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Trusts and Estates Law Section Newsletter

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A Message from the Section Chair

Betsy Hartnett

Greetings. Our New York State Bar Association is a dynamic and proactive organization advancing the interests of the members of the bar while effecting good for our community. One of its more exciting initiatives is one President Vincent E. Doyle introduced this year. It is the Section Diversity Challenge 2011-2012. The goal is for each of the Sections of the Bar to develop and execute initiatives to increase the diversity of the Section's membership, leadership and programs and to evaluate the results. Our Section is very fortunate in that past Chair Gary Friedman recognized the need and formed a Diversity Committee in 2010. Our committee, led by Lori Anne Douglass and Anne Bederka, has been very active since then. You will find an introduction to this committee in our next issue.

Our Committee is very excited about the Diversity Challenge and is committed to getting the win for the Trusts and Estates Law Section. I am confident they will. As we plan for meetings, CLE programs, committee assignments, awards or other Section activities, please incorporate an objective to increase the cultural and ethnic diversity of the activity. We will all benefit from greater diversity in our profession.

As I write this we are completing our Section budget for the 2012 fiscal year. While the Bar Association provides guidelines on budgeting and the initial draft budget, our Section's Treasurer Carl T. Baker and our Finance Director Lorraine Paceleo put considerable

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effort into reviewing the results of the prior year and suggesting changes and refinements to the initial draft. Our total budgeted revenue for the 2012 fiscal year is $452,250. The budget is balanced. Our Section is fortunate to maintain an accumulated surplus. A portion of that surplus will be committed to the Diversity Challenge and to a membership initiative directed at Surrogates. The officers remain committed to looking for the best value and highest quality of service to our Section members.

On the legislative front, this was a seminal year in that the Marriage Equality Act went into effect July 24, 2011. The statute presents a myriad of legal issues, as federal laws impose limitations to true equality and universal recognition of same-sex marriage. Our Section, together with the Family Law Section and the Bar's Committee on LGBT People and the Law, will sponsor a conference and simultaneous video conference link entitled "Same-Sex Marriage in New York: What Every Practitioner Needs to Know." The program's goal is to prepare attorneys to give clients proper advice and counsel on numerous issues, including taxes, estate planning, children, dissolution and interstate recognition of New York same-sex marriages. Please look for further information on this conference.

In our Section we are focused on how the SCPA and EPTL may be affected by the Marriage Equality Act. Ilene Cooper and Darcy Katris are co-chairing an ad hoc subcommittee for that study. Our Taxation Committee, chaired by Larry Keiser, is joining members of the Tax Section and the New York Department of Taxation and Finance to begin a discussion on the impact of the same-sex marriage legislation on various New York tax matters. Carolyn Lee (cjlee@JonesDay.com) is spearheading this effort for the Tax Section. Please contact any of these individuals if you wish to contribute to their efforts.

Other New York legislation that affects our practice passed both houses and was sent to the Governor's office. Assembly Bill A7729 amends EPTL 2-1.13, which was added last year in response to the repeal of the Federal estate and generation-skipping transfer taxes in 2010. In December the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "2010 Act") retroactively reinstated the estate tax. The 2010 Act also gives the estates of decedents dying in 2010 an option to elect out of the estate tax and be subject to a carry-over basis regime. EPTL 2-1.13 required clarification in light of the Federal election options created by the 2010 Act. As a result of the amendment, credit shelter formula clauses in testamentary documents of decedents dying in 2010 will now be interpreted with reference to a $5 million Federal estate and GST tax exemption amount regardless of whether the estate is subject to an estate tax or a modified carry-over basis regime.

Another clarifying initiative was made to the renunciation statute, EPTL 2-1.11, with respect to renunciations by joint tenants and tenants by the entirety. Bill A6837 modifies the 2010 amendment to EPTL 2-1.11 to make clear that a renunciation can be made when a joint tenancy is created or at the death of a joint tenant by adding language consistent with Treasury Regulations § 25.2518-2. Our Section submitted a Memorandum in Support of this legislation.

In response to the Court of Appeals decision *In Re Singer*, 13 NY 3d 447 (2009), which greatly altered the scope of SCPA 1404 examinations where a will contains an in terrorem clause, Bill A6838A was introduced as a clarification of the scope of the statutory safe harbor. This measure expands the safe harbor at the discretion of the Surrogate so long as special circumstances are presented that show that the person to be examined may provide information with respect to the validity of the will that is of substantial importance or relevance to a decision to file objections to the will. The Memorandum in Support asserts that this measure, along with the Uniform Rule 207.27 which limits examinations before trial, will entrust to the Surrogate the "intelligent management of the discovery process." I have asked our Surrogate Court and Estate Litigation committees to monitor this legislation and to make any further recommendations in light of its impact on our practice.

Finally, the decanting statute, EPTL 10-6.6, was substantially revised. Importantly, the measure permits a trustee to pay over the principal of a trust to a new trust even if the trustee does not have absolute discretion to invade principal. With respect to inter vivos trusts, it is no longer necessary to file the decanting instrument with the court unless the trust has been the subject of a proceeding in the Surrogate's Court. The new statute clarifies how the decanting operates in the context of a multi-beneficiary trust. As a safeguard the statute now expressly prohibits any trust changes that would adversely affect tax structuring relating to the invaded trust. Lastly, the revised statute clarifies fiduciary duties with regard to decanting and sets a standard of care.

Elizabeth A. Hartnett

Editor's Message

In October the Trusts and Estates Law Section will gather in Buffalo, New York for a joint Fall Meeting with the Elder Law Section. To mark the occasion, this issue of the *Newsletter* includes two pieces highlighting an important area where our practices intersect—namely, planning for incapacity. In "Hidden Pitfalls in the Statutory Short Form Power of Attorney," Austin Bramwell identifies some surprising traps for the unwary in New York's new statutory power of attorney forms. He offers sage advice on the preparation and execution of these forms to help avoid inadvertently exposing a client's power of attorney to attack. Jonathan Rikoon, Mordy Serle and Louise Yang outline the current New York law on end of life decisions, both by appointed health care agents and under the recent Family Health Care Decisions Act (FHCDA), which applies when no agent or guardian has been appointed. Their comprehensive article includes interesting observations about the degree to which a health care agent or surrogate must take into account a patient's religious and moral beliefs in making end of life decisions.

Section members who attended our Spring Meeting in Turnberry Isle, Florida, in April will recall Carlyn McCaffrey's excellent presentation on "Fixing Broken Trusts." Carlyn discussed the various tools available under state law to fix wills and irrevocable trusts, as well as some of the likely federal tax consequences of each approach. For those of you who were unable to attend the meeting, I'm very pleased to include in the *Newsletter* a two-part article adapted from Carlyn's course book outline. The first installment appears in this issue and explores construction and reformation proceedings.

Among the many important legislative developments in New York this past year was the adoption of the New York Prudent Management of Institutional Funds Act (NYPMIFA) on September 17, 2010. The Office of the Attorney General's Charities Bureau released guidance on the legislation on March 17, 2011. Michael Cooper reports on the many ways in which NYPMIFA affects New York not-for-profit organizations, including new rules on the investment and spending of endowments and other institutional funds. His article is required reading for anyone representing charitable organizations or donors.

In our second installment of "The Liability Reporter," Michael Ryan reports on two post-*Schneider* estate planning malpractice cases in New York and a recent Ethics Opinion of the New York State Bar Association's Committee on Professional Ethics. Opinion 865 addresses whether in the wake of *Schneider* an attorney who prepared a client's estate plan may ethically agree to represent an executor in connection with the administration of the client's estate.

In this issue we also introduce a new regular feature, the "Florida Update," by David Pratt and Jonathan Galler. This column summarizes recent legislative activity and noteworthy decisions pertaining to Florida trusts and estates law.

The editorial board is soliciting submissions for the Spring 2012 *Newsletter*. We welcome articles and columns, case reports and materials from continuing legal education or other presentations (either original or adapted for publication here), as well as opinion pieces and letters to the editor. The deadline for submission is December 15, 2011.

Cristine M. Sapers

The editorial board of the T*rusts and Estates Law Section Newsletter* is:

Cristine M. Sapers cmsapers@debevoise.com
Editor in Chief

Wendy H. Sheinberg wsheinberg@davidowlaw.com
Associate Editor

Richard J. Miller, Jr. rjm@mormc.com
Associate Editor

Jaclene D'Agostino jdagostino@farrellfritz.com
Associate Editor

Naftali T. Leshkowitz ntl@leshkowitzlaw.com
Associate Editor

Hidden Pitfalls in the Statutory Short Form Power of Attorney

By Austin W. Bramwell

Despite complaints from the bar,[1] it appears that the new Statutory Short Form Power of Attorney (the "Short Form POA") and Statutory Gifts Rider (the "SGR") adopted in 2009[2] and substantially revised in 2010 (retroactive to September 1, 2009)[3] are here to stay.[4] The new forms, while improvements in many ways over the prior statutory forms, are technically demanding and create a number of traps for the unwary. Some traps are well-known, others more obscure. This article describes some of the surprising ways in which lawyers can inadvertently expose their clients' powers of attorney to attack.

Mistakes in the Short Form POA or SGR come in three kinds. First, some mistakes may prevent an instrument from qualifying as a Short Form POA but not from creating a valid power of attorney. An instrument that fails to meet the requirements of a Short Form POA may still create a valid power of attorney in New York if it satisfies the execution requirements of Section 5-1501B(1)(a)-(c) of the General Obligations Law (GOL) and contains the exact wording of the "Caution to the Principal" and "Important Information for the Agent" paragraphs of the Short Form POA.[5] Unlike a Short Form POA,[6] however, a non-statutory power of attorney is not generally required to be accepted by third parties. To escape any obligation to respect a power of attorney, no matter how unreasonable the grounds, it seems that third parties need only identify one defect that causes it to fail to be a Short Form POA.

Second, some mistakes potentially prevent a purported Short Form POA from creating a power of attorney altogether. The legislation creating the Short Form POA and SGR expanded the number of possible ways in which a power of attorney may be fatally defective. As potentially fatal defects are not always easy to spot and avoid, the new Short Form POA and SGR demand a whole new degree of diligence.

Finally, some mistakes may create ambiguity as to the scope of the agent's powers. One might think that statutory forms in which the principal confers powers simply by initialing spaces could not leave much room for dispute. When it comes to the SGR, however, what at first glance looks straightforward may become ambiguous against the backdrop of Title 15 of Article 5 of the General Obligations Law ("Title 15"). Examples of such a drafting trap are discussed towards the end of this article.

I. Mistakes that Potentially Convert a Short Form POA into a Non-Statutory Power of Attorney

The preparer "improves" the language or punctuation of the Short Form POA. The Short Form POA contains typographical inconsistencies that lawyers generally find embarrassing. For example, paragraph (d) of the form follows the British convention of placing the sentence-ending period outside of the closed quotation mark.[7] Just one sentence later, paragraph (e) places the period within the closed quotation mark.[8] Lawyers who aspire to high professional standards may feel the urge to correct this inconsistency.

The urge should be resisted. Section 5-1501(2)(n)-(o) of the GOL provides that the Short Form POA and the SGR "must…contain the exact wording" of the statutory forms. To be sure, the statute goes on to provide that "a mistake in wording, such as in spelling, punctuation or formatting, or the use of bold or italic type" will not prevent a Short Form POA or SGR from being treated as such. Perhaps under this relaxed "exact wording" standard, a mere switch in the order of punctuation marks does not render a form defective. Strictly speaking, however, GOL § 15-1501(n)-(o) only forgives inadvertent "mistakes" in punctuation, not deliberate corrections. It is not certain that any intentional change in punctuation, no matter how benign, will not convert a Short Form POA into a non-statutory power of attorney. (The statute even creates a perverse incentive to be careless, lest one be accused of having deliberately changed the form.) Cautious lawyers should retain the typographical errors in the form.

The preparer deletes "unnecessary" language. For experienced trusts and estates lawyers, it almost goes without saying that they should not delete any section of the Short Form POA or SGR. Once again, while a "mistake in wording" may be forgiven under GOL § 5-1501(2)(n)-(o), the statute does not appear to permit preparers to strike whole sections of a Short Form POA or SGR. To modify a Short Form POA, preparers may add language under paragraph (g) designated "modifications." GOL § 5-1503 states that a power of attorney containing modifications under paragraph (g) "is not prevented" from being a Short Form POA, even if those modifications effectively cancel other paragraphs of the form (such as the powers provisions). By negative implication, it appears that modifications other than under paragraph (g) will disqualify a Short Form POA.

Unfortunately, the Short Form POA can easily deceive lawyers not familiar with Title 15 into thinking otherwise. The Short Form POA contains extensive language that many (if not most) principals do not need. For example, some individuals may not wish to designate successor agents as permitted in paragraph (c), make "modifications" as permitted in section (g), authorize gift-giving as permitted in paragraph (h) (and the SGR) or designate a "monitor" as permitted in paragraph (i) of the form. Lawyers who normally would not include unnecessary or confusing boilerplate in their documents may feel tempted to delete those paragraphs in the hope of making the form less daunting to clients.

The Short Form POA makes that temptation all the more inviting by designating as "OPTIONAL" those paragraphs that the principal may not wish to complete. Those who have read Title 15 carefully understand that, by "optional," the form means that the principal need not complete a particular section. It does *not* mean that the section can be removed from the form. Nonetheless, the correct reading of the Short Form POA is not obvious on its face. Sadly, it is likely that many inexperienced attorneys have already and will continue to surmise incorrectly that they may strike the "optional" paragraphs.

II. Mistakes that Potentially Invalidate a Power of Attorney

The preparer corrects the cautionary language of the Short Form POA. Under the legislation creating the Short Form POA, *all* powers of attorney, not just Short Form POAs, must now include the same cautionary language to the principal and the agent that is found in the Short Form POA.[9] The additional requirement is designed to protect individuals from dishonest agents who might recommend the use of a non-statutory form that does not warn principals of the document's significance.[10] To achieve that result, GOL § 5-1501B(1)(d) now provides that a valid power of attorney must contain the "exact wording" of the paragraphs of the Short Form POA found under the headings "Caution to the Principal" and "Important Information for the Agent." Unlike GOL § 5-1501(2)(n), GOL § 5-1501B(1)(d) does not go on to permit mistakes of spelling, punctuation or formatting. By negative implication, therefore, it may be that not even a misspelled word in the "Caution to the Principal" or "Important Information for the Agent" language can be forgiven.

Unfortunately, that language is some of the most confusing in the Short Form POA. The following sentence, for example, which appears under "Important Information for the Agent," contains an outright falsehood:

> You may not use the principal's assets to benefit yourself or anyone else or make gifts to yourself or anyone else unless the principal has specifically granted you that authority in this document, which is either a Statutory Gifts Rider attached to a Statutory Short Form Power of Attorney or a Non-Statutory Power of Attorney.[11]

Literally, this sentence states that "this document"—i.e., the Short Form POA—is either a "Statutory Gifts Rider" or a "Non-Statutory Power of Attorney." If the Short Form POA has been properly prepared and executed, the statement is false. On the other hand, if the Short Form POA contains a defect that causes it to be treated as a non-statutory power of attorney, the statement is true. In that case, "this document" will at least be a "Non-Statutory Power of Attorney" albeit not a "Statutory Gifts Rider." In other words, the "Important Information for the Agent" is only accurate if the power of attorney is *not* in statutory form.

To rectify this absurdity would be a mistake. As noted above, the Short Form POA must contain the "exact wording" of the "Important Information for the Agent" warning. Clients rightly confused by the form should be told that certain illogical language must be included if the Short Form POA is to be considered valid.

The preparer fails to use twelve-point font or larger. Unlike the statutory forms authorized under prior law, the new Short Form POA and the SGR are long and (at least to many clients) tedious. To make the forms look shorter, a preparer might be temped to shrink their size by using a smaller font than typical. Eleven-point font, for example, often works well with boilerplate-heavy documents.

To use any font size smaller than twelve points would also be a mistake. GOL § 5-1502B(1)(a) now provides that any valid power of attorney, not just a Short Form POA, must "be typed or printed using letters which are legible or of clear type no less than twelve point in size…." The second "or" in this sentence appears to provide two alternatives for satisfying this requirement: either a power of attorney can be typed or printed in a manner that is "legible" or it can be typed or printed in twelve point font. (The elided language theoretically creates a third alternative if the power of attorney is handwritten. Given the length of the new required cautionary language, however, a valid handwritten power of attorney is unlikely.) In other words, the statute permits a power of attorney to be in a size smaller than twelve points, so long as it is "legible."

It would be unwise, however, to risk a challenge from a third or hostile party that a particular Short

Form POA is not "legible." Some individuals, after all, struggle to read even twelve-point font. The smaller the font, the larger will be the class of individuals who will not actually be able to read the form comfortably. Generally, whether a document is legible is a question of fact that ultimately requires a jury trial.[12] Given the uncertainty over the meaning and application of the term "legible," attorneys should always prepare the Short Form POA and the SGR in twelve-point font or larger. As a prophylactic measure, it may even be prudent to use a larger font, such as thirteen points.

The agent fails to date the Short Form POA. GOL § 5-1501B(1)(c) provides that a valid power of attorney must be "signed and dated" by an agent.[13] Unfortunately, while the form provides a signature line for the agent, it does not contain any space for the agent to fill in the date. If the lawyer fails to instruct the agent to date the instrument, notwithstanding the lack of any space for doing so, the power of attorney may be invalid. To avoid this trap, perhaps the best procedure is to affix an adhesive "post-it" tab to every Short Form POA reminding the agent to write in the date. The tab should not be removed until the agent has both signed and dated the form. Once again, the Short Form POA on its face invites malpractice.

The dates of execution are typed in rather than written by hand. When the exact day on which an individual will execute a particular instrument is known in advance, it often makes sense to have the date printed in the form. For example, notary publics have been known to fail to complete acknowledgment forms properly. By filling in known information in advance, the preparer can reduce the chances of error.

In the case of a Short Form POA or SGR, however, the principal (and the agent) should handwrite the date of the instrument. GOL § 5-1501B(1)(b) provides that, to be valid, a power of attorney must be "signed *and dated* by a principal with capacity…." (Emphasis added.) Likewise, GOL § 5-1514(9)(b) provides that an SGR must be "signed and dated."[14] Arguably, a Short Form POA or SGR is not properly "dated" within the meaning of these sections unless the principal (and/or the agent) writes in the date in his or her own hand. In other words, in this view, the principal may not rely on a third party (not even the form preparer) to date the instrument.

One might argue that an individual no less "dates" a document by agreeing to a date already typed in than by filling in the date himself or herself. Under the venerable "principle of signatures," courts have long recognized that an agent may execute a document on a principal's behalf.[15] There is no guarantee, however, that GOL § 5-1501B(1) or GOL § 5-1514(9)(b) incorporates the principle of signatures. Under GOL § 5-1501(2)(m), the verb "sign" is now defined broadly to mean either "to place any memorandum, mark or sign, written, printed, stamped, photographed, engraved or otherwise upon an instrument in writing" or "to use an electronic signature." The statute is silent, however, on whether any of the acts constituting a signature may be carried out by a third party on the signatory's behalf.

Meanwhile, Title 15 suggests a strict division of labor between principal and preparer. Under paragraph (g) of the SGR, the preparer should indicate that he or she prepared the SGR. After the form has been prepared, the principal then makes the SGR effective by signing and dating it. Read together, GOL § 5-1514(9)(b) and paragraph (g) of the SGR imply that, while the preparer is authorized to prepare the form, he or she may not infringe on the prerogative of the principal to "sign and date" it.

In contrast to the SGR, the Short Form POA does not contain a paragraph indicating who prepared the form. Nevertheless, the legislative history makes clear that one purpose of the new power of attorney legislation is to ensure that principals understand the gravity of granting a power of attorney.[16] In adopting the 2009 reforms, the legislature implicitly concluded that a principal's lawyer cannot be trusted to explain adequately the implications of signing a power of attorney.[17] Given the legislative distrust of form preparers, wherever Title 15 carves out a role for the principal (such as signing and dating) as opposed to the preparer, the preparer should not attempt to fulfill that role on the principal's behalf. Lawyers should instead ask clients to date their Short Form POAs and SGRs themselves.

Further support for the view that the principal should both sign and date a power of attorney comes from the contrast between the formalities for executing a power of attorney and the formalities for executing a will. Section 3-2.1 of New York's Estates, Powers & Trusts Law (EPTL) provides that a testator must "sign" his or her will if it is to be validly executed. It does not state that the testator should date it as well.[18] The contrast suggests that an additional step—namely, to date the instrument—that is not required of a testator is required of a principal who executes a power of attorney.

Unlike Title 15, EPTL 3-2.1(a)(1) expressly permits a valid will to be signed by another person at the testator's direction. Similarly, section 2981(2)(a) of the Public Health Law permits a valid health care proxy to be signed at the principal's direction. No such procedure is expressly permitted in order to execute a valid power of attorney.[19] This does not necessarily mean that Title 15 in fact prohibits a principal from executing a power of attorney by having another "sign and date" it. On the other hand, the contrast may suggest that, unlike a will or health care proxy, a power of attorney or SGR may not be validly "signed" or "dated" by a third

party, including even the form preparer. Once again, to avoid risk, the best procedure is to ask clients to date their Short Form POAs and SGRs themselves.

Potential donees witness the SGR. Under GOL § 5-1514(9)(b), a validly executed SGR must be witnessed by two individuals, who, by a cross-reference to EPTL 3-2.1(a)(2), must have been present when the SGR was signed (or must have had the principal's signature acknowledged to them).[20] The rationale for requiring witnesses is that, as gift-giving powers can substantially alter a principal's testamentary plan, the formalities for executing a valid SGR should be similar to the formalities for executing a valid will.[21] As it happens, however, the formalities for executing an SGR are in some respects significantly *more* demanding than the formalities for executing a will.

In particular, New York long ago abolished the common law "interested witness rule" that invalidates a will witnessed by individuals to whom the will makes a beneficial disposition.[22] GOL § 5-1514(9)(b), by contrast, provides that an SGR must be "witnessed by two persons who are not named in the instrument as permissible recipients of gifts…." If either witness is a potential recipient of gifts, therefore, the SGR may be invalid.

