of certain estate expenses among those beneficiaries in the same proportion as they respectively cause such expenses to be incurred. It is most commonly used to describe the apportionment of taxes among the beneficiaries of the estate. It is also sometimes used to apply to the apportionment of costs of administration.” *Robert S. Hunter, Estate Planning and Administration in Illinois, §139.1 (3rd ed., Volume 2, 1997), West Group (emphasis added)*

2. **Landmark Trust Co. v. Aitken, 224 Ill.App.3d at 852-854 (1992):**

““Equitable apportionment” is the term which is used to describe the process of distributing the burden of certain estate expenses among those beneficiaries in the same proportion as they respectively cause such expenses to be incurred. (*Horwitz v. Ritholz* (1984), 125 Ill.App.3d 193, 198, 80 Ill.Dec. 530, 533, 465 N.E.2d 642, 645.) The United States Supreme Court has held that States are free, if they so choose, to apportion the burden of estate taxes. (*Riggs v. Del Drago* (1942), 317 U.S. 95, 97-98, 87 L.Ed. 106, 110-11, 63 S.Ct. 109, 110.) While many jurisdictions have specific statutes providing for equitable apportionment of estate taxes among beneficiaries of the taxable estate, except where provided for otherwise by the will (Annot., 37 A.L.R.2d 14 (1954)), Illinois applies this doctrine only by case law. The Illinois Supreme Court has permitted apportionment of Federal estate taxes among recipients of *probate and nonprobate* assets where a decedent dies intestate, leaving property subject to probate as well as property held in joint tenancy and outside of probate (*Roe v. Estate of Farrell*

(1978), 69 Ill.2d 525, 14 Ill.Dec. 466, 372 N.E.2d 662), and also where the decedent did not provide any direction as to the payment of Federal estate taxes in his will (*In re Estate of Gowling* (1980), 82 Ill.2d 15, 44 Ill.Dec. 297, 411 N.E.2d 266). In other words, Illinois recognizes contribution from surviving joint tenants and life insurance beneficiaries towards payment of the Federal estate tax upon the jointly owned property or life insurance proceeds which an executor or administrator must include in the decedent's gross estate for Federal estate tax purposes, along with contribution from the legatees or devisees for the taxes generated by the decedent's probate estate assets. However, equitable apportionment of Federal estate tax liability among recipients of probate and nonprobate assets is not recognized under Illinois law when the will directs, as in the instant case, that the estate will be responsible for payment of "all estate, inheritance, succession and transfer taxes", and that "my executors shall not be entitled to reimbursement therefor from any persons against whom such taxes may be levied or assessed, or from any person who may have received any property so taxed." (See *Horwitz*, 125 Ill.App.3d at 201-02, 80 Ill.Dec. at 535, 465 N.E.2d at 647.) Such language is construed to be a clear intention to the contrary of equitable apportionment. Additionally, a direction in a will that taxes were to be paid from the residuary estate without reimbursement from any person has been held to be a clear expression of the testator's intent that the equitable apportionment doctrine should not apply. *In re Estate of Fry* (1989), 188 Ill.App.3d 336, 339-40, 135 Ill.Dec. 752, 754, 544 N.E.2d 109, 111."

3. General summary of Illinois principles relating to apportionment

- a. In an intestate estate, the tax will be equitably apportioned between surviving heirs and joint tenants;
- b. In testate estates, absent a clear and strong direction in the will against apportionment, the tax will be apportioned between probate and nonprobate assets with the apportioned share of the probate assets first paid from the residue of the estate;
- c. Property passing to a surviving spouse by intestacy, testacy, or by statutory share which qualifies for a marital deduction, will not share liability for estate taxes. (for example, a surviving spouse's statutory share equals one-third of the decedent spouse's estate without any reduction for estate taxes).

4. Other issues.

- a. Costs of administration may be apportioned between probate and non-probate assets. Roe v Estate of Farrell, 69 Ill 2d 525, 14 Ill Dec 466, 372 NE2d 662, 41 AFTR 2d 78-1461 (1978). However, it is unclear how such apportionment is made (i.e., upon amounts or time expended in collecting and transferring of respective assets?). For example, if significant non-probate assets require little attention from the representative and the attorney, to what degree can administration costs be apportioned to such assets?
- b. Enforcement of apportionment rights by executor/trustee - separate action or by citation proceedings.