An invalid SGR may in turn invalidate the entire power of attorney that it accompanies. GOL § 5-1501(2)(o) provides that "[i]f the authority (SGR) on the statutory short form is initialed by the principal, the statutory short form power of attorney must be executed in the manner provided in section 5-1501B of this title simultaneously with the statutory gifts rider." GOL § 5-1501(2)(n) provides that the SGR "must be executed in the manner provided in § 5-1514, simultaneously with the statutory short form power of attorney in which the authority (SGR) is initialed by the principal." Reading these two provisions together, it appears that if (SGR) on the Short Form POA is initialed, then an SGR must be executed in accordance with the formalities of GOL § 5-1514(9). It follows that if the SGR is *not* properly executed, then the invalid SGR potentially renders the entire Short Form POA defective.

Unfortunately, Title 15 does not contain any "severance" provision that would protect an otherwise valid power of attorney from being invalidated by a defective SGR. On the contrary, Title 15 provides that the Short Form POA and SGR "must be read together as a single instrument."[23] Arguably, if the Short Form POA and SGR constitute a single instrument, then the set of formalities required to execute that single instrument must consist of the combined formalities for executing both components. In other words, neither form is properly executed unless both forms are properly executed.

A sympathetic court might in the end uphold a Short Form POA accompanied by a defective SGR. Fair as that outcome may seem, cautious lawyers ought not to take it for granted. The two forms are designed to ensure that principals know what they are doing when they execute powers of attorney. Any relaxation of the formalities required to execute the "single instrument" consisting of the Short Form POA and SGR would (one might argue) defeat this purpose.

Permissible recipients of gifts are unlikely to witness an SGR if the principal limits potential donees to a specified class—such as the principal's spouse and descendants—and the SGR is signed at the preparer's office. In that case, the document will typically be witnessed by attorneys or staff of the law office, who will not be permissible donees under the SGR. In those situations where a principal plans to sign the SGR at home or in a hospital without attorney supervision, the preparer must take care to instruct the principal not to have family members or other permissible donees witness the SGR.

Not all SGRs limit potential recipients of gifts to immediate family members, however. Under GOL § 5-1514(3), the agent can be authorized to make gifts in any amount, to any person or persons, and in virtually any manner. A grant of broad gifting powers has compelling advantages. For example, the agent can make lifetime gifts to legatees named in the principal's will (which may include friends and more distant relations) so as to use up the annual federal gift tax exclusion[24] with respect to each legatee. No similar such exclusion is available for estate tax purposes. In addition, the agent can eliminate the expense and delay of probate by making transfers to a revocable trust created by the principal or, if the principal has not created a revocable trust, to a new revocable trust whose provisions mirror the provisions of the principal's will (which again may include non-family members as beneficiaries).

Finally, broad gifting powers can eliminate potential ambiguities in the scope of the agent's powers. Whenever the agent has the power to make gifts, it is often advantageous to authorize the agent to make gifts in trust. On the other hand, if the principal names only a narrow class of potential donees, such as descendants, it will be unclear to what extent the restriction in the class of donees negates the power to make gifts in trust. Even trusts created primarily for the benefit of descendants, for example, normally include an "alternate takers" clause that specifies how property will be disposed of if no descendants are living. If an agent purports to make a gift in trust, but there is even a remote possibility that the trust property could pass to persons other than those included in the class of donees, then the agent's gift may be void. To avoid ambiguity and to allow for maximum planning flexibility,

therefore, including gifts in trust, principals should consider authorizing their agents to make gifts to as broad a class of persons as possible.

If a client fears that the agent will take these gifting powers too far, the client can set forth his or her wishes to the agent in a separate instrument. As GOL § 5-1505-2(a)(1) provides that an agent has a duty to follow the instructions of the principal, an agent who disregards the principal's wishes courts potentially serious liability.[25] A statement of wishes might provide, for example, that the agent may continue a pattern of gift-giving or estate planning, make deathbed gifts to save taxes or avoid probate or, during a period of incompetency from which the principal is not expected to recover, engage in estate tax savings strategies (such as gifts to grantor retained annuity trusts or installment sales to grantor trusts). The statement of wishes can even discourage or forbid the agent from acting so long as the principal is competent and available to act. Such a statement can have virtually the same effect as a "springing" power of attorney but without unduly restricting flexibility or inviting disputes over whether the event triggering the agent's powers has occurred. Finally, a separate statement of wishes can provide comfort to an agent who might otherwise be reluctant to make gifts or engage in estate tax planning strategies. In light of these advantages, attorneys should in many cases be preparing three documents under Title 15 for their clients: a Short Form POA, an SGR granting broad gift-giving powers and a separate statement of wishes to the agent.

That said, without proper drafting, a broad grant of gift-giving powers can easily run afoul of the interested witness rule. If the witnesses to the SGR are not explicitly carved out of the class of potential donees, then the witnesses may be deemed to be "named in the instrument as permissible recipients of gifts," in which case the entire SGR (and, as discussed above, the accompanying Short Form POA) may be rendered ineffective. If the principal wishes to authorize the agent to make gifts to any persons, therefore, the gift-giving powers should be drafted to exclude witnesses from the class of potential donees.

III. Other Drafting Mistakes

At least in the author's view, attorneys should almost always advise their clients of the benefits of broad gift-giving powers. GOL § 5-1514(c) provides that the principal may authorize the agent to make gifts in a variety of different ways, from opening a joint account with the principal and donee as joint tenants to designating the donee as a beneficiary of a retirement plan account. Nine such ways are listed in GOL § 5-1514(c), while the flush language goes on to describe two more. GOL § 5-1514(c)'s comprehensiveness assures that agents can be given powers to make gifts in virtually any manner.

Unfortunately, if the SGR is not properly drafted, GOL § 5-1514(c) can invite ambiguity. If the SGR lists some of the gift-giving techniques of GOL § 5-1504(c) but not others, a negative inference may arise that the agent is not permitted to exercise the omitted powers. The legislation adopting the new Short Form POA clarified that powers with respect to bank accounts, life insurance policies and retirement plans do not include powers to designate or change beneficiaries unless the authority to do so is "conveyed" in an SGR (or non-statutory power of attorney executed in the same manner as an SGR).[26] To avoid disputes over whether a particular power has actually been conveyed, the SGR should set forth all of the gifting techniques listed in GOL § 5-1504(c).[27] A long list of gifting powers will increase the SGR's length. It is better to expand a form, however, than to allow latent ambiguities. For each technique, for the reasons discussed earlier, witnesses should also be excluded from the class of beneficiaries. Otherwise, the entire Short Form POA may be rendered invalid.

IV. Conclusion

Lurking in Title 15 are many ambiguities and traps for the unwary attorney. While the new Short Form POA and SGR make many welcome improvements to the old statutory forms, they are all too easy to misuse. Attorneys must read and study Title 15 carefully in order to make sure that they are carrying out their clients' wishes properly.

Endnotes

1. *See* The New York State Law Revision Commission Report on the Statutory Gifts Rider to Powers of Attorney, September 1, 2010 at 14 ("Some lawyers have expressed concern that the Gifts Rider requires more time and does not achieve its goal of education, is not consumer friendly, is more burdensome, and adds an unnecessary layer of complexity for a client of diminished capacity."); *see also* Anthony J. Enea, *What Every Attorney Should Know about the New Durable Power of Attorney Form*, NYSBA Trusts and Estates Law Section Newsletter, Fall 2009, Vol. 42 No. 3.
2. 2008 N.Y. Laws 644, as amended by 2009 N.Y. Laws 4.
3. 2010 N.Y. Laws 340.
4. A power of attorney is a written instrument in which an individual authorizes an agent to act on his or her behalf. N.Y. General Obligations Law § 5-1501(2)(j) (GOL). The Short Form POA can be found at GOL § 5-1513 and the SGR at GOL § 5-1514(10).
5. GOL § 5-1501B(1)(d). The "Caution to the Principal" and "Important Information for the Agent" warnings can be found at GOL § 5-1513(1)(a) and GOL § 5-1513(1)(n).
6. *See* GOL § 5-1504.
7. GOL § 5-1513(1)(d).
8. GOL § 5-1503(1)(e).

9. GOL § 5-1501B(1)(d). *See also Matter of Estate of Kelley*, 26 Misc. 3d 621 (Surr. Ct. Westchester Co. 2009) (rejecting a power of attorney because it lacked the requisite cautionary language).
10. *See* New York State Law Revision Commission 2008 Recommendation on Proposed Revisions to the General Obligations Law Powers of Attorney (hereinafter the "2008 Recommendation") at 40 ("A Principal who understands the risks and obligations created in a power of attorney can be more active or vigilant in ensuring that the Agent is acting properly").
11. GOL § 5-1513(1)(e).
12. *Gozan v. Mutual Life Ins. Co. of New York*, 353 N.Y.S.2d 137 (N.Y. County Sup. Ct. 1974), *rev'd by* 374 N.Y.S.2d 323, *aff'd and reinstated by* 358 N.E.2d 499 (submitting to jury trial the sole question of whether a life insurance application was legible).
13. A power of attorney may be executed by the agent at a later time than it is executed by the principal. GOL § 5-1501B(1)(c). Lawyers may disagree on whether the agent should execute the power of attorney as soon as possible after it is executed by the principal. On the one hand, the agent's execution of the power of attorney triggers onerous obligations. *See* GOL § 5-1505. Mere failure to act can potentially subject the agent to liability. GOL § 5-1505(2)(b) ("The agent may be subject to liability for conduct *or omissions* which violate any fiduciary duty") (emphasis added). Just by accepting the appointment, the agent may unexpectedly become subject to regulatory requirements, such as obligations to report to the Treasury Department and/or the Internal Revenue Service the principal's foreign bank, securities or other financial accounts and/or foreign financial assets. *See* 31 CFR 1010.350; IRC § 6038D. (To protect the agent from potential liability for failure to report such items, the principal may wish to provide in the Short Form POA under "Modifications" that the agent has no authority over such items unless the agent delivers a notice to the principal affirmatively accepting such authority.) On the other hand, the preparer may not (unless the agent is a client) have any ethical duty to protect the agent from liability. Further, a power of attorney executed by a principal but not by an agent may have little practical utility, for if the principal becomes incompetent, the lawyer may not be able to obtain the principal's permission to share the power of attorney with the agent. In most cases, therefore, it is best to have at least one agent (preferably an agent to which the lawyer does not owe ethical duties) to execute the power of attorney.
14. GOL § 5-1514(1) also permits a non-statutory power of attorney to confer gifting powers if executed in accordance with the requirements of an SGR.
15. *See, e.g*, *Combe's Case*, 77 Eng. Rep. 843, 847, 9 Co. Rep. 75, 76-77 (1614) ("[W]hen any has authority as attorney, to do any act, he ought to do it in his name who gives the authority, for he appoints the attorney to be in his place, and to represent his person"); *Pentz v. Stanton*, 10 Wend. 271, 275 (N.Y. Sup. Ct. 1833) ("There is no doubt that a person may draw, accept or endorse a bill by his agent or attorney, and that it will be as obligatory upon him as though it were done by his own hand").
16. *See generally* 2008 Recommendation.
17. *See* 2008 Recommendation at 22 ("The Principal can delegate these sweepings powers to the Agent without fully recognizing their scope (particularly if the Principal executes the document without the benefit of legal counsel)…."). The 2008 Recommendation does not reject the possibility that even principals who have "the benefit of legal counsel" may not fully recognize the scope of the powers delegated to the agent.
18. Most lawyers nonetheless do ask the testator to write in the date of his or her will, so as to prove that the will was both signed and witnessed within thirty days as required by EPTL 3-2.1(a)(4).
19. GOL § 5-1514 does incorporate by reference the witnessing requirements of EPTL 3-2.1(b), which itself permits a testator to acknowledge that a signature was affixed "by his direction." Thus, it may in fact be possible for a third party to execute an SGR at a principal's direction.
20. It is also possible to confer gifting powers using a valid non-statutory power of attorney that is signed by two witnesses. GOL § 5-1501B(2)(b); GOL § 5-1514(1); GOL § 5-1514(9)(b). Although the SGR form includes a line for acknowledgment before a notary, it is unclear whether the SGR is required to be notarized. To avoid doubt, a notary should always be asked to acknowledge the principal's signature on both the Short Form POA and the SGR.
21. The New York State Law Revision Commission Report on the Statutory Gifts Rider to Powers of Attorney, September 1, 2010 at 12 ("The requirement of two witnesses to the Gifts Rider accompanying that statutory form power of attorney, or a non-statutory power of attorney with gifting authority, is designed to draw the principal's attention to the importance of the document and its potential effect on his or her estate").
22. EPTL 3-3.2(a). A disposition to an interested witness may be cut down or voided, but he or she is still competent to witness a will. For a review of the history of the interested witness rule in New York, see Jill Choate Beier, Theresa A. Kraker and Joseph T. La Ferlita, *Defining Beneficial Dispositions Under EPTL 3-3.2: Should Tax Non-Apportionment Clauses Count?*, NYSBA Trusts and Estates Law Section Newsletter, Summer 2011, Vol. 44 No. 2.
23. GOL § 5-1501(2)(n)-(o).
24. Internal Revenue Code § 2503(a).
25. *See also Matter of Ferrara*, 852 N.E.2d 138 (N.Y. 2006) (holding, somewhat illogically given that gifts by definition deplete the donor's assets in order to enrich the donee, that an agent has a duty to act in the principal's best interest even when exercising gifting powers). An interesting question is the extent to which an agent's duty to follow the instructions of the principal conflicts with the duty, also codified in GOL § 5-1505-2(a)(1), to act in his or her best interests. A principal's specific instructions, such an instruction to hold and never sell a particular security, may in fact go against the principal's best interest.
26. GOL § 5-1502D(1); GOL § 5-1502F(1); GOL § 5-1502L(2).
27. Incorporation of these powers by reference is inadvisable, lest the rule against incorporation by reference that applies to wills be applied by a similar line of reasoning to the SGR. *Cf. In re Klosinski*, 746 N.Y.S.2d 350 (Sur. Ct., Kings Co. 2002) ("The rationale for not allowing incorporation by reference is the possibility of fraud or mistake in relying on an outside writing, not executed in accordance with the formality required to execute a will, to determine the devolution of an estate").

Austin W. Bramwell is an associate in the trusts and estates department of Milbank, Tweed, Hadley & McCloy LLP. He is member of the Trusts and Estates Law Section of the New York State Bar Association.

Overview of End of Life Law in New York State

By Jonathan J. Rikoon, Mordy Serle and Louise D. Yang

Jonathan J. Rikoon

Mordy Serle

Louise D. Yang

The law concerning the end of a person's life is fraught with confusion. Ethics, religious beliefs, medical opinions and emotional and financial strains on the person's relatives all color and complicate the issue. People with the capacity to make their own medical decisions are permitted to consent to or refuse medical treatment, including life-sustaining treatment and artificial nutrition or hydration.[1] When a person lacks this capacity, the law attempts to determine what decision the person would have made and then to implement that decision. New York, as well as many other states, has attempted to address this issue by allowing adults who are not incapacitated to appoint health care agents to make medical decisions on their behalf once they are determined to lack the ability to make health care decisions. This article outlines current New York law with respect to end of life decisions for individuals with and without appointed health care agents. The extent of the health care agent's authority and the rights of the patient's family are also explored, although the law surrounding individuals diagnosed with mental retardation or developmental disability[2] is not addressed.

I. Extent of Appointed Health Care Agent's Authority

Pursuant to New York Public Health Law (PHL) article 29-C, any competent adult (referred to as a principal in the statute) may appoint a health care agent (an "Agent") by executing a health care proxy in accordance with the terms of the statute.[3] When the principal is determined to lack health care decision making capacity,[4] the Agent's authority pursuant to the health care proxy automatically comes into effect. With the exception of any express limitations stated by the principal in the health care proxy, the Agent, on the principal's behalf, may make almost all health care decisions that the principal could have made, and the Agent has priority over any other person with respect to health care decisions.[5] The federal district court in *Stein v. Co. of Nassau* addressed the question of a health care agent's authority to make decisions outside of the hospital context, such as choosing whether to receive treatment and at which hospital to receive treatment.[6] In *Stein*, the appointed Agent (the principal's wife) demanded that the ambulance take the principal back to the hospital that had recently released him, but the ambulance crew refused and instead took the principal to the nearest hospital. The court analyzed PHL § 2982 and decided that the health care proxy was valid outside of a hospital setting "[b]ecause the statute empowers health care agents 'to make any and all decisions' that a principal can make, [which] means that health care agents *must* be able to make the kinds of decisions that do not take place in hospitals, and thus do not occur in hospital settings."[7]

Following *Stein*, the New York Supreme Court Kings County[8] agreed that the authority of health care agents applies outside of a hospital setting (notwithstanding the partial reversal of *Stein* on other grounds). The *Verponi* decision also held that no written determination of incapacity by a physician is required[9] for an Agent to be empowered to act on behalf of the principal if the principal is unresponsive. (The Second Circuit in the *Stein* appeal had speculated whether that was true; *Verponi* decided the issue expressly.)

One major carve-out to the Agent's otherwise broad authority relates to decisions regarding artificial nutrition and hydration.[10] The Agent is not authorized to make such decisions unless the principal's wishes regarding such procedures are "reasonably known."[11] In determining the principal's wishes in this regard, courts have sometimes applied a "clear and convincing" evidentiary standard, which must be met by the party wishing to withhold or withdraw the artificial nutrition and hydration. The application of the "clear and convincing" standard is subject to debate and is discussed in more detail below.

When making health care decisions on behalf of a principal, the Agent must consult with a licensed physician or other health care worker, and the Agent's decision must be in accordance with the principal's wishes (including any religious and moral beliefs).[12] The Agent has the right to receive all medical information and re-

cords necessary to make his or her decision,[13] but the required consultation need not take place at the hospital or at the same time as the Agent makes the decision.[14] If the principal's wishes are unknown, then a decision (other than one to withdraw or withhold artificial nutrition or hydration) in the principal's best interest will be sufficient.[15]

II. Challenges to and Revocation of the Health Care Agent's Authority

Although lawmakers and the courts have tried to define and limit an Agent's authority as clearly as possible, this has not stopped challenges to an Agent's authority, nor are such challenges likely to cease altogether given the potential ramifications of health care decisions. PHL § 2992 permits certain individuals, including the health care provider and the principal's family members and close friends, to challenge the principal's health care proxy to (a) determine the validity of the health care proxy,[16] (b) remove the Agent on the grounds of unavailability or bad faith or (c) override the Agent's decision on the grounds of bad faith or because the decision was not in accordance with the requirements of PHL §§ 2982(1) and (2).[17]

Several New York cases have addressed the second category of challenges, usually on the grounds of bad faith,[18] and the cases generally provide that mere disputes regarding the principal's religious beliefs are insufficient to challenge the Agent's authority. In *Borenstein v. Simonson*,[19] the principal's sister petitioned for the removal of the principal's daughter as Agent after the Agent refused to allow a percutaneous endoscopic gastrostomy tube (a type of artificial feeding tube sometimes referred to as a "PEG" tube) to be inserted into the principal even though the principal was "committed to traditional or religious Judaism."[20] The court reviewed differing Jewish views on artificial feeding before concluding that no evidence was offered suggesting that the Agent's actions were in bad faith.[21] In a similar case, petitioners argued that the Agent (the principal's wife) should be removed for acting in bad faith and contrary to petitioner's Jewish beliefs by directing that life-sustaining procedures be discontinued, including that the principal's mechanical ventilator be disconnected.[22] The petitioners in that case practiced Orthodox Judaism and asserted that their faith provided that an individual's life should be prolonged using artificial means, but the court determined that the principal did not share the petitioners' beliefs after hearing testimony that the principal did not observe Orthodox Judaism and "wanted to live life to the fullest, not to merely exist"[23] (even though he was brought up in an Orthodox household and wanted his brother to officiate his funeral).[24] The court therefore found no grounds to remove the Agent. In general, once an Agent has been appointed, it has been difficult to prove that the Agent was acting in bad faith.

III. Surrogates Make Health Care Decisions Where No Agent Has Been Appointed

Most individuals fail to appoint an Agent. In cases where there is no Agent under a health care proxy and no guardian, the Family Health Care Decisions Act (FHCDA),[25] enacted in 2010, permits a patient's family members, domestic partner or close friends (a "Surrogate") to make health care decisions upon the patient's incapacity. Prior to the law's enactment, New York law offered very little authority for family members to make health care decisions for incapacitated patients, even if the decision involved consent to a beneficial treatment.[26] Limited protection may have been available under the informed consent statutes,[27] but many health care providers were unwilling to take the risk associated with allowing family members to make such decisions, especially when the decision involved removing life-sustaining treatment.[28] The applicability of the FHCDA with respect to patients with mental disabilities is complex and, in general, the FHCDA does not replace previously enacted rules regarding such patients.[29]

The FHCDA makes it clear that a Surrogate should only be sought as a last resort when no Agent or mental health guardian has been appointed pursuant to other provisions of New York law. [30] The FHCDA lists, in order of priority, the persons who may act as the Surrogate: the patient's guardian appointed by a court pursuant to article 81 of the Mental Hygiene Law who is authorized to make decisions about health care,[31] the patient's spouse or domestic partner, the patient's adult child and so forth.

The FHCDA specifies that "[o]ne person" should be designated as the Surrogate.[32] (Similarly, only one individual at a time may be designated as an Agent under a health care proxy.[33]) If the patient has more than one adult child, then it is presumably the responsibility of the hospital or nursing home to determine which child should be the Surrogate. Any disputes regarding Surrogate appointment, if they cannot be resolved informally, should be resolved by the hospital's ethics review committee.[34] Where disputes regarding the form of treatment arise between the Surrogate and another person lower on the surrogate list, three options are generally available: an informal resolution, review by the ethics review committee or a court order (for which the court will consider whether the Surrogate has fulfilled his or her duties).[35]

The FHCDA also provides a solution for cases where the patient does not have one of the listed persons to act as Surrogate. The hospital must make reasonable efforts to determine whether its patient has a health care agent or a person who can serve as surrogate under PHL § 2994-d. [36] If no such Agent or person is available and the patient lacks capacity to make health care decisions, the hospital must then identify (to the extent reasonably

possible) the patient's wishes and preferences, including his or her religious and moral beliefs, with respect to pending health care decisions. For routine medical treatment, the FHCDA allows the attending physician to make decisions on the patient's behalf. For major medical treatment, the attending physician must seek agreement from another health care professional directly responsible for the patient's care before making the decision. Stricter regulations are provided for decisions to withhold or withdraw life-sustaining procedures (see below).

The extent of the Surrogate's authority is similar to that provided to an Agent appointed in a health care proxy except that the FHCDA imposes a different standard for decisions to withhold or withdraw life-sustaining treatment, and the authority of the Surrogate is limited to making health care decisions in general hospitals and nursing homes.[37] If the patient has already made a decision about the proposed health care (orally or in writing) or about the withdrawal or withholding of life-sustaining treatment (either orally, during hospitalization and in the presence of two witnesses over 18 years of age or in writing), then the Surrogate's consent is not required.[38] If the Surrogate is called upon to make a decision, the decision must be made in accordance with the patient's wishes, including the patient's religious and moral beliefs, or if they are not known, in the best interests of the patient.[39]

IV. Evidentiary Standard for Withholding or Withdrawing Life-Sustaining Procedures

While many health care decisions made by an Agent or Surrogate are relatively non-controversial, decisions regarding life-sustaining procedures tend to give rise to more challenges. Life-sustaining procedures generally include cardiopulmonary resuscitation and mechanical ventilation. Some commentators distinguish artificial nutrition and hydration from the other types of life-sustaining procedures because, unlike air, "[t]he patient does not live in an environment of food, ready for intake… [food] must be supplied, and in this regard ceasing to provide nutrition and hydration takes on more the flavor of denying the patient air, not just assistance in breathing."[40] As a result of this distinction, artificial nutrition and hydration were singled out for special treatment in PHL article 29-C, which provides that the Agent does not have authority to make decisions on artificial nutrition and hydration if the patient's wishes regarding them are not reasonably known and cannot with reasonable diligence be ascertained.

Clear and Convincing Standard

Although several decisions have applied a clear and convincing standard for proving the patient's wishes regarding the withholding or withdrawing of life-sustaining procedures (including artificial nutrition and hydration), the stringency of the standard is still unclear. The seminal case in New York on this issue is *In re O'Connor*[41] (decided before the enactment of PHL article 29-C), in which the court concluded that the record lacked "clear and convincing proof" that the patient had made a "firm and settled commitment, while competent," to decline the type of medical assistance at issue under the circumstances.[42]

The *O'Connor* standard was difficult to meet; despite testimony in the *O'Connor* case indicating that the patient had stated to several witnesses over a period of several years that she did not want to be kept alive using artificial means, the court found such testimony to be insufficient to meet the required standard. The standard has been eroded in subsequent years as lower courts found the requirements to be too stringent.[43] In *In re Christopher*,[44] for example, the court found clear and convincing evidence showing that the patient would not wish a PEG tube to be inserted after distinguishing the circumstances from those in *O'Connor* based on the fact that the patient in *O'Connor* had a gag reflex problem, which prevented her from swallowing, whereas the patient in *In re Christopher* did not.[45]

As noted above, *O'Connor* was decided before the enactment of the health care proxy statute, which does not reference the "clear and convincing" standard. It is therefore unclear whether courts should apply the "clear and convincing" standard when an Agent has been appointed; several New York cases have applied the "clear and convincing" standard when a health care proxy is involved, but the court in *S.I. v. R.S.* believed that the legislature, in passing PHL article 29-C in 1990, replaced the clear and convincing standard of *O'Connor* with a statutory "reasonableness standard" [46] in situations where a health care agent has been designated. (This is because the health care proxy statute refers to the principal's wishes as they are "*reasonably* known" or can be ascertained with "*reasonable* diligence" [emphases added].)

Reasonableness Standard

Unlike the "clear and convincing" standard, the "reasonableness" standard is not one of the classic evidentiary standards of proof (preponderance of the evidence, clear and convincing or beyond a reasonable doubt). One way of viewing this anomaly is to treat the "reasonableness" standard not as an evidentiary standard of proof at all, but instead as the level of certainty with which an *Agent* must know the principal's wishes. It is, arguably, a directive addressed to the Agent rather than to the Court.

The enactment of PHL article 29-C was partly a response to the decision of the U.S. Supreme Court in *Cruzan v. Dir., Mo. Dep't of Health*,[47] which recognized a constitutional right to refuse treatment and suggested that states should allow the appointment of health care agents to prevent a person's wishes from being denied

after the person becomes incompetent simply because he or she failed to provide explicit oral or written instructions.[48] If the New York legislature intended to take up the invitation of the Supreme Court to establish a procedure to avoid disputes over the level of proof of the person's intent, it is unlikely that the legislature intended to require that an Agent produce "clear and convincing" evidence demonstrating that he or she knew the principal's wishes. The statute was also influenced by the 1985 Task Force on Life and Law and the 1988 *O'Connor* decision by the Court of Appeals, and the statute's legislative history has been read to the effect that the legislature intended to relax the clear and convincing standard in those cases where individuals took advantage of the new law to appoint a health care agent.[49]

Similarly, the carve-out in PHL article 29-C for artificial nutrition and hydration should not be governed by the "clear and convincing" standard. This carve-out prevents the Agent from making decisions in the principal's best interests only if the principal's wishes regarding the administration of artificial nutrition and hydration are not reasonably known and cannot with reasonable diligence be ascertained.[50] Nothing in the statutory language or legislative history suggests that a clear and convincing evidentiary standard must be layered on top of the reasonable knowledge requirement when a decision regarding the administration of artificial nutrition and hydration is involved.

This interpretation (whereby the Agent must reasonably know the principal's wishes instead of proving those wishes by clear and convincing evidence) can also be reconciled with the facts of the pre-*S.I.* cases, which applied the clear and convincing standard even when a health care proxy was involved. The pre-*S.I.* cases, either did not specifically apply the clear and convincing standard to the determination of the principal's wishes, or evidence of the principal's wishes was so grossly insufficient as to fail any standard of proof.

In *In re Balich*,[51] the principal stated on her health care proxy that she did not wish to be given tube feedings if she had irreversible brain damage. The court required clear and convincing evidence that the principal had sustained irreversible brain damage but did not require clear and convincing evidence as to the principal's wishes.[52]

In *Borenstein*, [53] the court stated that it was applying the clear and convincing standard (and impliedly rejected the arguments presented here), although the evidence regarding the principal's wishes was so lacking in substance that it would have satisfied neither the clear and convincing standard nor the reasonableness standard. In this case, the principal's health care proxy named her daughter as her Agent but did not provide any indication with respect to her wishes regarding the administration of artificial nutrition and hydration. The Agent also failed to provide any evidence showing that the principal would wish to decline the insertion of a PEG tube to provide nutrition and hydration. Under these circumstances, the court concluded that the principal's "wishes in that regard are not reasonably known and cannot with reasonable diligence be ascertained. There is surely no 'clear and convincing' evidence on this specific issue."[54]

Similarly, the party wishing to remove life-sustaining treatment in *In re Univ. Hosp. of State Univ. of N.Y.*[55] did not present any evidence regarding the patient's wishes to have life-sustaining treatment withdrawn once the court struck from evidence the patient's living will/power of attorney and health care proxy. Thus, the standard of proof made no difference—there was no proof adduced at all.

The FHCDA Standard

The applicability of *S.I.*'s reasonableness standard is uncertain, but the recent passage of the FHCDA may strengthen the *S.I.* court's approach because neither the FHCDA nor the health care proxy statute (both of which were enacted after the *O'Connor* decision) refers to a clear and convincing standard.[56] The legislature certainly could have referred to that evidentiary standard and explained how it was intended to interact with reasonable knowledge, if that was the intent.[57]

Although the FHCDA uses the reasonableness standard for most health care decisions, a different standard must be met when a Surrogate's decision is to withhold or withdraw life-sustaining treatment.[58] The Surrogate must first comply with the requirements of PHL § 2994-d(4) (namely, that the decision be in accordance with the patient's religious and moral beliefs, or if they are not reasonably known and cannot with reasonable diligence be ascertained, in the patient's best interests).[59] If the Surrogate completes that analysis and determines, for example, that the patient wanted to have treatment withheld or withdrawn under the circumstances, that decision cannot be implemented unless one of the following two additional conditions is satisfied.[60] First, the procedures may be withheld or withdrawn if the Surrogate decides that the procedures would be an extraordinary burden to the patient and an attending physician determines, along with an independent physician, that (a) the patient's illness will cause death within six months, whether or not treatment is provided, or (b) the patient is permanently unconscious. Alternatively, the procedures may be withdrawn if the Surrogate decides that the procedures would involve such pain, suffering or other burden as to result in it being inhumane or extraordinarily burdensome and the patient has an irreversible or incurable condition as determined by an attending physician and an independent physician.

Where no Agent or Surrogate is available to make the decision on the patient's behalf, the FHCDA autho-

rizes the withholding or withdrawal if (a) approved by a court or (b) the attending physician, with independent concurrence of a second physician designated by the hospital, determines to a reasonable degree of medical certainty that the life-sustaining treatment is of no medical benefit to the patient and the provision of such treatment would violate accepted medical standards.[61]

Since the FHCDA has been in effect for less than a year, the case law interpreting its standard for withdrawing or withholding life-sustaining treatment is limited. One recent case is *In re Zornow*, in which the children of a devout Catholic patient with no health care proxy disagreed about whether their mother should be provided with artificial nutrition and hydration. The court had previously appointed co-guardians for the patient pursuant to Mental Hygiene Law article 81, and its decision focused on providing guidelines of authority (derived from PHL § 2994-d(5)) for the co-guardians in making end of life decisions for the patient. The court stated that the FHCDA statute changed the presumption when the patient has not indicated his or her wishes regarding life-sustaining treatment from a "presumption of life" to a "presumption of termination."[62] The court then considered the conditions set out in PHL § 2994-d(5) and relied on the position of the Catholic Church (presumptively representing the patient's religious views) on such conditions to reach the conclusion that, except under certain exceptional circumstances such as imminent death, the patient must be provided with food and water even if administered artificially.[63]

The *Zornow* court was not faced with a situation in which the patient's expressed or implied wishes or best interests supported withholding or withdrawing treatment. (In this case, the court found at least an implied wish in favor of artificial nutrition and hydration.) However, if the PHL § 2994-d(4) inquiry had determined that the patient's wishes or best interests were in favor of withholding or withdrawing treatment, treatment nevertheless could not be withheld or withdrawn unless there was also compliance with the stringent additional requirements of PHL § 2994-d(5) discussed above.

The recent cases as well as the enactments of PHL article 29-C and 29-CC demonstrate the erosion of the *O'Connor* "clear and convincing" standard. However, the standard may still be applicable in certain circumstances, such as when determining whether a prior oral or written decision (such as an advance directive) by the patient is sufficiently clear to rely on for treatment decisions without seeking a Surrogate's decision.[64]

V. The Effect of Advance Directives on the Agent's or Surrogate's Authority

Given the need to establish a patient's prior wishes with respect to end of life decisions, some individuals sign advance directives, such as a living will or medical directive, a Do Not Resuscitate (DNR) order or a Medical Orders for Life Sustaining Treatment (MOLST) form, in order to make their wishes clearly known.

A living will or medical directive, which may accompany a health care proxy, sets out the individual's wishes for health care in the event he or she is unable to make health care decisions. While there is no New York statutory authority supporting the use of a living will, its use became widespread after the *O'Connor* decision required "clear and convincing" evidence before life-sustaining treatment could be withdrawn or withheld. If a medical directive constitutes "clear and convincing" evidence, then the expressed wishes regarding life-sustaining treatment can be used to challenge the authority of an Agent if the Agent reaches a contrary decision, or in the absence of an Agent will take precedence over any decision made by a Surrogate pursuant to the FHCDA.[65] Likewise, if the medical directive contains the individual's wishes regarding non-life-sustaining treatment, the statutory duties imposed upon the Surrogate and the Agent generally require him or her to honor those wishes.

When a patient has a cardiac or respiratory arrest, a DNR order will prevent medical personnel from attempting cardiopulmonary resuscitation (CPR). If a patient does not have a DNR, he or she will be presumed to consent to CPR.[66] Before the enactment of the FHCDA, New York law provided for both a statute regulating DNR orders in hospitals and nursing homes and a statute regulating non-hospital DNR orders. The FHCDA repealed the sections relating to DNR orders in hospitals and nursing homes, although DNR orders for residents of mental hygiene facilities and non-hospital DNR orders were preserved. Decisions regarding DNR orders in hospitals and nursing homes must now follow the standards and procedures set out in the FHCDA because a DNR order is viewed as a type of decision to withhold or withdraw life-sustaining treatment.[67] First, the order must be written in the patient's medical record.[68] Second, under constitutional and common law, a patient with capacity can consent to a DNR order.[69] Third, if the patient does not have capacity, his or her Surrogate can consent to a DNR order if the decision is made in accordance with the standards set out in PHL §§ 2994-d(4) and (5). Finally, if a patient does not have a Surrogate, a DNR order can be entered by the attending physician if the decision is made in accordance with the standards set out in PHL § 2994-g(5)(b) for withholding or withdrawing life-sustaining treatment. If, however, a patient without capacity to make health care decisions has an appointed health care Agent, then the Agent will have the authority to consent to a DNR.[70]

A MOLST form is generally completed by the treating physician in conjunction with the patient and is appropriate for patients in long-term care facilities with serious health conditions who want to avoid life-sustaining treatments. A MOLST form can combine both a

hospital DNR and a non-hospital DNR as well as specify other end of life decisions, and the New York Department of Health has approved a MOLST form which can be found on their website.[71] The form is honored in hospitals and nursing homes as well as in non-hospital settings.[72] Unlike a health care proxy, which requires a determination that the patient lacks capacity before becoming effective, the orders on the MOLST form are effective immediately.[73] Consent for a MOLST form can be provided by the patient if the patient has capacity to consent or by an Agent or Surrogate.[74]

The effect of a DNR order or a MOLST form on an Agent's or Surrogate's authority will depend on who consented to the DNR order or the MOLST form. If consent was given by the patient when the patient had capacity, an Agent may not be able to override the expressly stated decision. If the consent was given by an Agent or Surrogate, then the consent may be challenged in the same manner as other decisions made by an Agent or Surrogate.

VI. Inconsistencies in New York's Health Care Law and Proposed Changes

The FHCDA was a much needed addition to New York's health care law, but it has at the same time created some inconsistencies within the health care legal framework. For example, the FHCDA modified the DNR law governing DNRs in hospitals and nursing homes but left the old law in effect for certain mental hygiene facilities. Similarly, the appointment of surrogates under PHL article 29-CC applies only to hospitals and nursing homes. There is no reason why different institutions require different sets of rules, and both the New York City Bar Association Committee on Health Law and the Committee on Bioethical Issues agree that the reach of the FHCDA should be expanded to encompass other institutions.[75] Another inconsistency is the different standards applied to an Agent or a Surrogate making decisions regarding artificial nutrition and hydration. As discussed previously, an Agent may not make decisions about artificial nutrition and hydration if the principal's wishes regarding such treatment are not reasonably known and cannot with reasonable diligence be ascertained.[76] However, a Surrogate appointed pursuant to the FHCDA may still be able to make the decision under these same circumstances if it is in accordance with the principal's best interests (and, if the decision is for withdrawal of treatment, it also satisfies certain other conditions).[77]

New York Assembly Member Richard N. Gottfried has recently proposed legislation that may rectify some of these inconsistencies. The proposed bill would make very limited changes to the FHCDA (amending the FHCDA so that it would also govern decisions in hospices), but the scope of the bill may be expanded further based on modifications suggested by interested parties.[78]

VII. Conclusion

Generally, New York has tried to implement a system whereby an individual's wishes regarding medical treatment at the end of his or her life are adhered to as closely as possible. A patient may choose to appoint an Agent in advance of incapacity, may have a Surrogate appointed and may even attempt to explicitly declare his or her wishes pursuant to an advance medical directive. The legislature and courts, however, have left any decisions open to challenge in order to prevent abuses or misuses of the system.

Endnotes

1. *See Fosmire v. Nicoleau*, 75 N.Y.2d 219, 226, 551 N.Y.S.2d 876 (1990) (following *Schloendorff v. Society of N.Y. Hosp.*, 211 N.Y. 125 (1914) and stating that "[t]he common law of this State established the right of a competent adult to determine the course of his or her own medical treatment").
2. *See* N.Y. Surrogate's Court Procedure Act 1750-b (SCPA).
3. *See* N.Y. Public Health Law § 2981 (PHL).
4. *See* PHL § 2983(1) (requiring that the attending physician make, to a reasonable degree of medical certainty, a determination that the patient lacks capacity to make health care decisions in order for the Agent to act); *see also Stein ex rel. Stein v. Barthelson*, 2011 WL 1332052 at *2 (2d Cir. 2011) (finding that there was no evidence that patient's attending physician had made a written determination of incapacity and speculating that the Agent therefore had no authority to dictate where the patient would be treated). *But see*, *Verponi v. City of N.Y.*, *infra* n. 8 (holding that no determination of incapacity is needed for an unresponsive patient).
5. PHL §§ 2982(1) and (4).
6. *Stein v. Co. of Nassau*, 642 F. Supp.2d 135 (E.D.N.Y. 2009), *rev'd in part on other grounds sub nom. Stein ex rel. Stein v. Barthelson*, 2011 WL 1332052 (2d Cir. 2011).
7. *Stein*, 642 F. Supp.2d at 142.
8. *Verponi v. City of N.Y.*, 2011 WL 1991719 (Sup. Ct., Kings Co. 2011).
9. *See* PHL § 2983.
10. Although the Family Health Care Decisions Act (the "FHCDA") (see PHL art. 29-CC, enacted in 2010) permits a surrogate to make decisions on artificial nutrition and hydration even when the patient's wishes are unknown, the FHCDA did not change the law relating to health care agents. However, where the patient's wishes regarding artificial nutrition and hydration (or in contested cases, other life-sustaining treatments) are unknown, commentators believe that the standards set out in the FHCDA, at PHL § 2994(d)(5), should govern the health care agent's decision, even though the agent's authority derives from PHL art. 29-C rather than art. 29-CC. *See* 1-3 Bender's New York Elder Law § 3.06[7] (2010).
11. PHL § 2982(2).
12. *Id.*
13. PHL § 2982(3).
14. *Stein*, 642 F. Supp.2d at 142 (stating that "the statute imposes no temporal or physical limitation concerning where or when this 'consultation' must take place").
15. PHL § 2982(2).
16. PHL § 2981(1)(b) presumes every adult to be competent to appoint a health care agent, and the burden of proving incompetence is on the challenger.
17. PHL § 2982(1) subjects the Agent's authority to any express limitations set forth in the health care proxy, and PHL § 2982(2) requires that the Agent, when making the decision, consult with

a listed health care worker and that the decision be in accordance with the patient's religious or moral beliefs or if not reasonably known, in accordance with the patient's best interests.