III. SAMPLE TAX CLAUSES.

EXHIBIT A. EXECUTOR PAY ALL TAXES WITHOUT APPORTIONMENT OR REIMBURSEMENT - BURDEN ON THE RESIDUE; NO SPECIFIC WAIVER OF REIMBURSEMENT FOR SECTION 2207A AND 2207B PROPERTY

EXHIBIT B. EXECUTOR PAY ALL TAXES - SECTION 2206 AND 2207 PROPORTIONATE REIMBURSEMENT RIGHTS RETAINED FOR LIFE INSURANCE AND POWER OF APPOINTMENT PROPERTY; NO SPECIFIC WAIVER OF REIMBURSEMENT FOR SECTION 2207A AND 2207B PROPERTY

EXHIBIT C. EXECUTOR PAY ALL TAXES - SECTION 2206 AND 2207 INCREMENTAL REIMBURSEMENT RIGHTS RETAINED FOR LIFE INSURANCE AND POWER OF APPOINTMENT PROPERTY; NO SPECIFIC WAIVER OF REIMBURSEMENT FOR SECTION 2207A AND 2207B PROPERTY

EXHIBIT D. EXECUTOR TO PAY TAXES, EXCEPT EXECUTOR NOT TO PAY TAXES GENERATED BY (i) POWER OF APPOINTMENT PROPERTY; (ii) QTIP PROPERTY (UNLESS FOR GST PURPOSES THE DECEASED SPOUSE IS TREATED AS TRANSFEROR); (iii) LIFE INSURANCE NOT OWNED BY THE DECEDENT (i.e., IRREVOCABLE LIFE INSURANCE TRUSTS). THE EXECUTOR IS ALSO NOT TO PAY GST TAX ON DIRECT SKIPS CAUSED BY A DISCLAIMER OR FROM A TRUST NOT CREATED BY THE DECEDENT (i.e., A MARITAL TRUST).

EXHIBIT E. TAX CLAUSE IN QTIP MARITAL TRUST OF FIRST SPOUSE TO DIE STATING INTENTION THAT SURVIVING SPOUSE NOT PAY TAXES ATTRIBUTABLE TO QTIP TRUST. INCREMENTAL REIMBURSEMENT RIGHTS FOR SURVIVING SPOUSE

EXHIBIT F. PRIMARY TAX BURDEN ON LIVING TRUST - SECONDARY BURDEN ON PROBATE ESTATE

EXHIBIT G. SECONDARY TAX BURDEN ON LIVING TRUST - PRIMARY BURDEN ON PROBATE ESTATE

EXHIBIT A. EXECUTOR PAY ALL TAXES WITHOUT APPORTIONMENT OR REIMBURSEMENT - BURDEN ON THE RESIDUE; NO SPECIFIC WAIVER OF REIMBURSEMENT FOR SECTION 2207A AND 2207B

PROPERTY.³

I direct my executor to pay from the residue of my estate passing hereunder, without apportionment or reimbursement, all of my debts, all expenses of administration of property wherever situated passing under this will or otherwise, and all estate, inheritance, transfer, and succession taxes other than any tax on a generation-skipping transfer which is not a liability of my estate (including interest and penalties thereon, if any) which becomes due by reason of my death.

- This clause bases the burden for all debts, expenses and taxes (other than generation-skipping taxes) on the residue of the estate. The general right to apportionment is waved;
- However, because this clause would does not waive the right to reimbursement for Sections 2207A and 2207B property as there is no specific reference to such statutes.