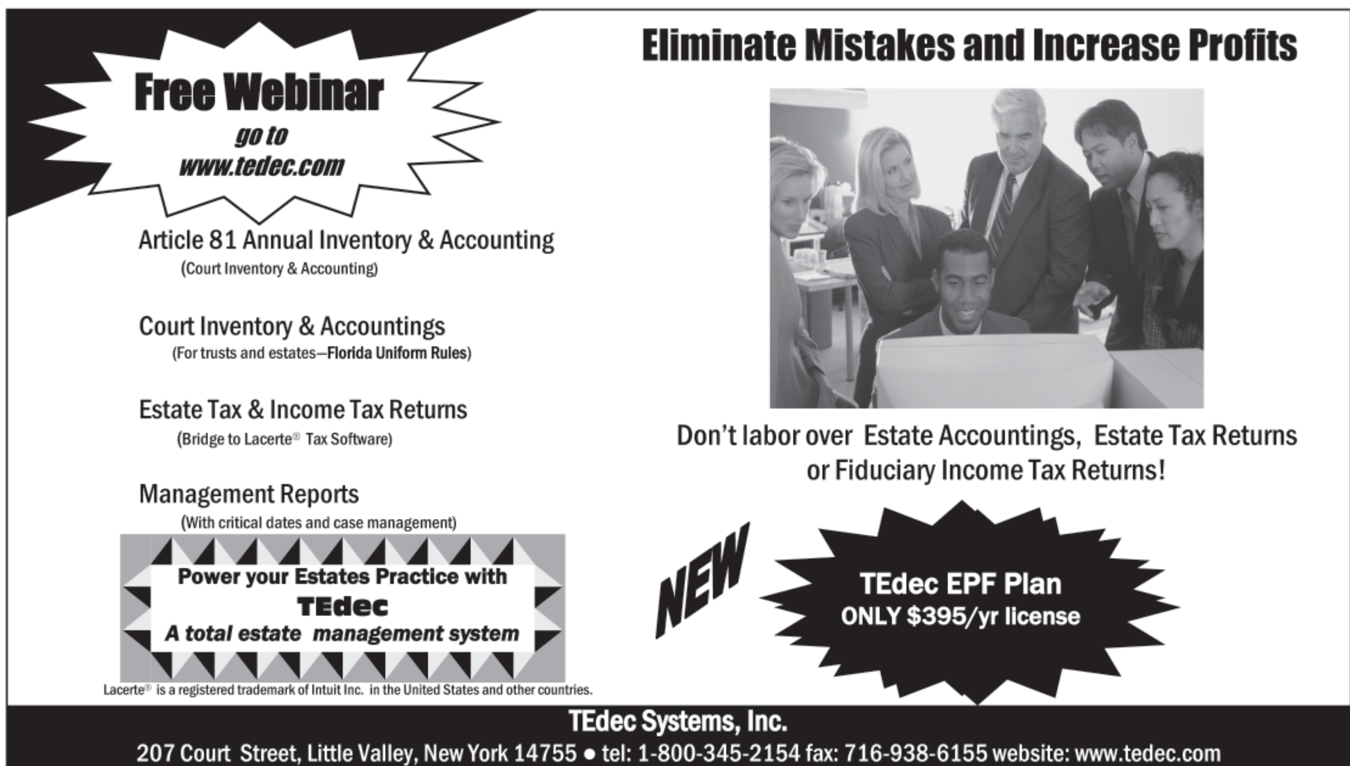
18. Challenges based on unavailability have also been brought. *See e.g., In re Susan Jane G.*, 33 A.D.3d 700, 823 N.Y.S.2d 102 (2nd Dep't 2006) (finding the Agent "no longer reasonably available, willing, and competent to fulfill his obligations under Public Health Law article 29-C"). For challenges based on the validity of a health care proxy and to override an Agent's decision, *see S.I. v. R.S.*, 24 Misc.3d 567, 877 N.Y.S.2d 860 (Sup. Ct., Nassau Co. 2009).
19. 8 Misc.3d 481, 797 N.Y.S.2d 818 (Sup. Ct., Queens Co. 2005).
20. *Borenstein*, 8 Misc.3d at 497.
21. *Id.* at 497-501.
22. *S.I.*, 24 Misc.3d 567.
23. *Id.* at 574.
24. *Id.* at 572.
25. 2010 N.Y. Laws ch. 8, A.7729-D (Gottfried et al.) and S.3164-B (Duane et al.).
26. *See* Robert N. Swidler, *New York's Family Health Care Decisions Act*, N.Y. St. B.J., vol. 82, no. 5, at 18 (June 2010) (stating that "there was no statute or regulation that generally empowered family members to consent to treatment when the patient could not and scant caselaw support for such authority").
27. *See* PHL § 2805-d(4)(c).
28. *See* Swidler, *supra* note 26, at 20.
29. For a more detailed description of who has authority to make health care decisions for patients with mental disabilities, see Robert N. Swidler, *Surrogate Decision-Making for Incapable Adult Patients with Mental Disabilities: A Chart of the Applicable Laws or Regulations* (revised Jan. 12, 2011), <http://www.nysba.org/Content/NavigationMenu/PublicResources/FamilyHealthCareDecisionsActInformationCenter/CompleteChart1-12-11.PDF>.
30. PHL §§ 2994-b(2) and (3) (stating that the attending physician has a duty to make reasonable efforts to determine whether a patient has an appointed health care agent pursuant to a valid health care proxy or has a mental disability such that the Mental Hygiene Law or the Surrogate's Court Procedure Act would apply).
31. N.Y. Mental Hygiene Law § 81.22(a)(8) (MHL) was amended by the FHCDA to permit courts appointing a guardian to grant the guardian the power to act as the patient's Surrogate pursuant to PHL art. 29-CC. Presumably, a guardian appointed after the enactment of the FHCDA must specifically be granted this power in order to be accorded the highest priority pursuant to PHL § 2994-d(1). Prior to the amendment, MHL § 81.22(a)(8) permitted courts to grant the guardian authority to make certain health care decisions. It is likely that an art. 81 guardian appointed prior to the enactment of the FHCDA with the authority to make health care decisions would be accorded the same priority, although the FHCDA is unclear on this point. *See* PHL § 2994-d(1)(a) (giving priority to "[a] guardian authorized to decide about health care pursuant to article eighty-one of the mental hygiene law").
32. PHL § 2994-d(1).
33. PHL § 2981.
34. PHL § 2994-m(2)(b)(iii).
35. *See* FAQs of the New York State Bar Association FHCDA Resource Center (hereinafter FAQs), <http://www.nysba.org/Content/NavigationMenu/PublicResources/FamilyHealthCareDecisionsActInformationCenter/FAQ_HTML.htm> (last accessed February, 2011) (stating that where there are disputes regarding the patient's treatment, "[i]f the higher priority person insists upon the provision of life-sustaining treatment, the hospital cannot discontinue such treatment without a court order" and that "[i]f the surrogate directs the withdrawal or withholding of treatment but a lower priority person insists upon the provision of treatment, the hospital generally should seek judicial review before withdrawing or withholding treatment, although it does not have a legal obligation to do so").
36. PHL § 2994-g.
37. PHL § 2994-b(1). The authority of the Surrogate may be expanded to include hospices. *See* note 79.
38. PHL § 2994-d(3)(a)(ii).
39. PHL § 2994-d(4).
40. *Borenstein*, 8 Misc.3d at 493.
41. 72 N.Y.2d 517, 531 N.E.2d 607 (1988).
42. *Id.* at 522.
43. *See* Bernadette Tuthill, *Want to Terminate Life Support? Not in New York: Time to Give New Yorkers a Choice*, 26 Touro L. Rev. 675 (2010) (stating that "the dissent's prediction that the standard would prove unworkable or inhumane began to come to fruition as lower courts scrambled to distinguish *O'Connor*").
44. 77 Misc.2d 352, 675 N.Y.S.2d 807 (Sup. Ct., Queens Co. 1998).
45. *Id.* at 355.
46. *S.I.*, 24 Misc.3d at 569-71 (stating that "[w]hile it appears to this Court…that the legislature rejected the clear and convincing standard when a health care proxy has been created, some courts are still applying the more stringent standard, thereby continuing the legacy of confusion and legal uncertainty").
47. 497 U.S. 261 (1990).
48. *See Cruzan*, 497 U.S. at 289-290; *Borenstein,* 8 Misc. 3d at 492 (discussing the rationale behind art. 29-C).
49. *S.I.*, 24 Misc.3d at 568-569.
50. PHL § 2982 is structured so that most health care decisions should first be made in accordance with the patient's wishes and if those wishes are not reasonably known and cannot with reasonable diligence be ascertained, then in accordance with the patient's best interests. For decisions regarding the administration of artificial nutrition and hydration, however, the "best interests" alternative is not available; decisions on these matters can be made only if the Agent reasonably knows or with reasonable diligence can ascertain the patient's wishes.
51. 2003 WL 21649907 (N.Y. Sup. Ct., Suffolk Co. 2003).
52. It could be argued that the clear and convincing standard was not applied because the patient's written health care proxy would have satisfied that standard anyway.
53. 8 Misc.3d at 495.
54. *Id.*
55. 194 Misc.2d 372, 377, 754 N.Y.S.2d 153 (Sup. Ct., Onondaga Co. 2002).
56. *See* FAQs (stating that "a key purpose of the FHCDA was to eliminate the clear and convincing standard for clinically appropriate end-of-life decisions. Under the FHCDA, the surrogate must make the decision based on the patient's wishes 'if reasonably known' or else based on the patient's best interests").
57. *See* Report on Legislation by the Committee on Health Law and the Committee on Bioethical Issues (S.3164-B and A.7729-D) (reissued Jan. 2010) (stating that "[u]nder the proposed bill, there is no need for the surrogate to show clear and convincing evidence of the patient's wishes with respect to medical treatment").
58. PHL § 2994-d(5).
59. *See In re Zornow*, 31 Misc.3d 450, 919 N.Y.S.2d 273 (Sup. Ct., Monroe Co. 2010) (in a dispute over whether artificial feeding should be withdrawn, where no health care proxy or advance directive was provided, the court suggested that the religious and moral beliefs of the patient take precedence over the standards required by PHL § 2994-d(5)(a) if the patient's beliefs

are inconsistent with the standards required by the statute, at least if those beliefs favor administration of treatment).

60. PHL § 2994-d(5).
61. PHL § 2994-g(5).
62. *Zornow*, 31 Misc.3d at 455 (stating that "[i]ronically, now when a principal selects a person whom he or she trusts in a health care proxy to make decisions on his or her behalf, the law of that proxy is that, absent an indication to the contrary, that person must provide food and water [citation omitted], while someone designated by statute in whom the patient may have no trust whatsoever, can terminate his or her life earlier than his or her natural death by such deprivation of food and water, despite the principal never having indicated a desire for such earlier termination"). Nevertheless, PHL § 2994-d(5) provides very substantial safeguards against ill-considered withholding or withdrawing of treatment.
63. *Id.* at 456-59.
64. *See* FAQs (stating that "a prior oral or written decision to withdraw or withhold life-sustaining treatment should be sufficiently specific to have met the 'clear and convincing evidence' standard before it may be relied upon without seeking a surrogate decision, inasmuch as the clause was not intended to change pre-FHCDA reliability standards for prior decisions by the patient himself or herself").
65. *Id.*
66. PHL § 2962(1).
67. PHL § 2994-a(19).
68. PHL § 2994-i.
69. *See Fosmire*, 75 N.Y.2d at 226 (stating that "we affirmed the basic right of a competent adult to refuse treatment even when the treatment may be necessary to preserve the person's life"); FAQs (stating that "[a]s a matter of constitutional and common law, it is clear that a patient with capacity can consent to a DNR or DNI order, just as a patient with capacity can direct the withdrawal or withholding of other life-sustaining treatments").
70. PHL § 2962(5).
71. <http://www.health.state.ny.us/professionals/patients/patient_rights/molst/>.
72. *See* PHL art. 29-CCC.
73. 1-3 *Bender's New York Elder Law* § 3.05[5].
74. *See* PHL § 2994-cc.
75. *See* n. 1 of Report on Legislation by the Committee on Health Law and the Committee on Bioethical Issues (S.3164-B and A.7729-D) (reissued Jan. 2010).
76. PHL § 2982(2).
77. *See* PHL § 2994-d(5). However, if the decision is for withdrawal of artificial nutrition or hydration, other conditions may also have to be satisfied. *See* note 53.
78. *See The Proposed Surrogate Decision-Making Improvement Act (SDMIA)* (included in the handout by Russell N. Adler, from Elder Law 2011: The Basics & More, Association of the Bar of the City of New York); *see also* A.7343, 234th N.Y. Leg Sess.; Memorandum in Support with Modifications, Elder Law Section, New York State Bar Association (May 10, 2011).

Jonathan J. Rikoon is a partner at Debevoise & Plimpton LLP and chairs the firm's Trusts and Estates Group. He is a member of the Trusts and Estates Law Section, a Vice-Chair of its Committee on Taxation and former Chair of its Committee on Estate Litigation.

Mordy Serle and Louise D. Yang are associates in the Trusts and Estates Group at Debevoise.



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Fixing Estate Planning Documents

By Carlyn S. McCaffrey

Mistakes happen. Laws change. Circumstances change. Any of these events can cause an estate planning document to no longer accomplish its intended purpose. The current trend toward more complex and frequently changing tax laws and the growing popularity of long-term trusts are likely to increase the number of trust agreements or wills that need some sort of fixing after they have become irrevocable.

Fortunately, as the need for fix-ups has grown, the range of available, user-friendly state law fix-up techniques has also expanded.[1] And the Internal Revenue Service seems to have become more accepting of the products of these techniques. This is the first in a two-part series of articles that will explore the different methods currently available for fixing irrevocable estate planning documents, principally wills and irrevocable trust agreements, and discuss the likely federal tax consequences of using each of the available approaches.

Wills and trusts are creatures of state law, and state law dictates how their terms can be changed after the death of their testatrixes or, in the case of trust agreements, after they have become irrevocable. The general methods available under state law for effecting changes to irrevocable estate planning documents are construction, reformation, amendment and decanting. This article discusses construction and reformation, and the next will discuss amendment and decanting, as well as statutory state law provisions that prevent certain types of trust provisions that are likely to cause unintended tax problems from taking effect.

I. Federal Tax Consequences

Achieving a Desired Tax Result

Once a beneficiary or a group of beneficiaries and their advisors has chosen a state law method for making a change, before implementation they should determine the federal tax consequences of the change and of the method selected for making it. If a particular tax result is an important motivation for making the change, they should determine whether the change will accomplish the tax result sought to be achieved.

There are two principal reasons why changes in the terms of a will after its testatrix has died or changes in the terms of an irrevocable trust agreement may not achieve the desired tax results. The first is the Bosch rule; the second is the completed transaction rule.

The Bosch Rule. Although state law determines the existence of the kinds of property interests and rights that are subject to tax under the federal estate, gift and generation-skipping transfer tax systems,[2] a state court decision as to the existence of such interests and rights in any particular situation will not necessarily be binding on the IRS. The Supreme Court decided in *Commissioner v. Estate of Bosch* that the IRS is entitled to have the Tax Court or another federal court determine the proper result under state law, unless a decision as to that result has been made by the highest state court of last resort.[3] Although the federal court determining the state law result must give proper regard to the relevant rulings of other courts of the state, it has the power to reach a decision contrary to such rulings even if one of such rulings binds the parties to the federal tax controversy.

The Completed Transaction Rule. The completed transaction rule applies to changes made after a taxable event, such as the death of a testatrix or the transfer of property by gift to an irrevocable trust, has already occurred. It operates to prevent a reformation of a will or a reformation or amendment of the trust instrument from being effective retroactively to change the tax consequences under the document as written even if that reformation or amendment is consistent with state law.[4]

The completed transaction rule should not apply to changes effected by construction proceedings. A construction proceeding is not intended to change the terms of the instrument but merely to determine what is meant by those terms. A reform to a trust instrument that permits a settlor to take back all or a portion of her transfer to a trust because of a mistake made in connection with the transfer should also be effective to cause the transfer to have been incomplete for gift tax purposes when made despite the completed transaction rule. In these cases, the incompleteness of the transfer is caused not by the reform itself but by the state law that gives the settlor the right to ask for the reform.[5]

A state court decree construing or changing the terms of an irrevocable trust instrument issued before a taxable event will be binding on the IRS if it is binding on the parties even if the decree is inconsistent with state law. The IRS reached this conclusion in Revenue Ruling 73-142.[6] The Revenue Ruling dealt with the estate tax effectiveness of an erroneous decree that eliminated a settlor's right to appoint herself as trustee of a trust she had created. The power of a settlor to ap-

point herself as trustee of a trust, in the view of the IRS, effectively attributes to her all the powers held by the trustee. In the case of the trust described in the ruling, those powers were sufficient to cause the trust property to be included in the settlor's gross estate. The IRS concluded that the erroneous decree would avoid this result. In the words of the IRS,

> [W]hile the decree would not be binding on the Government as to questions relating to the grantor's power to appoint himself as trustee prior to the date of the decree, it is controlling after such date since the decree, in and of itself, effectively extinguished the power. In other words, while there may have been a question whether the grantor had such power prior to the decree, there is no question that he did not have the power thereafter.

Revenue Ruling 73-142 did not deal with the potentially adverse tax consequences to the settlor of initiating a proceeding in which he lost a tax significant right.

Avoiding Adverse Tax Results

There are a variety of adverse tax consequences that can be caused by changing the terms of an irrevocable trust.

Gift Tax Consequences. If, for example, the change is one that could not be made without the consent of a beneficiary whose interest under the original instrument is reduced, her consent could be treated as a transfer of a property interest. If the beneficiary did not receive adequate and full consideration in money or money's worth for that transfer, the transfer would be treated as a taxable gift.[7] Similarly, if the change is one that results in a settlor's loss of a power over gifted property the retention of which had rendered the gift incomplete, she may have made a taxable gift if the change could not have been made without her consent.

Generation-Skipping Transfer Tax Consequences. If the trust is one that was irrevocable on September 25, 1985, and is therefore protected from the generation-skipping transfer tax,[8] a change could cause the loss of that protection. The IRS has issued more than 500 private letter rulings in which it has taken the position that a change in the quality, value or timing of any powers, beneficial interests, rights or expectancies originally provided for under the terms of a pre-September 26, 1985 irrevocable trust can result in a loss of protection under the effective date rule.[9] Final generation-skipping transfer tax effective date regulations issued on December 20, 2000 describe several types of changes that the IRS has concluded will not result in a loss of effective date protection.[10] (These safe harbors are discussed more fully below). In more than 20 private letter rulings, the IRS has also applied these safe harbors to trusts that were not irrevocable prior to September 26, 1985 but to which GST exemption had been allocated. Throughout this article, such trusts and pre-September 26, 1985 trusts are referred to collectively as "GST protected trusts."

II. Construction

In General

Construction proceedings are used to ask a court to determine a testatrix's or a settlor's intent when the words of her will or trust instrument are ambiguous or when they do not make provision for a particular contingency that has occurred. An ambiguity can be one that is obvious from the text of the document, such as inconsistent identifications of the intended recipient of a particular gift, or one that is apparent only after considering facts not set forth in the instrument, such as the gift of a piece of property never owned by the settlor or testatrix. The former type of ambiguity is generally referred to as a "patent ambiguity"; the latter, as a "latent ambiguity." In a construction proceeding the words actually used in the document are given specific meaning or are used to form the basis for a judicial conclusion as to what the testatrix or settlor actually intended.

The court that is construing a will or trust document tries to do so based on the language of the instrument. If that fails, rules of construction and constructional preferences are available.

Examples of typical statutory rules of construction include anti-lapse statutes, which create a bequest in favor of the issue of certain predeceased legatees where no such provision exists in the original document,[11] and statutes that give a share of a residue that was ineffectively bequeathed to the other residuary legatees.[12]

Examples of typical constructional preferences are listed in § 11.3(c) of the Restatement Third of the Law, Property (Wills & Other Donative Transfers). The basic constructional preference is for a "construction that is more in accord with common intention than other plausible constructions." Other preferences listed include "the construction that is more in accord with the donor's general dispositive plan than other plausible constructions," "the construction that renders the document more effective than other plausible constructions"[13] and "the construction that gives more favorable tax consequences than other plausible constructions."[14]

For example, suppose a settlor transferred property to an inter vivos trust in a transfer that was intended to be complete for gift and estate tax purposes. The trust instrument reflected this intention and stated that all powers granted under the instrument were to be con-

strued in a manner consistent with this intention. But the instrument designated the settlor as a co-trustee and failed to preclude her participation in dispositive decisions. The instrument would be patently ambiguous as to the settlor's power to participate in dispositive decisions. The ambiguity could be resolved by resort to the constructional preference in favor of favorable tax consequences.[15]

If constructional rules and preferences fail to resolve an ambiguity, extrinsic evidence can be used to assist in the construction process, such as the testimony of the drafter as to the identity of particular beneficiaries or particular pieces of property named in the instrument. There is, however, a historic distinction between the use of extrinsic evidence in connection with the construction of wills and in connection with the construction of other donative instruments. Extrinsic evidence has generally been considered in construing donative instruments other than wills.[16] In contrast, courts, in deference to the statutory formalities that are required for the proper execution of a will, have been reluctant to admit extrinsic evidence to assist in the construction of wills, except in the case of latent ambiguities.[17] Over time this reluctance has gradually been eroding.[18] The Restatement Third of the Law, Property (Wills & Other Donative Transfers), in a provision that is perhaps more aspirational than an actual statement of the law as it exists today in a majority of the states, takes the position that ambiguous wills as well as other donative instruments can be construed in accordance with the donor's intention if no rule of constructional preference applies to the ambiguity and if the donor's intention can be established by a preponderance of the evidence.[19]

Since the court is merely deciding the meaning of the document, a construction decree speaks as of the effective date of the document, the date of the testatrix's death in the case of a will or the date a trust becomes irrevocable in the case of an inter vivos trust document. In theory, the document's provisions already have the meaning the court's decision determined. The court's only function is to tell the parties what that meaning is.

Likely Tax Consequences

If the IRS agrees that the construction decree is consistent with state law, the decree will operate retroactively to the date the original instrument became effective. As a result, the tax consequences of the document as of its effective date will be determined as if the decree, or the language provided by the decree, had been in the original instrument. The beneficiaries of the instrument who may have consented to the decree or have failed to object to it will not be deemed to have surrendered rights in a manner that might subject them to the gift tax. If the instrument is protected from the generation-skipping transfer tax, the protection will not be lost.[20] And, if the instrument establishes a charitable remainder trust, charitable remainder trust status will not be lost; nor will the decree be subject to the self-dealing rules.

Effect on the Marital Deduction. In *Estate of Mittleman v. Commissioner*,[21] a judicial construction of Jerome Mittleman's will by the D.C. Circuit saved the marital deduction for his estate. His will left his residuary estate to his wife in trust to provide for her "proper support, maintenance, welfare and comfort." The terms of the will gave the trustees the right to invade corpus for her support and gave the wife a testamentary general power of appointment over the remaining trust assets. The Tax Court concluded that Mrs. Mittleman's trust did not qualify for the marital deduction under I.R.C. § 2056 because, in its view, the will did not give her the right to all of the income from her trust. The D.C. Circuit construed the will to give her that right. The construction was based on the failure of the will to provide a direction to accumulate income, the relatively small size of the estate, which made it likely that the wife would need all the income for support, and the testator's intention, testified to by the drafter, that the trust qualify for the marital deduction.

A judicial construction of another decedent's will freed his wife's share of the residuary estate of the obligation to contribute to his estate taxes. As a result, more property passed to the wife, the marital deduction was larger, and the federal estate taxes were smaller. The text of the will contained no provision that could be construed to relieve the wife of this burden. The court's decision relies entirely on the constructional preference in favor of saving taxes. In the words of the court: "a testator's normal interest would be to maximize deductions and minimize tax liability; in other words, to have all interests passing to the surviving spouse pass without reduction by reason of death taxes."[22] The Tax Court concluded that this construction was consistent with state law and, therefore, was binding on the IRS in *Estate of Sawyer v. Commissioner*.[23]

Effect on Income Tax Liability. I.R.C. §§ 671 and 674 provide that the settlor of a trust will be treated as its owner (and, therefore, taxed on its income) if the trustee has the power to affect the beneficial enjoyment of the trust property unless such power can be exercised only by trustees no more than half of which are related or subordinate parties with respect to the grantor and none of which is the settlor. If a settlor has the power to remove a trustee and replace that trustee with herself, she will be treated as holding the power of the trustee, and the trust income will be taxable to her. Private Letter Ruling 200006027 focused on ambiguous language in a trust agreement which could have been read to give the settlor the right to replace one of the trustees of her trust with herself.[24] The trustee obtained a court order construing the ambiguous language to preclude

the settlor from appointing herself as trustee. The IRS concluded that the court order protected the settlor from being treated as the owner of the trust. The ruling appears to operate retroactively, as is appropriate, since the construction order speaks as of the inception of the trust.

A QSST, which is one of the types of trusts eligible to hold stock in an S corporation, is required to be held for a single beneficiary and to prohibit distributions to any person other than that beneficiary during the beneficiary's life.[25] The trust instrument that was the subject of Private Letter Ruling 9729036 could have been read to permit invasion powers in favor of persons other than the income beneficiary of each trust held under the instrument.[26] The IRS concluded that a construction of the trust instrument to preclude invasions would be consistent with state law and that, if such a construction were obtained, the trusts would be eligible to be treated as QSSTs.

Impact on GST Protected Trusts. Treasury Regulation § 26.2601-1(b)(4)(i)(C) provides that a "judicial construction of a governing instrument to resolve an ambiguity in the terms of the instrument or to correct a scrivener's error will not cause an exempt trust to be subject to the provisions of chapter 13, if—(1) the judicial action involves a bona fide issue; and (2) the construction is consistent with applicable state law that would be applied by the highest court of the state." There are a number of private letter rulings, some issued before and some after the issuance of this regulation on December 20, 2000, that describe several construction results that the IRS has concluded will not result in a loss of effective date protection.

In Private Letter Ruling 9545009,[27] for example, the IRS concluded, before the issuance of the regulation, that a judicial construction of a trust that is consistent with applicable state law will not be considered a modification of the trust for generation-skipping transfer tax purposes. The trustees described in the ruling sought four different construction decrees. The IRS examined each of them in light of its understanding of the applicable Minnesota state law. It decided that two of the requested constructions would be consistent with state law but that the two others would not be. The two consistent constructions would not result in a loss of generation-skipping transfer tax exemption; the two inconsistent constructions would.

The IRS will not always be the best determiner of what state law is, but for trustees who want to ensure continued protection against the generation-skipping transfer tax for their trusts, there is no other option. There is no appeal from an adverse ruling such as the one in Private Letter Ruling 9545009. Although the trustees could proceed with the construction proceeding despite the adverse ruling with the expectation of prevailing in court in the event their trusts' generation-skipping transfer tax exemption was challenged, many trustees would be reluctant to run the risk.

III. Reformation

In General

In practice, the line between construction and reformation is often blurred. The theoretical distinction is clear. A reformation proceeding is one in which a court is faced with unambiguous language that does not accomplish what the court concludes that the settlor intended. The court is not determining what the settlor intended by the words she used but, instead, is attempting to determine what she intended to say or would have intended to say if she had been aware of a particular set of circumstances or laws.

There are three basic kinds of reformations: (i) the reformation that fixes a mistake made by the drafter so that the document reflects the settlor's original intention; (ii) the reformation that rewrites an instrument to achieve a result the court believes the settlor would have wanted to achieve if she had been aware of certain circumstances or laws that were in existence when the instrument was executed; and (iii) the reformation that changes an instrument to achieve a result the court believes the settlor would have wanted to achieve if she had been able to predict a post-execution change in circumstances or laws.

If there is a discrepancy between what the document says and what the settlor intended to say, the discrepancy is generally attributable to a mistake made by the drafter. This kind of mistake is often referred to as a "scrivener's error." A reformation that cures a scrivener's error is similar to a construction because it rewrites the instrument to reflect what the settlor intended as of the effective date of the document. A reformation that rewrites an instrument because of a settlor's mistake of fact or law or because of changes in circumstances or laws does not purport to reflect the settlor's actual intent but merely to approximate what her intent would have been if she had knowledge of the relevant circumstances and laws.

Reformation of inter vivos trust instruments is a familiar remedy used to cure mistakes, either scrivener's mistakes or other mistakes of fact or law.[28] The Restatement Third of the Law, Property (Wills & Other Donative Transfers) § 12.1 describes the remedy as follows:

> A donative document, though unambiguous, may be reformed to conform the text to the donor's intention if it is established by clear and convincing evidence (1) that a mistake of fact or law, whether in expression or inducement, affected

specific terms of the document; and (2) what the donor's intention was. In determining whether these elements have been established by clear and convincing evidence, direct evidence of intention contradicting the plain meaning of the text as well as other evidence of intention may be considered.[29]

One of the more common bases for a judicial finding of mistake is the failure to take advantage of or to qualify for a particular tax benefit. There are a variety of cases that permit the division of generation-skipping trusts into two or more trusts in order to permit one of them to be protected completely from the generation-skipping transfer tax by the allocation of GST exemption to it[30] or to divide a qualified terminable interest property (a "QTIP") trust into two trusts to enable the personal representative to make a reverse QTIP election as to one of them.[31] There are now over 40 states that have a statute permitting trust divisions.[32] The Internal Revenue Code was amended in 2001 to make it clear that severances of trusts can be effective for generation-skipping transfer tax purposes.[33]

Reformation has traditionally not been available for wills, since to change the language of a will would be inconsistent with the statutory formalities generally required for the execution of a will. The distinction between reformation of wills and reformation of inter vivos instruments is gradually disappearing. The rule in the Restatement set forth above applies to wills as well as to inter vivos instruments.[34] A number of states now have statutes that specifically permit the reform or modification of the terms of irrevocable trust agreements and testamentary trusts.[35]

Fixing the Scrivener's Error

The process by which a scrivener's error is fixed is often referred to as a reformation because, in many cases, the fix is accomplished through the addition or replacement of language rather than an interpretation of the existing language. The result to the parties should be the same regardless of which approach is used. If the IRS agrees that the reformation decree is consistent with state law, the decree should operate retroactively to the date the original instrument became effective in the same manner a construction decree operates.

Effect on the Marital Deduction. The decedent described in *Kraus v. Commissioner*[36] died with a trust intended to qualify for the marital deduction. Unfortunately, it did not give his spouse a general power of appointment, a required feature of a marital deduction trust prior to the date of Mr. Kraus' death. The lack of a general power of appointment was the result of a mistaken substitution of a limited power of appointment for a general power made by his attorney when making other amendments to the trust. The estate obtained a reformation decree from the Cook County Circuit Court that reformed the trust instrument to restore the deleted general power. The IRS and, initially, the Tax Court rejected the reformation because, in their view, the estate had not established the mistake with "clear and convincing" evidence, as is required by Illinois law. On remand, however, after reviewing additional evidence corroborating the fact that a mistake had been made, the Tax Court accepted the reformation and permitted the marital deduction.[37]

The estate of the decedent in *Rapp v. Commissioner* did not meet the success that Mr. Kraus' estate did.[38] The trust under Mr. Rapp's will was intended to qualify for the marital deduction but did not require payment of all income to the spouse. The estate obtained an order modifying the trust to give the spouse all income but the order was not a construction order. Instead, the petition, although it stated that the decedent intended the trust to qualify for the marital deduction, relied on a provision of California law that permits a court to modify a trust upon consent of all parties.[39] Unlike the proceeding in Kraus, no evidence was submitted that the decedent intended the trust to qualify for the marital deduction. The Ninth Circuit concluded that the will was not ambiguous, and since there was little evidence that the decedent had intended to create a marital deduction trust, the California court had erroneously reformed the will. As a result, it concluded that the order was not binding on the IRS and that the marital deduction would not be allowed.

Effect on GST Protected Trusts. As indicated above, Treasury Regulation § 26.2601-1(b)(4)(i)(C) provides that "a judicial construction of a governing instrument to resolve an ambiguity in the terms of the instrument or to correct a scrivener's error will not cause an exempt trust to be subject to the provisions of chapter 13, if—(1) the judicial action involves a bona fide issue; and (2) the construction is consistent with applicable state law that would be applied by the highest court of the state." There are a number of private letter rulings, some issued before and some after the issuance of this regulation, that describe several reformations that the IRS has concluded will not result in a loss of effective date protection.

In Private Letter Ruling 200040012, for example, the IRS concluded that a reformation that changed the distribution of trust principal at the end of the trust from a distribution to the then living grandchildren of the settlor to the settlor's child's then living issue, per stirpes would not cause the loss of the trust's effective date protection.[40] The settlor's child submitted an affidavit to the IRS that the settlor's intent was to provide for per stirpital distribution. The IRS concluded that the error cured was a scrivener's error and that state law

would permit reformation under the circumstances in order to conform the instrument to the intent of the settlor. As a result, it concluded that the reformation did not change any powers, beneficial interests, rights or expectancies.[41]

Gift Tax Impact. If a trust beneficiary consents to or fails to object to a change in a trust instrument that could have an adverse impact on her rights under the instrument, she could be treated as making a taxable gift. The interests of the settlor's grandchildren in the trust discussed above, for example, were reduced by the reformation decree. In Private Letter Ruling 200040012 the IRS concludes that no taxable gift occurred for the same reason it preserved the generation-skipping transfer tax exemption—the reformation was based on a scrivener's error and was consistent with state law.

The IRS reached similar results in a series of private letter rulings dealing with reformations that cut back a power of appointment from a general power to a limited power. In Private Letter Ruling 200144018, for example, a trust instrument gave the settlor's surviving spouse, as a trustee of the trust, a power to pay trust principal to herself as she deemed necessary for her "health, welfare and maintenance."[42] The use of the word "welfare" made the power a general rather than a limited power. The IRS concluded that a retroactive modification of the trust instrument to change the phrase "health, welfare and maintenance" to health, education, support and maintenance, would not be treated as a release of a general power of appointment for gift tax purposes because the modification was based on scrivener's error and was consistent with state law.

Impact on Charitable Remainder Trusts. There are several private letter rulings that permit substantial changes to charitable remainder trust instruments to be made without loss of charitable remainder trust status and without triggering the self-dealing rules. In Private Letter Ruling 9804036, for example, the IRS considered a proposed reform to a charitable remainder trust instrument that would change the trust's required payout from the lesser of the trust's income or 8% per year to a fixed 8% per year.[43] The settlor obtained a court order permitting the reformation contingent upon the trust receiving a favorable ruling from the IRS. The reformation order was obtained under a state law that permits reformation of trusts upon approval of a court to correct mistakes. The settlor and the trustee of the trust represented to the IRS that the settlor had intended to provide for an annual payout of 8% regardless of the amount of the trust's income. The attorney who drafted the trust instrument was undergoing cancer treatment at the time and admitted to making a mistake in the drafting process. The IRS concluded that the reformation would not violate I.R.C. § 664 and would not be treated as an act of self-dealing. The IRS's reasoning, which gives some indication as to the kind of support it looks for before issuing rulings of this kind, is set forth below:

> Ordinarily, we would consider a charitable remainder trust's reformation of its payment provision to be an act of self-dealing under section 4941(d)(1)(E) of the Code. However, under the circumstances presented in this case, we find no act of self-dealing, since we are satisfied that the signatory parties to the Trust Instrument never intended to create a NIMCRUT payment method trust in the first place. A key fact in our consideration is that Trust has been consistently administered using the Fixed Percentage method. Another is that the payment provision error was discovered, and action to correct the error was taken, in a relatively short period of time after Trust was created. Another is E's sworn admission of a drafting mistake. Another is the lack of evidence that A or other income beneficiaries are reducing their own taxes or using the benefit of hindsight in making the change to the Fixed Percentage payment method.

Tax Consequences of Existence of Right to Reform. In some cases, the fact that a scrivener's error has occurred will give a settlor the right to revoke her transfer. The existence of this revocation right will make the transfer incomplete for gift tax purposes. If the settlor obtains a reformation order directing the return of the property to her, the order will merely confirm a preexisting right. As a result, the revocability should be effective for gift tax purposes despite the completed transaction rule discussed above.

In *Dodge v. United States*,[44] *Dodge v. Commissioner*[45] and *Touche v. Commissioner*,[46] the courts confirmed that the taxpayers' gifts of real estate were revocable to the extent that their deeds conveyed more than they had intended to convey. As a result, in the two *Dodge* cases, the taxpayers, whose gifts had been made to charity, were able to obtain an income tax charitable deduction in a subsequent year for a gift of a portion of the property that their earlier deeds had covered. And in the *Touche* case, the taxpayer was relieved of gift tax liability for the excess gifts.

Reformation to Correct a Mistake in Facts or Laws

If the IRS agrees that the reformation decree is consistent with applicable state law and that it can be

made without the consent of beneficiaries whose rights are reduced, the reformation decree should not cause adverse gift tax consequences and should not cause a charitable remainder trust to lose charitable remainder trust status or to attract self-dealing taxes. If the tax law specifically recognizes the efficacy of reformations, it may operate retroactively to secure certain tax benefits that would not have been available in the absence of the reformation. It may, however, cause a trust to lose generation-skipping transfer tax effective date protection.

Reformation or Rescission—Retroactive Gift Tax Relief. The taxpayer in *Berger v. United States* created irrevocable trusts and transferred most of his assets to them because of a mistaken belief that the transfer was required in order to comply with the federal government's conflict of interest rules applicable to those holding high level government positions.[47] When Mr. Berger discovered he was not going to receive an offer of employment by the federal government and that the transfer to an irrevocable trust would not have been necessary even if he had received and accepted such an offer, he obtained a court order converting his trusts from irrevocable to revocable. He then sought a refund from the IRS for gift taxes paid on his transfers to the trusts. Because Pennsylvania law permits the revocation of a gratuitous transfer into trust that was made as a result of the transferor's mistake of fact or law, the District Court deciding the refund claim decided that the trust was revocable and that Mr. Berger was entitled to a refund.

Each of the taxpayer's parents in *Breakiron v. Gudonis* created a qualified personal residence trust with his or her respective one-half undivided interest in property.[48] Upon expiration of the ten year term provided for in the trust agreements, if the settlor of the trust was living at the time, the property would pass to the settlor's two children who would then hold the property together as tenants-in-common. The taxpayer attempted to disclaim his interest in the property so that the entire property would be held by his sister. In order to avoid the taxpayer being deemed to have received the property and then transferred it to his sister as a gift, the taxpayer needed to effect "qualified disclaimers" of the property pursuant to I.R.C. § 2518. The taxpayer's disclaimers, however, which were executed (upon the advice of counsel) within nine months of the trusts' termination rather than within nine months of the trusts' creation, were untimely and thus not valid qualified disclaimers.[49]

The taxpayer sought rescission of the disclaimers by claiming he would not have effected them had he known he would have been subject to gift tax liability.[50] The Massachusetts district court found that the taxpayer was entitled to rescission because under Massachusetts state law a written instrument may be rescinded on the basis of mistake, and it was clear to the court that the taxpayer's intention was inconsistent with the disclaimers. As a result, the court further held that because the disclaimers were rescinded, it was as if they were never executed, and thus, there were no transfers by the taxpayer to give rise to the contested gift tax liability.

Effect on GST Protected Trusts. Treasury Regulation § 26.2601-1(b)(4)(i)(C), which is discussed above, will not serve to protect a GST protected trust from loss of its effective date protection if it is reformed to correct mistakes other than scrivener's errors. This provision of the regulations is limited to judicial construction of a trust instrument to either resolve an ambiguity or to correct a scrivener's error. The settlor's mistake as to law or fact does not constitute a scrivener's error.

The only source of protection for this type of reformation is found in Treasury Regulation § 26.2601-1(b)(4)(i)(D). This provision protects any modification to a protected trust so long as the modification is valid under state law, does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation than those who held the interest before the modification and does not extend the time for vesting of any beneficial interest in the trust beyond the time originally provided in the trust instrument.

Fixing Faulty Charitable Remainder Trusts. The Internal Revenue Code permits instruments that create charitable remainder trusts that do not comply with all of the technical requirements set forth in the Code to be reformed to bring them into compliance.[51] If the reformation is a qualified reformation within the meaning of the Code, it will operate retroactively to allow a charitable deduction as of the creation of the trust.

In order to have a qualified reformation, there must first be a change in the governing instrument by "reformation, amendment, construction or otherwise." If the instrument is not ambiguous, if it does not by its terms permit an amendment and if state law does not permit amendment, a reformation proceeding would seem to be the only route to accomplishing compliance.

Starting in 1974 with the *Stalp* decision, New York State has developed a body of case law permitting this type of reformation.[52] There are few other reported cases reaching the same conclusion in other states,[53] but over 30 states permit such reformation by statute.[54]

Fixing Faulty Qualified Domestic Trusts. Bequests to non-citizen spouses are eligible for the marital deduction only if the bequest is made to a qualified domestic trust (a "QDOT"), the technical requirements for which are spelled out in I.R.C. § 2056A and its regulations. Treasury Regulation § 20.2056A-4(a)(2) permits non-qualifying trusts to qualify by means of a reformation

proceeding commenced on or before the due date for the decedent's estate tax return.

As is the case with charitable remainder trust reformations, the reformation must be permissible under state law. New York State, following its cases in the charitable remainder trust area, has allowed reformations to reform ordinary marital trusts into QDOTs.[55]

Reformation Because of Changes in Facts or Laws

The tax consequences of this type of reformation should be the same as the tax consequences of a reformation for mistake as to existing facts or laws. If the IRS agrees that the reformation decree is consistent with applicable state law and that it can be made without the consent of beneficiaries whose rights are reduced, the reformation decree should not cause adverse gift tax consequences and should not cause a charitable remainder trust to lose charitable remainder trust status or to attract self-dealing taxes. If the tax law specifically recognizes the efficacy of reformations, it may operate retroactively to secure certain tax benefits that would not have been available in the absence of the reformation. It may, however, cause a trust to lose generation-skipping transfer tax effective date protection.

The examples discussed above in connection with reformations to achieve a result the settlor would have wanted to achieve if she had been aware of certain facts or laws should apply to this type of reformation as well.

Endnotes

1. *See generally,* Unif. Trust Code, §§ 410–417 (amended 2005); Restatement Third, Property (Wills & Other Donative Transfers) Division IV (2003); F. Ladson Boyle, *When It's Broke—Fix It: Reforming Irrevocable Trusts to Change Tax Consequences*, 53 Tax Law 821 (2000); Ronald Chester, *Modification and Termination of Trusts in the 21st Century: The Uniform Trust Code Leads a Quiet Revolution*, 35 Real Prop., Prob. & Tr. J. 698 (Winter 2001); Mary Louise Fellows, *In Search of Donative Intent*, 73 Iowa L. Rev. 611 (1988); Joseph W. de Furia, Jr., *Mistakes in Wills Resulting From Scriveners' Errors; The Argument for Reformation*, 40 Cath. U. L. Rev. 1 (1990); Richard F. Storrow, *Judicial Discretion and the Disappearing Distinction Between Will Interpretation and Construction*, 56 Case W. Res. 65 (2005); Clifton B. Kruse, Jr., *Reformation of Wills: The Implication of Restatement (Third) of the Law of Property (Donative Transfers) on Flawed but Unambiguous Testaments*, 25 ACTEC Notes 299 (2000); John H. Langbein and Lawrence W. Waggoner, *Reformation of Wills on the Ground of Mistake: Change of Direction in American Law?*, 130 U. Pa. L. Rev. 521 (1982); Marilyn G. Ordover & Charles F. Gibbs, *Correcting Mistakes in Wills and Trusts*, N.Y. Law J. (August 6, 1998) 3; James L. Robertson, *Essays: Myth and Reality—or, Is it "Perception and Taste"?—in the Reading of Donative Documents*, 61 Fordham L. Rev. 1045 (1993); Barry F. Spivey, *Completed Transaction, Qualified Reformation and Bosch: When Does the IRS Care About State Law of Trust Reformation?,* ACTEC Notes (Spring 2001); William R. Culp, Jr. & Briani Bennett Mellen, *Trust Decanting: An Overview and Introduction to Creative Planning Opportunities*, 45 Real Prop., Prob. & Tr. J. 1 (Spring 2010).
2. *Helvering v. Stuart*, 317 U.S. 154 (1942); *Morgan v. Comm'r*, 309 U.S. 78 (1940); *Blair v. Comm'r*, 300 U.S. 5 (1937).
3. *Comm'r v. Estate of Bosch*, 387 U.S. 456 (1967). The IRS takes the position that a decree by the highest state court will not be binding on the IRS unless it actually determines property rights. As a result, for example, a post-death determination by the highest state court that a decedent did not have a general power of appointment during her life would not be binding on the IRS since it would not have any actual effect on anyone's property rights. G.C.M. 39183 (March 6, 1984). A well-reasoned opinion could, however, be evidence of what the state law is.
4. *See, e.g., Van Den Wymelenberg v. United States*, 397 F.2d 443 (7th Cir. 1968), *cert. denied* 393 U.S. 953 (1968); *American Nurseryman Publishing Company v. Comm'r*, 75 T.C. 271 (1980), *aff'd without published opinion*, 673 F.2d 1333 (7th Cir. 1982); *M. T. Straight Trust v. Comm'r*, 24 T.C. 69 (1955), *aff'd*, 245 F.2d 327 (8th Cir. 1957). The IRS has, however, allowed retroactive changes that operate to increase a taxpayer's tax liability. See, for example, PLR 200002029 (October 14, 1999), in which the IRS permitted the reformation of a charitable remainder trust to allow the remainder to be passed to a private, rather than a public, foundation, on condition that the taxpayer file an amended tax return for the year of her gift to the charitable remainder trust, reducing the amount of her charitable contribution deduction.
5. *See, e.g., Dodge v. United States*, 413 F.2d 1239 (5th Cir. 1969); *Berger v. United States*, 487 F. Supp. 49 (W.D. Pa., 1980); *Touche v. Comm'r*, 58 T.C. 565 (1972), *acq.* 1972-2 C.B. 3; *Dodge v. Comm'r*, T.C. Memo. 1968-238.
6. Rev. Rul. 73-142, 1973-1 C.B. 405.
7. IRC §§ 2511 and 2512. References to "IRC §" refer to sections of the Internal Revenue Code of 1986, as amended, or to corresponding sections of the Internal Revenue Code of 1954, as amended.
8. Tax Reform Act of 1986 § 1433(a); Treas. Reg. § 26.2601-1(b)(1)(i). A testamentary trust will be protected from the generation-skipping transfer tax if the will it is held under was executed before October 22, 1986 and the decedent died before January 1, 1987. Treas. Reg. § 26.2601-1(b)(2)(i).
9. The IRS first adopted this position in PLR 8851017 (September 22, 1988).
10. Treas. Reg. § 26.2601-1(b)(4). The text of the regulations makes it clear that the IRS limited the scope of the regulations to the issue of the loss of effective date protection. It states that the regulation does not apply "in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of IRC § 1001."
11. *E.g.*, N.Y. Estates, Powers & Trusts Law 3-3.3 (EPTL).
12. *E.g.*, N.J. Stat. Ann. § 3B:3-37; EPTL 3-3.4.
13. *E.g.*, *In re Englis' Will*, 141 N.E. 2d 556 (N.Y. 1957). *See also* de Furia, *supra* note 1, at 113–127; Langbein & Waggoner, *supra* note 1, at 538–541.
14. *E.g.*, *Putnam v. Putnam*, 316 N.E. 2d 729, 737 (Mass. 1974); *Gesner v. Roberts*, 225 A.2d 697 (N.J. 1967); *In re Estate of Lepore*, 492 N.Y.S.2d 689 (Kings Co. Surr. Ct. 1985); *Estate of Mittleman v. Commissioner*, 522 F. 2d 132 (D.C. Cir. 1975); *Sawyer v. Sawyer*, 374 N.E. 2d 166 (Ohio 1977), accepted as controlling for tax purposes in *Estate of Sawyer v. Comm'r*, 73 T.C. 1 (1979).
15. This type of drafting error will not cause a gift or estate tax problem for transfers made after 1996 if the transfer is adequately disclosed as a complete gift on a gift tax return. Treas. Reg. § 301.6501(c)(f)(5).
16. *See, e.g., Berman v. Sandler*, 399 N.E. 2d 17 (Mass. 1980) (insertion into irrevocable trust instrument of missing phrase based on extrinsic evidence); *Irish v. Irish*, 65 A.2d 345 (Pa. 1945) (insertion

into irrevocable trust instrument of a missing provision based on extrinsic evidence); *Brinker v. Wobaco Trust Ltd.*, 610 S.W.2d 160 (Tex. Civ. App. 1980) (court permitted extrinsic evidence to show that a reference to settlor's issue was meant to be limited to his issue with his first wife).