³ Adapted from Drafting Wills and Trust Agreements, (ICLE-1990), Chapter 13

EXHIBIT B. EXECUTOR PAY ALL TAXES - SECTION 2206 AND 2207 PROPORTIONATE REIMBURSEMENT RIGHTS RETAINED FOR LIFE INSURANCE AND POWER OF APPOINTMENT PROPERTY; NO SPECIFIC WAIVER OF REIMBURSEMENT FOR SECTION 2207A AND 2207B PROPERTY.⁴

I direct my executor to pay from the residue of my estate passing hereunder, without apportionment or reimbursement, all of my debts, all expenses of administration of property wherever situated passing under this will or otherwise, and all estate, inheritance, transfer, and succession taxes other than any tax on a generation-skipping transfer which is not a liability of my estate (including interest and penalties thereon, if any) which becomes due by reason of my death, except that the amounts by which any such items shall be increased by reason of property over which I have a power of appointment or by reason of any proceeds of life insurance shall be paid by, charged to, and collected from the person (or ratably by the persons) holding or receiving the property in the proportion which the value of the property bears to my taxable estate. I authorize my executor to take such action as may be necessary to collect payments for these items from the legatees and beneficiaries responsible therefor, and my executor may withhold such amounts from any property otherwise distributable to any legatee or beneficiary hereby made responsible for their payment.

EXHIBIT C. EXECUTOR PAY ALL TAXES - SECTION 2206 AND 2207 INCREMENTAL REIMBURSEMENT RIGHTS RETAINED FOR LIFE INSURANCE AND POWER OF APPOINTMENT PROPERTY; NO SPECIFIC WAIVER OF REIMBURSEMENT FOR SECTION 2207A AND 2207B PROPERTY.

I direct my executor to pay from the residue of my estate passing hereunder, without apportionment or reimbursement, all of my debts, all expenses of administration of property wherever situated passing under this will or otherwise, and all estate, inheritance, transfer, and succession taxes other than any tax on a generation-skipping transfer which is not a liability of my estate (including interest and penalties thereon, if any) which becomes due by reason of my death, except that the amounts by which such items shall be increased by reason of property over which I have a power of appointment or by reason of any proceeds of life insurance shall be paid by, charged to, and collected from the person (or ratably by the persons) holding or receiving that property. I authorize my executor to take such action as may be necessary to collect payments for these items from the legatees and beneficiaries responsible therefor, and my executor may withhold such amounts from any property otherwise distributable to any legatee or beneficiary hereby made responsible for their payment.

⁴ Exhibits C and D are adapted from Drafting Wills and Trust Agreements, (IICLE-1990), Chapter 13

EXHIBIT D. EXECUTOR TO PAY TAXES, EXCEPT EXECUTOR NOT TO PAY TAXES GENERATED BY (i) POWER OF APPOINTMENT PROPERTY; (ii) QTIP PROPERTY (UNLESS FOR GST PURPOSES THE DECEASED SPOUSE IS TREATED AS TRANSFEROR); (iii) LIFE INSURANCE NOT OWNED BY THE DECEDENT (i.e., IRREVOCABLE LIFE INSURANCE TRUSTS). THE EXECUTOR IS ALSO NOT TO PAY GST TAX ON DIRECT SKIPS CAUSED BY A DISCLAIMER OR FROM A TRUST NOT CREATED BY THE DECEDENT (i.e., A MARITAL TRUST).⁵

FIRST: My executor shall pay all expenses of my last illness and funeral, costs of administration including ancillary, costs of safeguarding and delivering legacies, and other proper charges against my estate (excluding debts secured by real property or life insurance). Except as hereinafter provided, my executor shall also pay all estate and inheritance taxes and generation-skipping taxes on direct skips which are assessed by reason of my death. Interest and penalties concerning any tax shall be paid and charged in the same manner as the tax. My executor shall make these payments from my estate without apportionment or reimbursement or charging any direct skip property.

My executor shall not pay death taxes caused by:

- (a) Property over which I may have a power of appointment,
- (b) Property in which I may have a qualifying income interest for life, unless for generation-skipping tax purposes the property has an inclusion ratio of zero and is treated as if the qualified terminable interest property election had not been made,
- (c) Proceeds of insurance policies on my life which I did not own at my death, and
- (d) Property constituting a direct skip for generation-skipping tax purposes which is caused by a disclaimer or which is from a trust not created or appointed by me.