17. For a general discussion of this issue, see Langbein & Waggoner, *supra* note 1.
18. *See, e.g., Taff v. Aulman*, 133 Cal Rptr. 737 (Cal. Ct. App. 1976) (extrinsic evidence admitted to show that testatrix intended her estate to pass to her family rather than, as provided in her will, to her "heirs," a term that under California law at the time included her deceased husband's family because her estate included community property); *Erickson v. Erickson*, 716 A.2d 92 (Conn. 1998) (extrinsic evidence permitted to create provision validating will despite testator's marriage after execution); *Engle v. Siegel*, 377 A.2d 892 (N.J. 1977) (extrinsic evidence permitted to overcome the statutory constructional rule in favor of surviving residuary legatee).
19. Restatement Third, *supra* note 1, § 11.2(a).
20. Treas. Reg. § 26.2601-1(b)(4)(i)(C).
21. *Estate of Mittleman v. Comm'r*, 522 F.2d 132 (D.C. Cir. 1975).
22. *Id.* at 168.
23. *Sawyer v. Commissioner*, 73 T.C. 1 (1979). *See also* PLR 2000450004 (June 30, 2000); PLR 9834027 (May 26, 1998).
24. PLR 200006027 (November 9, 1999).
25. IRC § 1361(d).
26. PLR 9729036 (April 23, 1997). *See also* PLR 9729037 (April 23, 1997); PLR 9729038 (April 23, 1997).
27. PLR 9545009 (August 11, 1995). Similar results were reached in PLR 200123012 (March 2, 2001), PLR 200123013 (March 2, 2001), PLR 200123014 (March 2, 2001), PLR 200116031 (January 19, 2001), PLR 200036013 (May 30, 2000), PLR 200036008 (May 3, 2000), PLR 200006027 (November 9, 1999), PLR 199907008 (November 13, 1998) and PLR 9729038 (April 23, 1997).
28. Langbein & Waggoner, *supra* note 1.
29. Restatement Third, *supra* note 1, § 12.1.
30. *See, e.g., Matter of Choate*, 533 N.Y.S.2d 272 (N.Y. Co. Surr. Ct. 1988).
31. *See, e.g., Matter of Branigan*, 609 A.2d 431 (N.J. 1992).
32. *See, e.g.*, 760 Ill. Comp. Stat. 5/4.25; EPTL 7-1.13; Tex. Prop. Code Ann. § 112.057; S.D. Codified Laws § 55-3-29; Uniform Trust Code § 417. See the Restatement Third, *supra* note 1, § 12.2, and Boyle, *supra* note 1, n.52 and 53, for a list of other state statutes permitting trust divisions.
33. IRC § 2642(a)(3).
34. *See also* Unif. Trust Code § 415: "The court may reform the terms of a trust, even if unambiguous, to conform the terms to the settlor's intention if it is proved by clear and convincing evidence that both the settlor's intent and the terms of the trust were affected by a mistake of fact or law, whether in expression or inducement."
35. *See, e.g.,* Mont. Code Ann. § 72-33-413; Alaska Stat. §§ 13.36.350, 13.36.345, 13.36.355; S.D. Codified Laws § 55-3-28; Fla. Stat. §§ 737.04113, 737.04115, 737.04116.
36. *Estate of Kraus v. Comm'r*, 875 F.2d 597 (7th Cir. 1989), *aff'g in part and rev'g and remanding in part* T.C. Memo. 1988-154.
37. *Estate of Kraus v. Comm'r*, T.C. Memo 1990-339.
38. *Rapp v. Comm'r*, 140 F.3d 1211 (9th Cir. 1998).
39. Cal. Prob. Code § 15403.
40. PLR 200040012 (June 29, 2000).
41. Similar results were reached in PLR 200201020 (October 2, 2001), PLR 200201017 (October 2, 2001), PLR 200147028 (August 9, 2001), PLR 200143019 (July 27, 2001) and PLR 199942016 (July 22, 1999).
42. PLR 200144018 (August 3, 2001).
43. PLR 9804036 (October 24, 1997). Similarly, the IRS permitted reformations based on scriveners' errors to permit the charitable remainder to be paid to a private, rather than a public, foundation in PLR 200002029 (October 14, 1999), to redefine income to include post-contribution capital gain in PLR 9833010 (May 14, 1998) and to change the required payout from the lesser of income or 7% of the trust value to a flat 7% in PLR 9822041 (March 2, 1998).
44. *Dodge v. United States*, 413 F.2d 1239 (5th Cir. 1969).
45. *Dodge v. Comm'r*, T.C. Memo 1968-238.
46. *Touche v. Comm'r*, 58 T.C. 565 (1972).
47. *Berger v. United States*, 46 A.F.T.R.2d 6146 (W.D. Pa. 1980).
48. *Breakiron v. Gudonis*, 2010 U.S. Dist. LEXIS 80888 (Mass. Dist. Ct. 2010).
49. *See* IRC § 2518(b)(2) and Treas. Reg. § 25.2518-2(c)(3)(i).
50. Instead taxpayer claimed he would have transferred the property to his sister by creating a new QPRT with her as the beneficiary.
51. IRC §§ 170(f)(7), 2522(c)(4), and 2055(e)(3).
52. *In re Stalp*, 359 N.Y.S.2d 913 (N.Y. Co. Surr. Ct. 1974). *See also In re Glick*, 537 N.Y.S.2d 984 (N.Y. Co. Surr. Ct. 1989); *In re Kander*, 454 N.Y.S.2d 229 (N.Y. Co. Surr. Ct. 1982); *In re Rayvid*, 388 N.Y.S.2d 211 (Queens Co. Surr. Ct. 1976).
53. *See In re Estate of Burdon-Muller*, 456 A.2d 1266 (Me. 1983); *Cochran Estate*, 7 Pa. D. & C.3d 359 (Pa. 1978).
54. See VA. Code Ann. § 55-554.18, Colo. Rev. Stat. § 15-1-1002, D.C. Code Ann. § 21-1801, 760 Ill. Stat. 60/1, N.J. Rev. Stat. Ann. §§ 3B:11-8 to -15, Tex. Prop. Code Ann. §§ 112.055 and 122.056 and the other statutes referred to in Restatement Third, *supra* note 1, § 12.2.
55. *See, e.g.*, *In re Thor* (N.Y. Law J., November 29, 1980, at 29, col. 6); *In re Feldman* (N.Y. Law J., October 23, 1989); *In re Nangle* (N.Y. Law J., August 15, 1989).

Carlyn S. McCaffrey is a partner of McDermott Will & Emery LLP and is co-head of the private client practice in the firm's New York office. She focuses her practice on tax and estate planning for high net worth individuals. She is a member of the Tax Section of the New York State Bar Association and the former co-chair of the Section's Estates and Trusts Committee.

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Managing Not-for-Profit Funds: What Every Practitioner Should Know About NYPMIFA

By Michael J. Cooney

Following the vast majority of the jurisdictions in the United States, New York adopted its version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA)—known as the New York Prudent Management of Institutional Funds Act or "NYPMIFA"—on September 17, 2010. Guidance from the Office of the Attorney General's Charities Bureau was released on March 17, 2011, providing vital guidance on the application of the statute.[1] Anyone representing a not-for-profit institution incorporated or chartered in the state, or a donor to any such institution, should be familiar with the statute and the aspects that make NYPMIFA unique.

NYPMIFA applies to "institutional funds," which are funds held by not-for-profit corporations organized under the New York Not-for-Profit Corporation Law (N-PCL) or by charitable trusts whose trustees are New York not-for-profit corporations.[2] They include "endowment funds," which are institutional funds subject to restrictions imposed by the donor as to the amount that can be spent on a current basis.[3] The best publicized aspect of the statute, adopted as Article 5-A of the N-PCL, is the liberalization of an institution's ability to spend from newer endowment funds that have not yet experienced positive investment returns. The statute, however, affects many different parts of the charitable institution, and so should be considered at many levels—including the development office, finance committee, investment committee and even the governing Board. The effective date of the statute was its date of adoption, so entities need to be in compliance currently.

Practitioners representing not-for-profit corporations will want to review the following areas: solicitation and restriction (including gift acceptance policies and standard gift acceptance forms); investment and delegation of investment management (and the statute's impact on investment policies, investment manager agreements and investment committee minutes); restricted fund reporting and expenditure (and the impact on internal accounting systems, establishment of spending rates and Board/committee reporting); and donor relations (including the required notice to existing, available endowment donors). Those representing donors will need to be familiar with many of these same elements but should also understand them from the charity's perspective.

NYPMIFA also can affect an institution's accounting presentation and, therefore, its compliance with financial ratios and bond or debt covenants. This impact, while very real, is an outcome of accounting rules, not legal principles. There may be disagreement with respect to NYPMIFA when viewed through the lenses of each of these disciplines, and organizations must understand and manage the effects of each.

I. Dipping into Underwater Endowments

Some History

Prior to the enactment of the Uniform Management of Institutional Funds Act (UMIFA) in New York in the 1970s, institutions had an incentive to invest endowments for current return in order to meet their spending needs, as well as to preserve capital so as to honor the endowment restriction imposed by donors. This resulted in a heavy concentration in investments with fixed returns such as bonds and compromised the ability of institutions to invest endowment funds in equities and other assets that over time would provide a higher total return in the form of both current income and appreciation.

The adoption of UMIFA allowed charitable institutions to recharacterize certain gains as income currently available for expenditure. This was usually accomplished by the governing Board (or a Board committee) appropriating for expenditure a stated percentage of the total value of a fund on a given date, which was typically averaged over the most recent 12 or 20 quarters to smooth the impact of market changes. There then developed a number of variations on this theme of "total return" spending and investment, which had the effect of driving higher investment returns, diversifying portfolios and making returns more predictable and thus more manageable.

An endowment fund could be thought of as a series of layers, with the bottom layer being the historic dollar value (or HDV)—the amount originally gifted by the donor—which under the law could not be spent under any circumstances. Newer endowment funds, which had not yet enjoyed capital growth given the recent market drop, were generating only limited amounts of expendable income (i.e., interest, dividends and so on), with no capital gains to support charitable goals. Institutions were free to contact available donors and ask for relief from spending restrictions, as well as to seek court relief in appropriate cases.

With the adoption of NYPMIFA, the governing Board is subject to a general standard of prudence in spending from an endowment fund, subject to the specific standards set forth in the statute, allowing invasion of the historic dollar value.[4]

While many charities will welcome this flexibility, governing Boards are still required to balance historic market performance and the need for current income against inflation, preservation of capital and a number of other factors. Organizations may elect not to exercise this new ability to invade endowment corpus, or they may still decide to preserve some amount of HDV on a fund-by-fund basis, regardless of what their spending formula may otherwise allow. Donors, too, will want to consider whether they wish to restrict their endowed or other use-restricted gifts through explicit language in the gift agreement, a practice specifically contemplated by NYPMIFA. The new statute thus does not so much do away with HDV (despite elimination of the concept from the law) as change the way in which fiduciaries consider HDV in exercising their new powers.

The Donor Notice Requirement

Other jurisdictions enacting UPMIFA did not see the need to provide special notice to prior endowment donors about the change in the law concerning access to historic dollar value. As under the predecessor UMIFA statute, the statute simply applies retroactively to existing donor funds, thus avoiding the need for institutions to account separately for assets received before a certain date and manage them accordingly.

New York has an additional requirement, however, intended to provide donors of endowment funds existing on September 17, 2010, with the ability to prevent spending of the original funding value of their gifts. New York institutions are thus faced with the prospect of having some of their existing endowment funds subject to the new spending rules, while other funds may still be subject to the prohibition against expenditure of HDV.

The notice requirement in the statute, set forth at N-PCL § 553(e)(1), is unequivocal in its application, a point emphasized by the Charities Bureau in its recent guidance (the "Guidance"). Before an institution appropriates from a endowment fund under N-PCL § 553(a), it must give the donors to the fund, if available, 90 days notice of their right to opt out of the new spending rule.

This aspect of NYPMIFA may be broader than the drafters of the statute realized. The notice requirement in the statute does not distinguish between funds that are "underwater"—i.e., currently below historic dollar value—and other funds with appreciation that could have been spent under the old law. Because the power to appropriate unrealized gains for expenditure has been repealed by the new law, these amounts cannot be spent without notice to donors, even absent any intention to appropriate the HDV. In addition, it was less than clear when NYPMIFA first went into effect whether the "first time" requirement pertains to the establishment of the spending rate by the Board (or investment committee) post-enactment or the actual spending from endowment funds. The Guidance clarifies that it is the fiduciary decision to appropriate which requires notices to be sent, although it does not require responses necessarily to be received. After notice is sent, a Board may appropriate income and net appreciation in excess of HDV during the 90-day notice period as long as it is prudent to do so under NYPMIFA.[5]

Accordingly, the first time after September 17, 2010, that an institution's Board appropriates funds for expenditure, it must be sure that the statutory notice under N-PCL § 553(e)(1) has been provided to available donors. The organization's auditors may inquire on this point.

The statute does not specifically address how the notice requirement applies to multiple donor endowments, such as class funds, memorial funds and the like. The Guidance expresses the view that institutions are required to send the notice to "all available donors of endowment gifts who executed the gift instrument before September 17, 2010, unless a statutory exception applies."[6] The statute and the Guidance thus require the institution to look closely at the circumstances of each multiple donor endowment and establish whether indeed notice is required to each contributor. For example, both the availability of the donor and the institutional endowment solicitation exception[7] should be closely considered.

The statute specifically requires that the language in the notice be in "substantially" the form set forth in N-PCL § 553(e)(1). That language may be confusing and perhaps even misleading to the vast majority of endowment donors, who no doubt are unfamiliar with the arcane ***patois*** of endowment spending. Thus, the development office, working together with the finance office and legal counsel, will need to settle on a notice that is sufficient under the law. Donor responses—especially those precluding the full use of the appropriation power—will need to be recorded in writing and incorporated into the institution's fund management.

The Charities Bureau in its Guidance has spoken to the steps to be taken to determine whether a donor is "available." In particular, where the donor's current address is unknown, the institution must make reasonable efforts to find the donor, including Internet searches and contacting known associates of the donor, such as an attorney who represented the donor when the gift was made.[8] Further, the Charities Bureau emphasizes than an institution should maintain records document-

ing the efforts made to locate donors, even if those efforts ultimately do not succeed in making contact.

II. Development Office

NYPMIFA is not generally perceived as a statute affecting the institution's fundraising function, but the special notice requirement for available donors to existing endowment funds obviously does so. There are several other provisions in the law that demand immediate attention from development officers to assure that the organization is protecting itself properly.

Proper Classification of Gift Restrictions

A necessary starting point for any analysis of donor-restricted funds is a proper legal classification of the assets as they are accepted by the institution. For example, to constitute a true endowment under New York law, the restriction must arise from a clearly expressed donor limitation. A "Board-restricted endowment" or "quasi-endowment" is not really legally restricted at all. New York law is clear that, whether under N-PCL § 513(b), Estates, Powers & Trusts Law 8-1.1 or New York's common law, any gift received with donor restrictions must be applied in accordance with those restrictions. To do otherwise is a breach of the fiduciary duty of the institution's governing Board.

Defining the "Donor"

More so perhaps than in any other jurisdiction adopting the uniform act, NYPMIFA contemplates a high degree of donor involvement and oversight. Institutions have obligations under the statute to identify and track restricted-fund donors, so the identification of this special class is very important.

The term "donor" under the statute includes not only the person (such as an individual, a corporation or a foundation) who makes a gift, but also any person designated in a gift instrument to act in the place of the donor.[9] This means that the development office needs to be aware of any gift agreement that provides the donor with the ability to designate, whether in the agreement itself or afterward, someone else to act as the donor's representative under the statute. The donor's executors, heirs, successors, assigns, transferees or distributees are not considered the "donor" for purposes of the statute, unless they are so designated by the donor.

Interestingly, the definition of "donor" under the statute is limited to those circumstances in which a gift is made "pursuant to a gift instrument." The law therefore puts a heavy emphasis on the existence of a "gift instrument" (defined at N-PCL § 551(c)), which can also include an institutional solicitation. Absent some form of writing or other record by which a gift is made, there appears to be no "gift instrument" and so no "donor" under NYPMIFA.

Other Issues of Donor Standing and Notice

In order to bring a valid legal challenge against a not-for-profit with respect to the use of its assets, a party must have legal standing. The general rule in New York State is that donors, absent a specific agreement to the contrary or special circumstances, do not have legal standing to sue a charity.[10] There are several circumstances under NYPMIFA, however, where donor notice is required. These notice requirements establish a clear need to maintain accurate and accessible information on gift instruments, including an institutional solicitation, under which gifts are made to an institutional fund. The precise nature of those gift records should be decided in light of the requirements of the law and the facilities of the institution, but would appear to require at a minimum information about the identity and address of the donor, the gift amount and any specific restrictions on the use of the funds.

Gift Acceptance Policy

A comprehensive gift acceptance policy is an essential tool for the development office, helping to shape the conversation on complex gifts so that both the institution and the donor are satisfied. Charities are well-counseled to review and update their gift acceptance policy regularly.

NYPMIFA requires that the institution, "[w]ithin a reasonable time after receiving property," decide whether to retain gifted property or liquidate it.[11] The statute provides a greater amount of flexibility in retaining gifted assets than perhaps in the past.[12] The common provision in a gift acceptance policy requiring liquidation of gifts "as soon as practicable" now has a statutory basis and should reflect institutional practices on gift liquidation.

Endowment Gift Solicitation

New York's Executive Law Article 7-A deals generally with charitable solicitations in the state. It establishes a registration and annual reporting regime as well as mandates on charitable solicitations so that the programs and activities supported are clearly described. Religious institutions are exempt from its coverage generally, and educational institutions are also excepted from certain registration requirements.[13]

The statute has been amended at Executive Law § 174-b(2) to require that any endowment solicitation by an institution subject to NYPMIFA include a statement making prospective donors aware that, unless otherwise restricted, the organization may expend so much of an endowment fund as it deems prudent, consistent with the requirements of NYPMIFA. The language of the required disclosure is somewhat tortured and has a high probability for confusion within the donor community, so the development office will need

to review with counsel how best to make the required disclosure.

Gift Agreements

NYPMIFA recognizes that donors can modify the application of the statute in structuring their particular gifts. Such special provisions can ease or complicate the administration of donor-restricted funds and should be thoroughly discussed both internally and with the donor to assure that the institution can meet its obligations. The use of standard form gift agreements, acceptable within the institution and approved ahead of time by legal counsel, is an essential element to assuring success across a broad range of donors.

There are a number of donor reporting and naming opportunity provisions that should ideally be standardized for institutional use. Even a governing law clause of a gift agreement can have an important impact. Some organizations reserve in their standard form agreements the ability of a majority of the governing Board to vary the use or management of a restricted fund on certain conditions, without the involvement of, or notice to, the donor, a court or the Attorney General. NYPMIFA permits as much. Organizations with single page fund agreements may quickly find themselves out of step with their peer institutions in the prudent practice of establishing fundamental gift parameters at the time a fund is created.

III. Finance Office

Allocable Costs

The allocation of management and investment costs to institutional funds is an issue that deserves attention in both the gift acceptance policy and the investment policy. Donors may want to know what costs are charged against a fund, and those costs might be reflected in any voluntary report to the donor.

The new statute clarifies that the institution may incur only those costs that are "appropriate and reasonable in relation to the assets, the purposes of the institution, and the skills available to the institution."[14] There is no explicit language in the statute about the ability to clarify or amplify such charges, although the responsibilities of the institution are generally subject to the intent of a donor as expressed in a gift instrument.[15] Accordingly, the institution needs to decide which costs are properly allocable to restricted funds, likely including that portion of management and custodial fees and perhaps taxes related to a particular fund.

Annual Reporting

In addition to the reporting on restricted funds that accompanies the new Form 990, N-PCL § 513(b) requires that governing Boards cause accurate accounts to be kept of donor-restricted assets separate and apart from the accounts of other assets of the institution. Unless the terms of the particular gift instrument provide otherwise, the treasurer must make an annual report to the corporation's members (if there are members) or else to the governing Board concerning the assets held and the use made of them and their income. This is not a change from prior law but recognizes the need for accurate accounting and reporting so that the Board can meet its obligations.

Modifying Existing Funds

NYPMIFA liberalizes the statutory regime for the release or modification of donor restrictions, expanding the process and making the options and steps clearer. Of particular interest is N-PCL § 555(d), which now permits release or modification of restrictions for certain funds—those below $100,000 in value that are over twenty years old—on notice to the Attorney General and any available donor. No court approval is required in such cases.

More generally, institutions can now seek court release or modification of donor restrictions, even if the donor does not consent, on notice to the donor and the Attorney General.[16] The Guidance recommends that institutions solicit donor consent if the donor is available before requesting relief from a court or the Attorney General.[17]

Institutions are well-advised to review their existing funds to determine which, if any, are candidates for modification.

IV. Investment Management

Written Investment Policy

NYPMIFA requires that an institution have a written investment policy setting forth, among other things, guidelines on investment and the delegation of management and investment functions. Most organizations already have policies for the management of their investment, versus operating, assets, but the statute specifically requires that these policies be consistent with the provisions of NYPMIFA.[18] NYPMIFA's adoption raises two questions: to what extent must an institution's current policy incorporate or reference the statute; and what other changes to the policy may be required or appropriate to comport with the statute?

As to the first inquiry, mere reference to NYPMIFA or sections of it will hardly have the desired effect of directing fiduciaries and the institution on the proper use of assets. Some incorporation of NYPMIFA's terms will be necessary and their consideration reflected in regular meeting minutes.

As to the second question, NYPMIFA does not delineate what topics an investment policy should address. The Guidance helps to fill this gap by stating that an investment policy may address topics including: (1) general investment objectives; (2) permitted and

prohibited investments; (3) acceptable levels of risk; (4) asset allocation and diversification; (5) procedures for monitoring investment performance; (6) scope and terms of delegation of investment management functions; (7) the investment manager's accountability; (8) procedures for selecting and evaluating investment managers and other outside agents; (9) processes for reviewing investment policies and strategies; and (10) proxy voting.[19]

Institutional investment policies provide the basis for making investment decisions and communicating institutional imperatives to investment advisors and managers. They offer development offices a vehicle to educate fund donors on how their contributions will be invested. As a result, institutional investment policies will be in many ways unique to each institution, and the Guidance acknowledges that there is no "one size fits all" approach that applies to all institutions.[20] Investment policies should be modified with the assistance of legal counsel, based on institutional practices and resources.

Delegation of Investment Management

NYPMIFA preserves the ability of a governing Board to delegate responsibility for investment matters to a Board committee or other officers or persons within the organization. N-PCL § 554 governs external delegation to an independent investment advisor, investment counsel or manager, bank or trust company.[21] The statute provides that in selecting, continuing or terminating an agent, the institution must assess the agent's independence, including any conflicts of interest.[22]

To take full benefit of the reliance on the expertise of investment management consultants providing advisory services to the investment committee—whether on a discretionary or non-discretionary basis—the contractual and other requirements of the statute need to be met.[23] Such a delegation should be explicit, concise and in writing. It is vitally important to do so, because a proper delegation means the institution (and its Board) is not liable for the decisions or actions of an agent to which a function was delegated.[24] The failure to make a proper delegation means that the governing Board still retains full fiduciary responsibility for these assets.

In making or continuing the delegation to each agent, the institution must act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances.[25] The absence of conflicts should be noted in the minutes. The institution will establish or reaffirm the scope and terms of the delegation, including the payment of compensation, consistent with the purposes of the institution and the institutional fund.[26] The institution must monitor the agent's performance and compliance with the scope and terms of the delegation.[27]

Prudent Investor Standard

The new law brings New York into the new millennium with a prudent investor standard requiring the institution to manage and invest its funds in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.[28] A person with special skills or expertise, whether inside or outside the institution, is required by law to use them, thus creating a different standard of care for these individuals or firms.[29] This standard should be made clear to both internal and external delegees.

General Investment Considerations

N-PCL §§ 552(a) and 552(e)(1) require that institutions consider the following factors, if relevant, in managing and investing each institutional fund, except as otherwise provided by a gift instrument: (1) the purposes of the institution; (2) the purposes of the institutional fund; (3) general economic conditions; (4) the possible effect of inflation or deflation; (5) the expected tax consequences, if any, of investment decisions or strategies; (6) the role that each investment or course of action plays within the overall investment portfolio; (7) the expected total return from income and the appreciation of investments; (8) other resources of the institution; (9) the needs of the institution and the fund to make distributions and to preserve capital; and (10) an asset's special relationship or special value, if any, to the purposes of the institution. These elements should be set forth explicitly in the minutes of any meeting at which they are considered, as this is the best way to demonstrate their proper review. The statute comports with the current common practice of grouping similarly situated endowment or other funds for investment purposes.[30]

Investment Performance Reporting

The new law has a specific provision requiring the institution to make a reasonable effort to verify facts relevant to the management and investment of each fund.[31] The focus is clearly on the losses arising out of the Madoff and similar scandals, and the lack of verifiable information available to the fiduciaries who approved such investments.

Diversification

N-PCL § 552(e)(4) requires that the institution diversify the investments of each fund unless it prudently determines that because of special circumstances the purposes of the fund are better served without diversification.[32] Such a finding should be explicitly set forth in the accompanying minutes and must be reviewed as frequently as circumstances require, but at least annually. Consideration of diversification questions should be an issue addressed in the minutes of each meeting of the investment committee, along with the review of investment performance and investment guidelines.

IV. Setting the Endowment Fund Spending Policy

Appropriation for Expenditure

NYPMIFA provides that in deciding whether to appropriate from an endowment fund, an institution must act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and must consider, to the extent relevant, the following factors: (1) the duration and preservation of the endowment fund; (2) the purposes of the institution and the endowment fund; (3) general economic conditions; (4) the possible effect of inflation or deflation; (5) the expected total return from income and the appreciation of investments; (6) other resources of the institution; (7) where appropriate and circumstances would otherwise warrant, alternatives to expenditure of the endowment fund, giving due consideration to the effect that such alternatives may have on the institution; and (8) the investment policy of the institution.[33]

For those institutions that hold multiple endowment funds, the Guidance says that a board may make a single decision to appropriate from funds that are similarly situated and that any decision to appropriate from funds collectively would be justified if the eight factors described above could be applied to each fund individually in the same way.[34]

The seventh item in the list above is particular to New York and turns the usual exercise of the appropriation approval on its head. NYPMIFA now requires that fiduciaries consider alternatives to expenditure of the endowment fund before making a decision to spend from the fund. This would seem to be contrary to donor intent in establishing the fund—where the primary expectation is that the assets will be expended to further the purposes of the institution, and only accumulated to achieve that goal into the future.

The Guidance from the Charities Bureau emphasizes this particular requirement[35] and indicates that, where the investment function is separated by the investment committee from the finance committee, it is the latter body—with its broader command of institutional resources and needs—that would be responsible for establishing the endowment spending rate. Without an understanding of the demands of the annual budget and alternative resources, one would be hard-pressed adequately to consider alternatives to expenditures from an endowment fund.

Contemporaneous Records

N-PCL § 553(a) specifically requires that the institution keep a contemporaneous record describing the consideration given to each factor in making spending decisions, including the extent to which a factor affects the decision to appropriate and how much to appropriate, and permanently keep such records.[36]

Any minutes of a meeting dealing with appropriation decisions should document a number of findings:

- The institution has identified those endowment funds that are not subject to donor restrictions limiting the ability of the institution to apply its total return spending formula.
- The institution has identified those endowment funds that, as a result of a response to a specific notice provided to the donor, are subject to a limitation on the ability to spend the historic dollar value of the fund.
- The institution has considered, to the extent relevant, the eight favors listed above.
- The institution, in accord with written procedures it has developed, has identified similarly situated endowment funds for which a single appropriation decision can be made.[37]

Presumption of Imprudence—the "Massachusetts Rule"

The Commonwealth of Massachusetts, in adopting its version of UPMIFA in July of 2009, dropped what had become known as the "Massachusetts Rule." New York, however, saw fit to include the rule for the first time in its law.[38]

Under this rule, absent donor direction to the contrary, expenditure in any year of an amount greater than seven percent of the fair market value of an endowment fund raises a rebuttable presumption of imprudence in the case of funds established pursuant to gift instruments executed on or after September 17, 2010. The seven percent ceiling, however, is calculated on the basis of market values determined at least quarterly and averaged over a period of not less than five years immediately preceding the year in which the appropriation for expenditure is made. For an endowment fund in existence for less than five years, the fair market value of the endowment fund must be calculated for the period the endowment fund has been in existence.

This five-year look-back is a relatively long period of time and may not be supported by existing accounting systems within the institution.[39] As the Massachusetts rule applies only to new endowment funds, institutions should strongly consider whether explicitly to except out its application in donor agreements.

VI. Conclusion

NYPMIFA is a long-awaited change in New York law, with far-ranging effects on not-for-profit corpora-

tions. The operational and accounting changes that result are best considered with a full legal understanding of the statute and an appreciation of the resources and needs of the institution.

Endnotes

1. *A Practical Guide to the New York Prudent Management of Institutional Funds Act*, Office of the Attorney General, Charities Bureau, available at <http://www.charitiesnys.com>.
2. N-PCL § 551(d) and (e).
3. N-PCL § 551(b).
4. N-PCL § 553(a).
5. Guidance at p. 9.
6. *Id.*
7. Under this exception, notice is not required if "funds were received as a result of an institutional solicitation without a separate statement by the donor expressing a restriction on the use of funds." N-PCL § 551(e)(2)(C).
8. Guidance at p. 10.
9. N-PCL § 551(a-1).
10. *Compare Smithers v. St. Luke's Roosevelt Hosp. Ctr.*, 281 A.D.2d 127 (1st Dep't 2001) (where a New York court granted standing to a spouse, who had been named the special administratrix of her husband's estate, to enforce the intent of her husband's donation to a hospital) with *Rettek v. Ellis Hospital*, 2010 U.S. App. LEXIS 1863 (2d Cir. 2010) (denying standing).
11. N-PCL § 552(e)(5).
12. *See, e.g.*, N-PCL § 552(e)(1)(h) on an asset's "special relationship" or "special value" to the purposes of the institution.
13. Executive Law §§ 172-a(1) and 172-a(2)(g).
14. N-PCL § 552(c)(1).
15. N-PCL § 552(a).
16. Under prior law, court release or modification could be sought only if the donor was not available.
17. Guidance at p. 15. If the donor is not available or withholds consent, the Guidance urges institutions to submit draft petitions to the Charities Bureau before filing in court so that potential issues can be identified and resolved. *Id.*
18. N-PCL § 552(f).
19. Guidance at p. 14.
20. *Id.*
21. N-PCL § 551(k).
22. N-PCL § 554(a)(1). The Guidance elaborates on this point by stating that the selection of an outside agent should be based on the agent's competence, experience, past performance and proposed compensation, and not on any business or personal relationships between the agent and board members or other insiders. Although it is not required by the statute, the Guidance also recommends that institutions adopt conflict-of-interest policies requiring full disclosure by interested officers and directors of their business or personal relationships with any outside agent. Guidance at pp. 14-15.
23. For example, NYPMIFA requires—as did prior New York law—that each contract pursuant to which authority is delegated provide that it may be terminated by the institution at any time, without penalty, upon not more than sixty days' notice. N-PCL § 554(e).
24. N-PCL § 554(c).
25. N-PCL § 554(a).
26. N-PCL § 554(a)(2).
27. N-PCL § 554(a)(3).
28. N-PCL §§ 552(b), 553(a), and 554(a). In a long-awaited move to gender equality, N-PCL § 717(a) has been amended to replace the prudent "man" standard with that of a prudent "person."
29. N-PCL § 552(e)(6).
30. N-PCL § 552(d) (an "institution may pool two or more institutional funds for purposes of management and investment"). As discussed further below, the Guidance clarifies that institutions may group similarly situated funds for spending purposes as well.
31. N-PCL § 552(c)(2).
32. The Guidance does not expand on this requirement or what might constitute "special circumstances." This may present a potential issue for private family foundations that have been funded primarily with stock of a single issuer (such as stock of a company controlled by the family).
33. N-PCL § 553.
34. Guidance at pp. 11-12.
35. The Guidance says this factor is intended to ensure that boards will not automatically decide to spend from endowment funds if circumstances warrant exploring other possible alternatives. As an example, the Guidance suggests that if a fund has decreased in value, it may be prudent to consider steps such as increasing fund-raising efforts, decreasing or deferring expenditures, selling non-essential assets or reducing non-essential staff. Guidance at p. 12.
36. The Guidance adds that if a governing board determines that any factor is not relevant to a decision, it should document how it reached its conclusion. Guidance at p. 11.
37. The institution should document in writing why a group of funds is similarly situated (e.g., because of their purpose, type of investments or other factors). Guidance at p. 12.
38. N-PCL § 553(d).
39. Many charitable organizations have spending policies that are based on a three-year average of an endowment fund's fair market value. The Guidance notes that such spending policies may result in appropriations that are presumptively imprudent under the seven percent standard and that all spending policies must be reviewed to determine how they interact with the new standard. Guidance at p. 13. As a practical matter, many institutions will now have to perform separate calculations to determine whether particular spending decisions would be presumptively imprudent.

Michael J. Cooney is the head of Nixon Peabody LLP's Higher Education and Exempt Organization Practice. He represents a wide array of nonprofit and charitable institutions both within New York State and without.

The Liability Reporter

By Michael P. Ryan

"The assault on the citadel of privity is proceeding in these days apace."

—Benjamin Cardozo

In the wake of *In re Schneider*,[1] the New York trusts and estates community is now familiar with the increased exposure to malpractice liability that attorneys face for estate planning services provided to a deceased client. In this installment of the Liability Reporter, we report on several post-*Schneider* developments, including two New York cases and an opinion from the New York State Bar Association's Committee on Professional Ethics (which is reproduced on page 37).

In re Schuman

The facts in *In re Schuman*[2] do not really lend themselves to a *Schneider* analysis, except insofar as the plaintiff's attorney sought an extension of *Schneider* that was rejected by Surrogate Glen.

In *Schuman*, the decedent was survived by a spouse and three children. All four were named co-trustees (does this give you a sense of foreboding?) of a residuary trust under the Will, funded with valuable assets consisting of interests in closely held corporations that owned and managed commercial real estate. Litigation commenced early in the estate's administration. When the mother petitioned to settle her executor's account, two of the children objected. They also commenced a third party action against the mother's attorney and accountant charging these professionals with malpractice and with "aiding and abetting" the executor to breach her fiduciary duty.

The allegations of aiding and abetting concerned the objectants' fear that the mother, attorney and accountant were planning to split the residuary trust into three separate trusts, each with the mother as a co-trustee and one of each of the children as the other co-trustee. Presumably, the split, if it were even contemplated, would have divided the residuary trust equally among the three siblings and caused no increased costs or commissions. The objectants nevertheless charged that any such plans would have inured to their detriment because it would have given their mother "disproportionate control" over the estate properties. The court dismissed this allegation, finding the inchoate plans speculative and, if true, subject to consent of the interested parties and approval by the court.

The second line of attack against the attorney concerned allegations of malpractice; specifically, the objectants charged that the services performed by the attorney "were characterized by professional negligence, including the creation of inaccurate and ineffective documentation of transactions undertaken by the Executor of the Estate and deficient advice regarding taxes, the distribution of bequests made in the Will, and proceedings in the Surrogate's Court."[3] Surrogate Glen observed that the objectants played many roles in the estate—as successor co-executors of the decedent's will, as beneficiaries of pre-residuary bequests and as co-trustees and remainder beneficiaries of the residuary trust. In none of those roles, however, were the objectants in an attorney-client relationship with the attorney who represented the executor. The court ruled that the *Schneider* holding was expressly limited to a narrow set of circumstances not present here, i.e., claims for estate planning malpractice and claims made by the testator's personal representative. Surrogate Glenn next delivered the *coup de grâce* to the objectants by ruling that privity aside, their claims against the attorney were time-barred.

More interesting are the allegations against the accountant. The liability standard for accountant liability *vis-a-vis* the issue of privity is different than that established by *Schneider* for attorneys. The leading case on accountants' liability is *Credit Alliance v. Arthur Andersen.*[4] In *Credit Alliance*, the Court permitted negligence claims against an accountant by a non-client where: (1) the accountant was aware that its financial reports were to be used for a particular purpose; (2) the plaintiff was known by the accountant to be relying on its reports; and (3) the accountant through his or her own conduct evidenced his or her understanding of the plaintiff's intended reliance. In *Schuman*, the court found that the objectants failed to assert one of these elements of liability, namely that of their reliance on the accountants' work.

Leff v. Fulbright and Jaworski, L.L.P.

The First Department's decision in *Leff v. Fulbright and Jaworski, L.L.P.*[5] is especially worthy of note. It involved a malpractice claim brought by a widow against

the law firm that provided estate planning services both to her and to her late husband. Many estate planners represent spouses simultaneously—either jointly or as separate clients—avoiding the potential conflict with full disclosure, consent in writing, etc. In *Leff*, the surviving spouse commenced an action in Supreme Court alleging damages to her inheritance by virtue of the estate planning advice given to her husband. The plaintiff alleged that she and her husband had been represented jointly and that this representation was sufficient to breach the wall of privity. The court disagreed, saying the defendants had demonstrated that while they represented the wife in her estate planning and other matters, she was not in privity with them with regard to her husband's estate planning.

The court's decision suggested that if the facts had involved more intermingled interactions between husband and wife in the planning process, they might have satisfied the "approaching privity" standard for liability established by the Court of Appeals in *Prudential Ins. Co. of Am. v. Dewey, Ballantine, Bushby, Palmer and Wood*.[6] This would have required a showing that the defendants "knew and intended that their advice to plaintiff's late husband was aimed at affecting plaintiff's conduct or was made to induce her to act" or that she had "relied upon defendants' advice to her detriment."[7]

The court also made reference to *Estate of Nevelson v. Carro, Spanlock, Kaster and Cuiffo*.[8] In that case, the late sculptor Louise Nevelson and her son were advised to create a corporate entity as a vehicle to avoid estate taxation of her assets. The plan's failure to achieve the desired goal—and the resulting assessment by the IRS of millions of dollars in estate and gift taxes and substantial interest and penalties—led to a legal malpractice claim by the estate, the son and the corporation against the law firm.

The *Nevelson* opinion did not discuss privity issues, but it was cited by the *Leff* court as an example of a case where the plaintiff beneficiary "was intimately involved in the estate planning and relied upon the attorney's advice"[9] in establishing the corporation. The *Nevelson* decision is also interesting on procedural grounds. The court ruled that the law firm's summary judgment motion was fatally deficient in failing to offer expert opinion on the soundness of the estate plan and in relying only on its own "conclusory, self-serving statements."[10] The defendants' failure to establish a prima facie right to judgment also absolved the plaintiffs from the requirement to come forward with expert evidence of malpractice in opposition to the motion for summary judgment. Finally, the court rejected the defendants' argument that Nevelson's son refused to follow their advice and that any damages were his own fault. The court ruled that any such culpability on the part of the plaintiff was not a complete defense but would only go to the apportionment of comparative liability, which was for a jury to decide.

In a final consideration of *Leff*, practitioners should note that the plaintiff was represented by one of the premier plaintiffs' firms specializing in medical malpractice and other sophisticated torts.

Ethics Opinion 865

In Opinion 865,[11] the Committee on Professional Ethics of the New York State Bar Association considered the following question: may an attorney who prepared an estate plan for a client agree to act as counsel to the executor after the client's death?

Of course, the question challenges one of the fondest desires of the estate planner—to be able to represent the fiduciary after the client's demise. Indeed, some practitioners may consider the preparation of an estate plan as a loss leader that precedes the larger task of representing the fiduciary in the estate's administration.

In Opinion 865, the analysis begins with a reference to Rule 1.7 of the Rules of Professional Conduct, delineating the lawyer's responsibility to avoid a concurrent conflict of interest with the client. It then points to three different scenarios of concern: (1) the estate planner realizes he or she made an actionable mistake before the nominated executor requests representation; (2) the estate planner perceives no malpractice on his or her part when the retainer is signed; and (3) the estate planner discovers his or her possible malpractice only during representation of the fiduciary. Clearly, posing the questions in this fashion suggests the answers—the lawyer must withdraw from representing the fiduciary in the first and third instances but has no such duty in the second.

One suspects that this conclusion, commonsensical and unassailably logical as it is, may lend itself to further consideration as the *Schneider* case law develops. After all, one of the duties of an executor is the marshaling of estate assets, and that process may include, in our post-*Schneider* world, an analysis of the estate planning advice offered to the decedent. If the estate planner is also the fiduciary's attorney, could he or she be reasonably expected to render an impartial analysis of his or her own work? Would the court conclude that in a proceeding to settle an executor's final account, a beneficiary of the estate is precluded from objecting to the fiduciary's failure to commence a malpractice action? The outcome of such a challenge remains to be determined.

Opinion 865 concludes by stating that "even if the lawyer perceives some insignificant error or omission in the prior representation, the lawyer has no duty to

report it to the client."[12] Insignificance, like beauty, may be in the eye of the beholder. The courts will tell us more on this issue as time goes by.

Endnotes

1. 15 N.Y.3d 306, 907 N.Y.S.2d 119 (2010).
2. N.Y.L.J., May 6, 2011, p. 23 (Sur Ct., New York Co.).
3. *Id.*
4. 65 N.Y.2d 536, 483 N.E.2d 110, 493 N.Y.S.2d 435 (1985).
5. 78 A.D.3d 531, 911 N.Y.S.2d 320 (1st Dep't 2010).
6. 80 N.Y.2d 377, 590 N.Y.S.S2d 831 (1992).
7. *Leff,* 78 A.D.3d at 533.
8. 259 A.D.2d 232, 686 N.Y.S.2d 404 (1st Dep't 1999).
9. *Leff,* 78 A.D.3d at 532.
10. *Estate of Nevelson*, 259 A.D.2d at 284.
11. NYSBA Comm. on Professional Ethics, Formal Op. 865 5/10/11.
12. *Id.*

Michael P. Ryan is a partner in the Brooklyn office of Cullen and Dykman LLP and a member of the Schneider subcommittee of the Trusts and Estates Law Section.