The person holding or receiving the above-described property shall pay, either directly or to my executor, the amount, if any, by which the death taxes are increased as a result of the taxation of that property. If two or more properties cause an increase in a tax, the increase shall be allocated among the properties in proportion to their respective taxable values.

My executor's selection of assets to be sold to make the foregoing payments or to satisfy any pecuniary legacies, and the tax effects thereof, shall not be subject to question by any beneficiary.

My executor shall make such elections under the tax laws as my executor deems advisable. My executor shall allocate my generation-skipping tax exemption as it deems advisable, except that the exemption shall be allocated (a) first to property given by me rather than by another or appointed by me and (b) to a direct skip caused by a disclaimer only if no other allocation is advisable. My executor shall make elections and allocations without regard to the relative interests of the beneficiaries and without liability to any person. No adjustment shall be made between principal and income or in the relative interests of the beneficiaries to compensate for the effect of elections or allocations under the tax laws made by my executor or by the trustee.

The balance of my estate which remains after the foregoing payments have been made or provided for shall be disposed of as hereinafter provided.

⁵Form 101, Optional Clause 1, Will and Trust Forms (The Northern Trust Company)

EXHIBIT E. TAX CLAUSE IN QTIP MARITAL TRUST OF FIRST SPOUSE TO DIE STATING INTENTION THAT SURVIVING SPOUSE NOT PAY TAXES ATTRIBUTABLE TO QTIP TRUST. INCREMENTAL REIMBURSEMENT RIGHTS FOR SURVIVING SPOUSE.⁶

Upon the death of my wife any part of the principal of the Marital Trust not effectively appointed shall be added to or used to fund the Family Trust, except that, unless my wife directs otherwise by her will or revocable trust, the trustee shall first pay from the principal of the marital portion, directly or to the legal representative of my wife's estate as the trustee deems advisable, the amount by which the estate and inheritance taxes assessed by reason of the death of my wife shall be increased as a result of the inclusion of the marital portion in her estate for such tax purposes. The trustee's selection of assets to be sold to pay that amount, and the tax effects thereof, shall not be subject to question by any beneficiary.

⁶Form 101, Article FIFTH, SECTION 3, Will and Trust Forms (The Northern Trust Company)

EXHIBIT F. PRIMARY TAX BURDEN ON LIVING TRUST - SECONDARY BURDEN ON PROBATE ESTATE.⁷

Trust Provision

SECOND: Upon my death the trustee shall make the following payments from the principal of the trust estate. The trustee shall pay all expenses of my last illness and funeral, costs of administration including ancillary, costs of safeguarding and delivering legacies, claims allowable against my estate (excluding debts secured by real property or life insurance), and unsatisfied pre-residuary legacies under my will if my will contains a residuary legacy to this trust. The trustee shall also pay all estate and inheritance taxes assessed by reason of my death, except that the amount, if any, by which the estate and inheritance taxes shall be increased as a result of the inclusion of property in which I may have a qualifying income interest for life or over which I may have a power of appointment shall be paid by the person holding or receiving that property. Interest and penalties concerning any tax shall be paid and charged in the same manner as the tax. The trustee may make payment directly or to the legal representative of my estate, as the trustee deems advisable. I hereby waive all rights of apportionment or reimbursement for any payments made pursuant to this article.

Assets or funds otherwise excludable from my gross estate for federal estate tax purposes shall not be used to make the foregoing payments. The trustee's selection of assets to be sold for that purpose or to satisfy any pecuniary gifts, and the tax effects thereof, shall not be subject to question by any beneficiary.

The trustee shall make such elections and allocations under the tax laws as the trustee deems advisable, without regard to the relative interests of the beneficiaries and without liability to any person. No adjustment shall be made between principal and income or in the relative interests of the beneficiaries to compensate for the effect of elections or allocations under the tax laws made by the legal representative of my estate or by the trustee.

Any tangible personal property held by the trustee as of my death shall be distributed by the trustee in accordance with the provisions of my will.

The balance of the trust estate which remains after the foregoing payments have been made or provided for shall be held and disposed of as hereinafter provided.

Will Provision

FIRST: My executor shall not pay expenses of my last illness and funeral, claims, costs of administration and taxes assessed by reason of my death as I have directed their payment under the trust agreement hereafter mentioned, and I hereby confirm that direction.

My executor shall make such elections and allocations under the tax laws as my executor deems advisable, without regard to the relative interests of the beneficiaries and without liability to any person. No adjustment shall be made between principal and income or in the relative interests of the beneficiaries to compensate for the effect of elections or allocations under the tax laws made by my executor or by the trustee under the trust agreement hereafter mentioned.

EXHIBIT G. SECONDARY TAX BURDEN ON LIVING TRUST - PRIMARY BURDEN ON

⁷Forms 109 and 201, Will and Trust Forms (The Northern Trust Company)

PROBATE ESTATE.⁸

Trust Provision

SECOND: Upon my death, if I have no probate estate, or to the extent that the cash and readily marketable assets in the principal of the residue of my probate estate are insufficient, the trustee shall make the following payments from the principal of the trust estate. The trustee shall pay the expenses of my last illness and funeral, costs of administration including ancillary, costs of safeguarding and delivering legacies, claims allowable against my estate (excluding debts secured by real property or life insurance), and pre-residuary legacies under my will if my will contains a residuary legacy to this trust. The trustee shall also pay the estate and inheritance taxes assessed by reason of my death, except that the amount, if any, by which the estate and inheritance taxes shall be increased as a result of the inclusion of property in which I may have a qualifying income interest for life or over which I may have a power of appointment shall be paid by the person holding or receiving that property. Interest and penalties concerning any tax shall be paid and charged in the same manner as the tax. The trustee may make payment directly or to the legal representative of my estate, as the trustee deems advisable. I hereby waive all rights of apportionment or reimbursement for any payments made pursuant to this article.

Assets or funds otherwise excludable from my gross estate for federal estate tax purposes shall not be used to make the foregoing payments. The trustee's selection of assets to be sold for that purpose or to satisfy any pecuniary gifts, and the tax effects thereof, shall not be subject to question by any beneficiary.

The trustee shall make such elections and allocations under the tax laws as the trustee deems advisable, without regard to the relative interests of the beneficiaries and without liability to any person. No adjustment shall be made between principal and income or in the relative interests of the beneficiaries to compensate for the effect of elections or allocations under the tax laws made by the legal representative of my estate or by the trustee.

The balance of the trust estate which remains after the foregoing payments have been made or provided for shall be held and disposed of as hereinafter provided.

Will Provision

FIRST: My executor shall pay all expenses of my last illness and funeral, costs of administration including ancillary, costs of safeguarding and delivering legacies, and other proper charges against my estate (excluding debts secured by real property or life insurance). My executor shall also pay all estate and inheritance taxes assessed by reason of my death, except that the amount, if any, by which the estate and inheritance taxes shall be increased as a result of the inclusion of property in which I may have a qualifying income interest for life or over which I may have a power of appointment shall be paid by the person holding or receiving that property. Interest and penalties concerning any tax shall be paid and charged in the same manner as the tax. I waive for my estate all rights of apportionment or reimbursement for any payments made pursuant to this article. If, however, the cash and readily marketable assets in the principal of the residue of my estate are insufficient to make the foregoing payments in full, my executor shall certify the amount of the insufficiency to the then acting trustee under the trust agreement hereafter mentioned for payment.

My executor's selection of assets to be sold to make the foregoing payments or to satisfy any pecuniary legacies, and the tax effects thereof, shall not be subject to question by any beneficiary.

My executor shall make such elections and allocations under the tax laws as my executor deems advisable, without regard to the relative interests of the beneficiaries and without liability to any person. No adjustment shall be made between principal and income or in the relative interests of the beneficiaries to compensate for the effect of elections or allocations under the tax laws made by my executor or by the trustee under the trust agreement hereafter mentioned.

The balance of my estate which remains after the foregoing payments have been made or provided for shall be disposed of as hereinafter provided.

⁸Forms 109 and 201, Will and Trust Forms (The Northern Trust Company)