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Committee on Professional Ethics Opinion 865 (5/10/11)

Topic: Estate planner serving as attorney for executor; conflict of interest; legal malpractice

Digest: Lawyer who prepared estate plan for decedent may represent executor despite recent change in law of legal malpractice in *Estate of Schneider v. Finmann* (N.Y. 2010) provided that lawyer does not perceive a colorable claim of legal malpractice arising out of the estate planning.

Rules: 1.7, 1.10(a), 1.16.

FACTS

1. The inquirer prepared an estate plan for his client and supervised the execution of a Will in furtherance of the plan. The Will named the deceased client's nephew executor of his estate. The client has recently died, and the estate is ready for administration. The nephew has asked the inquirer to represent him in connection with the estate's administration, but the inquirer is concerned because a recent change in the law permits executors to sue estate planners for malpractice, and both the estate plan and the Will were prepared well within any period of limitations possibly applicable to the inquirer's conduct (meaning that the statute of limitations will not be available as a defense to any claim).

QUESTION

2. In light of *Estate of Schneider v. Finmann,* 15 N.Y.3d 306 (2010), may an attorney who prepared an estate plan for a client agree to act as counsel to the executor after the client's death?

OPINION

3. On June 17, 2010, in *Estate of Schneider v. Finmann*, 15 N.Y.3d 306 (2010), the New York Court of Appeals overruled a long line of cases in the estate planning field. The overruled cases had held that the doctrine of privity effectively barred the estates of deceased estate planning clients from filing a legal malpractice suit against the lawyers who planned the decedent's estate. In *Schneider*, the Court of Appeals held that the executor or personal representative of the decedent "stands in the shoes of the decedent," and therefore has "the capacity to maintain a malpractice claim on the Estate's behalf" (at 309).

4. Shortly after publication of the Court's decision in *Schneider*, a number of authorities speculated on the consequent expansion of an executor's obligations and liabilities, as well as the obligations and liabilities of lawyers providing estate planning services. Although the Court did not expressly give the estate's *beneficiaries* the right to bring a suit for legal malpractice, some commentators suggested that an aggrieved beneficiary might ask the executor to sue a lawyer whose alleged incompetence had caused him or her to receive less from the estate than he or she believed they otherwise would have obtained. *See, e.g.,* David Siegel, *New York State Law Digest*, No. 607, at 3-4 (July 2010). Others questioned whether an attorney could ethically agree to represent an executor in connection with the administration of any estate that the attorney had planned.

The relevant rule: Rule 1.7

5. We begin our analysis with Rule 1.7 of the Rules of Professional Conduct, which states in relevant part:

> (a) Except as provided in paragraph (b), a lawyer shall not represent a client if a reasonable lawyer would conclude that…(2) there is a significant risk that the lawyer's professional judgment on behalf of a client will be adversely affected by the lawyer's own financial, business, property or other personal interests.
>
> (b) Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation…(2) the representation is not prohibited by law…(3) the representation does not involve the assertion of a claim by one client against the another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and (4) each affected client gives informed consent, confirmed in writing.

6. Before applying Rule 1.7, we distinguish three different situations:

A. The lawyer who prepared the estate plan realizes at the outset—before commencing representation of the executor in the administration of the estate—that he (the lawyer) may have committed legal malpractice and that the executor would have a colorable malpractice claim against him.

B. The lawyer at the outset of representing the executor in the administration of the estate does not perceive any basis for claiming that he (the lawyer) committed malpractice, and does not believe the executor would have a colorable malpractice claim against him.

C. The lawyer did not initially perceive any basis for a legal malpractice claim against him, but has come to realize during the representation of the executor that he (the lawyer) may have committed legal malpractice and that the executor would have a colorable malpractice claim against him.

Situation A: Lawyer perceives colorable legal malpractice claim at outset

7. In the first situation— the lawyer who prepared the estate plan and/or drafted the Will realizes at the outset that the legal work was negligent to a degree that gives rise to a colorable (*i.e., prima facie*) claim of malpractice—a conflict of interest arises under Rule 1.7(a)(2). The conflict arises because there is a "significant risk" that the lawyer's professional judgment will be adversely affected. Moreover, if the lawyer realizes that the executor could assert a colorable claim of malpractice against the lawyer, the consent provisions of Rule 1.7(b) could not be satisfied. To permit the lawyer to undertake such a representation would place the lawyer in the manifestly untenable position of having to counsel the executor on whether to sue himself (the lawyer). In such circumstances, the lawyer could not "reasonably believe[]" that he could provide "competent and diligent representation" to the executor. In that instance, Comment [14] to Rule 1.7 is instructive. It says:

> [S]ome conflicts are nonconsentable. If a lawyer does not reasonably believe that the conditions set forth in paragraph (b) can be met, the lawyer should neither ask for the client's consent nor provide representation on the basis of the client's consent. A client's consent to a nonconsentable conflict is ineffective. …

8. Accordingly, if the preparer/drafter believes at the outset that the executor has a colorable claim of legal malpractice against him, then the preparer can neither ask for the executor's consent to the conflict nor represent the executor if the executor volunteers consent to the conflict. Therefore, the lawyer may not agree to represent the executor—and pursuant to the imputation rule, Rule 1.10(a), no other lawyer in the lawyer's firm may represent the executor either.

9. Moreover, we have held that an attorney is ethically bound to report to a client any significant error or omission that may give rise to a claim of malpractice. *See, e.g.,* N.Y. State 734 (2000) (legal services organization must report to client a "significant error or omission that may give rise to a possible malpractice claim"); N.Y. State 275 (1972) (lawyer has "affirmative duty" to advise client that lawyer's failure to act resulted in claim being barred by statute of limitations). An executor "stands in the shoes of the decedent" (*Schneider*). Thus, a lawyer in the first situation must report to the client (who was formerly the decedent, but is now the executor) that the lawyer's preparation of the estate plan has given rise to a colorable claim of malpractice against him. The same opinions, however, have noted that not all errors or omissions will give rise to a claim of malpractice. Some errors or omissions are insignificant, and there is no need to report them. That is essentially the second situation, which we address next.

Situation B: Lawyer *does not* perceive colorable legal malpractice claim at outset

10. In the second situation—the lawyer who prepared the estate plan or drafted the Will does not believe at the outset that the executor could assert a colorable claim for legal malpractice against him—our conclusion is different. If the preparer/drafter perceives no apparent basis for a claim of malpractice, then no "significant risk" arises that the lawyer's professional judgment on behalf of the executor will be adversely affected by the lawyer's own interests, and the need to obtain consent under Rule 1.7(b) is not triggered. Accordingly, there is no reason to require the lawyer or the lawyer's firm to decline representation of the estate. In such cases, the Court's decision in *Schneider* should have no effect on the long-established practices of the trusts and estates bar, and the lawyer may agree to represent the executor after the client's death. Moreover, even if the lawyer perceives some insignificant error or omission in the prior representation, the lawyer has no duty to report it to the client.

Situation C: Lawyer perceives colorable legal malpractice claim during representation

11. In the third situation—the lawyer does not perceive any basis at the outset for claiming that he committed malpractice, but comes to believe during the representation that the executor has a colorable claim for malpractice against the lawyer—the conflict again becomes nonconsentable. Just as in the first situation, the lawyer is in the untenable position of having to counsel the executor on whether to sue the lawyer. Rule 1.7(a)(2) does not distinguish between conflicts that exist at the outset of a representation and conflicts that arise during a representation. In either situation, the conflict is nonconsentable, both for the lawyer and for all other lawyers associated with his firm. Pursuant

to Rule 1.16(b)(1), the lawyer must withdraw (with the court's permission, if required) to avoid a violation of the Rules, and must upon withdrawal "take steps, to the extent reasonably practicable, to avoid foreseeable prejudice to the rights of the client" (the executor). Moreover, as in the first situation, the lawyer must report the apparent legal malpractice to the executor.

12. In sum, if the lawyer who prepared the estate plan knows at the outset or anytime after the representation of the executor commences that the quality of the plan is subject to a colorable challenge (or where the plan has in fact been challenged) on grounds that it was incompetently prepared, the lawyer cannot represent the executor, and furthermore must disclose to the executor any facts that would permit the executor to evaluate the apparent malpractice. If not, the lawyer may represent the executor in the administration of the estate.

13. Thus, the Court's decision in *Schneider* has not changed the basic conflicts issues in cases where legal malpractice in preparing the estate plan is not apparent. Lawyers who are engaged in estate planning have traditionally handled the administration of the estates that they have planned. For example, it has long been held that fiduciaries may retain their own firms to act as counsel on the estates that they administer. *See, e.g.,* N.Y. State 471 (1977) (receiver in a mortgage foreclosure action may retain the law firm of which he is a member as his counsel). The apparent risk in such retention has been viewed as outweighed by various advantages—both practical and economic—in permitting lawyer-fiduciaries and their firms to serve in both capacities. These advantages are outweighed only when the lawyer who prepared the plan perceives a colorable claim of legal malpractice, in which case Rule 1.7(b)(1) makes the conflict nonconsentable.

Settling a legal malpractice claim

14. A lawyer may settle a claim for malpractice with a client provided three conditions are satisfied: (a) the client has been fully apprised of the facts pertaining to the representation that may give rise to specific claims against the lawyer; (b) the lawyer has been discharged or has withdrawn from the representation; and (c) the lawyer has advised the client to secure independent counsel in the negotiation of the settlement agreement. *See, e.g.,* N.Y. State 591 (1988) ("A lawyer may ethically negotiate with a former client for the settlement or release of potential malpractice claims, but only after the lawyer takes specific steps to insure that the negotiations are fair," including withdrawing from representation). To satisfy this line of opinions, a lawyer who perceives a colorable malpractice claim against himself for his estate planning must withdraw pursuant to Rule 1.16 before seeking to settle the claim, and must apprise the client (the executor) of the facts giving rise to the malpractice claim and of the desirability of engaging independent counsel to evaluate the claim.

CONCLUSION

15. In light of *Estate of Schneider v. Finmann,* a lawyer who prepared an estate plan for a client may agree to act as counsel to the executor after the client's death as long as the lawyer does not perceive a colorable claim for legal malpractice before or during the representation of the executor. However, if the lawyer does perceive a colorable claim for legal malpractice before or during the representation, then the conflict is nonconsentable and the lawyer (and all other lawyers associated with his firm) must decline or withdraw from the representation and the lawyer must inform the executor of the facts giving rise to the claim.

(50-10)

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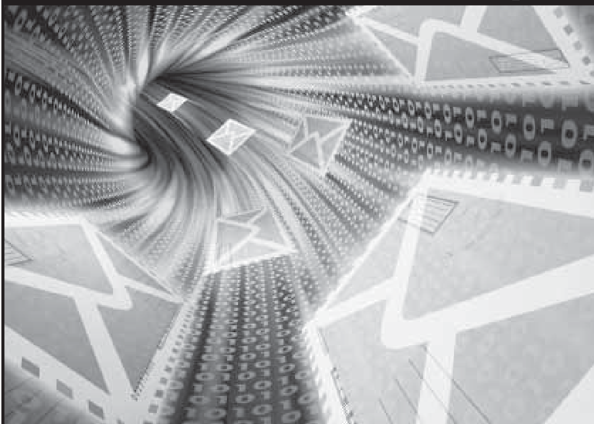

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Cristine M. Sapers, Esq.
Debevoise & Plimpton LLP
919 Third Avenue
New York, NY 10022-3902
cmsapers@debevoise.com

Articles should be submitted in electronic document format (pdfs are NOT acceptable), and include biographical information.

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Florida Update

By David Pratt and Jonathan Galler

LEGISLATIVE UPDATE

Amendment to Florida's LLC Charging Order Statute

David Pratt

In May 2011, Florida substantially amended its limited liability company charging order statute. Fla. Stat. § 608.433. The amendment shores up Florida's asset-protection laws in the wake of the Florida Supreme Court's controversial decision in *Olmstead v. FTC*, 44 So. 3d 76 (Fla. 2010).

In *Olmstead*, the Court held that a judgment creditor of the member of a "single-member" LLC is not limited to a charging order as its exclusive remedy and may instead obtain an actual ownership interest in the LLC in satisfaction of the judgment.

A charging order is a legal remedy that provides a judgment creditor with the right to receive distributions made by an LLC to its members. It does not entitle a judgment creditor to ownership or management rights. The Court concluded, however, that the charging order is not the sole remedy available because, unlike the corresponding provisions of Florida's Revised Uniform Partnership Act and the Florida Revised Uniform Limited Partnership Act, the LLC statute does not specifically state that the charging order is the "exclusive remedy" of a judgment creditor.

Because the language of the charging order statute at that time did not distinguish between single-member LLCs and multi-member LLCs, the *Olmstead* decision left unclear whether or not the Court's holding applied, or would be extended, to both types of LLCs. If the holding were to apply to multi-member LLCs, then not only would a member's ownership interests be subject to levy and sale in satisfaction of a judgment lien, but the non-debtor members of an LLC could find themselves joined by new (and likely unwanted) members.

The amendment to the statute ends this uncertainty. It expressly provides that a "charging order" is the sole and exclusive remedy by which the judgment creditor of a member of a multi-member LLC may satisfy its judgment from the member's interest in, or rights to distributions from, an LLC. The amendment also provides that a charging order is not the sole and exclusive remedy with respect to a single-member LLC so long as the judgment creditor can establish to the satisfaction of the court that distributions under a charging order will not satisfy the judgment in a reasonable time. In addition, the amendment states that nothing in the statute will limit (i) the rights of a secured creditor; (ii) the principles of law and equity that affect fraudulent transfers; (iii) the availability of equitable principles of alter ego, equitable lien or constructive trust or other equitable principles not inconsistent with the statute; or (iv) the jurisdiction of the court to enforce the charging order in a manner consistent with the statute.

Jonathan Galler

Protection from Creditors for Inherited IRAs

In May 2011, Florida amended its IRA protection statute to exempt "inherited IRAs" from claims of creditors. Fla. Stat. § 222.21. The amendment was enacted to clarify existing law and to address the controversial decision of Florida's Second District Court of Appeal in *Robertson v. Deeb*, 16 So. 3d 936 (Fla. 2d DCA 2009).

An inherited IRA is created when a decedent's IRA is transferred to a named beneficiary other than a spouse. The beneficiary of the original IRA typically may either withdraw those funds over a five-year period or transfer those funds to an inherited IRA and receive annual distributions over his or her remaining life expectancy.

In *Robertson*, a judgment creditor served a writ of garnishment upon the trustee of the debtor's inherited IRA. The debtor argued that his beneficial interest in the inherited IRA was exempt under the statute protecting IRAs from the claims of creditors. The court, however, held that the inherited IRA was not to be afforded the same statutory protections as the original IRA because the statute at that time referenced only the original "fund or account." The court determined that because an inherited IRA is treated, particularly for tax purposes, as a completely separate fund or account, it was not covered by the statute.

The *Robertson* decision was subsequently applied in bankruptcy court. *In re: Ard*, 435 B.R. 719 (Bankr. M.D. Fla. 2010). There, the court held that the treatment of an inherited IRA turns on the language of each state's IRA exemption statutes. Citing *Robertson*, the bankruptcy

court concluded that an inherited IRA is not afforded the same protections as a traditional IRA under Florida law and, thus, is not exempt in bankruptcy proceedings either.

The amendment to the statute expressly provides that an inherited IRA will be exempt from the claims of creditors. This is significant not only for Florida residents but also for anyone considering naming a Florida resident as the beneficiary of an IRA because the law of the beneficiary's domicile governs whether the inherited IRA will be protected from creditors.

Proposed Omnibus Trusts and Estates Legislation

In June 2011, Florida enacted omnibus trusts and estates legislation covering a wide range of topics that will be covered in greater detail in our next column. In brief, the bill: (1) amends Florida's evidence code rejecting the concept of a fiduciary exception to the attorney-client privilege; (2) amends certain statutory provisions governing the intestate share of a surviving spouse; (3) authorizes the reformation of a will to correct mistakes and the modification of a will to achieve tax objectives; (4) clarifies that the revocation of a will may not be challenged before the death of the testator; and (5) clarifies that certain payments by a trustee from trust assets are not subject to the 30-day deadline for filing a motion for taxation of fees and costs.

New Power of Attorney Act

In June 2011, Florida enacted a new power of attorney statute, the details of which will be covered in our next column. In brief, the new statute tracks the Uniform Power of Attorney Act but makes certain modifications for consistency with other Florida statutes. Notably, the new act prohibits springing and other conditional powers but permits the appointment of successor agents and co-agents and compensation for qualified agents. The act also requires that new powers of attorney be signed by the principal and two witnesses and be notarized. An exception exists, though, for powers of attorney created and properly executed under the laws of another state. This promotes the Uniform Act's aim of making powers of attorney portable between states. In addition, the act identifies mandatory duties of the agent, including the duty to maintain the principal's estate plan. Along similar lines, the act singles out certain powers that could affect the principal's estate plan, such as making gifts and creating and amending revocable trusts. Each such power may be granted only with additional formalities and is subject to specifically identified restrictions.

CASE LAW UPDATE

Testamentary Forgiveness of Debt

In a case of first impression, Florida's Fifth District Court of Appeal held that forgiveness of debt in a will is a testamentary bequest that may not operate to defeat the payment of obligations and expenses of the estate. The decedent, who had killed his wife, his stepdaughter and himself, died with a single asset: a one-half interest in a promissory note delivered to the decedent by his son. The note was unconditional and did not provide for its cancellation upon the holder's death. The decedent's will, however, unambiguously stated the decedent's intent to forgive the debt upon his death. Consequently, the only legal mechanism available to achieve this intent was to admit the will to probate. For that reason, the court held that the debt forgiveness was a testamentary devise that could not be effectuated until after the satisfaction of claims filed against the estate, including the wrongful death claims of the decedent's wife and stepdaughter.

Lauritsen v. Wallace, 2011 WL 1195873 (Fla. 5th DCA 2011).

Trust Reformation Requires Clear and Convincing Evidence

Florida law permits judicial reformation of the terms of a trust when clear and convincing evidence demonstrates that a mistake of law or fact affected the settlor's intent and the terms of the trust. Fla. Stat. § 736.0415. The clear and convincing standard is an intermediate standard of proof that falls between the "preponderance of the evidence" standard common in civil actions and the "beyond a reasonable doubt" standard of criminal actions. Florida's Third District Court of Appeal affirmed the denial of a petition for reformation where the trial court found that plaintiff had not met this heightened burden even though the scrivener of the trust at issue testified that the grantor never instructed him to establish the gifting priority that his draftsmanship created. The appellate court affirmed the decision, holding that it may not "overturn a trial court's finding regarding the sufficiency of the evidence unless the finding is unsupported by record evidence, or as a matter of law, no one could reasonably find such evidence not to be clear and convincing."

Reid v. Estate of Sonder, 2011 WL 1007137 (Fla. 3d DCA 2011).

Disposition of After-Acquired Assets

How should an estate dispose of assets acquired after the decedent's execution of his will, where the will contains no residuary clause and where the only remaining beneficiary is a specific legatee? Florida's First District Court of Appeal concluded that the statutory presumption against partial intestacy mandates that

the after-acquired property pass to the remaining beneficiary. In an emphatic and lengthy dissent, however, one judge on the panel concluded that the decedent's unambiguous intent should trump the presumption against partial intestacy, and that because the decedent made specific bequests to the named beneficiary and did not provide for the disposition of the residue, the after-acquired property should pass subject to Florida's intestate succession rules.

Basile v. Aldrich, 2011 WL 1496721 (Fla. 1st DCA 2011) (not yet final). *[Editor's note: This opinion was withdrawn and superseded before we went to press. We will report on the new opinion in our next issue.]*

Prudent Investor Standard

A Florida federal court affirmed Florida's commitment to the prudent investor standard in evaluating a trustee's investment conduct. Plaintiffs alleged that the corporate trustee breached its duty because the trust's market value would have been substantially higher had the trustee maintained a different asset allocation. The court granted summary judgment in favor of the trustee because plaintiffs failed to adduce evidence of any actual violation of the terms of the trust and Florida's prudent investor standard is a "test of conduct and not results." Fla. Stat. § 518.11(1)(b). The court also noted that plaintiffs had received quarterly account statements for many years without registering any objections and that the trustee's allocation decisions were the result of substantial requests for corpus distributions by one of the plaintiffs.

Figel v. Wells Fargo Bank, N.A., 2011 WL 860470, 3 (S.D. Fla. 2011).

Personal Jurisdiction Over Corporation Owned by Estate

The court's inherent power to monitor the administration of a Florida estate does not, in and of itself, confer personal jurisdiction over a New York corporation in which the estate has a 50% ownership interest. In a Florida action brought by a personal representative to enjoin a New York corporation from selling its real estate holdings, Florida's Fourth District Court of Appeal held that the complaint failed to allege facts sufficient to satisfy the requirements of Florida's long-arm jurisdiction statute. For example, the complaint did not allege that the corporation regularly conducted business in Florida. The mere fact that the decedent's 50% ownership in the corporation had passed to the estate was insufficient to confer personal jurisdiction over the foreign corporation.

Henderson v. Elias, 56 So.3d 86 (Fla. 4th DCA 2011).

Will Contest Alleging Insane Delusions

Florida courts will not enforce a will that the testator would not have made but for an "insane delusion" regarding one of the objects of her bounty. In a will contest brought by decedent's daughter on this and other grounds, Florida's Fourth District Court of Appeal reversed the trial court's judgment against the daughter and remanded for a determination as to whether the decedent suffered from such an insane delusion. Plaintiff alleged that her mother had substantially reduced her inheritance as a result of a mistaken belief that plaintiff had visited her only once in about ten years. Evidence was presented at trial that plaintiff and her mother had seen each other multiple times within the preceding seven years. But the trial court did not determine whether this contradiction in evidence established an insane delusion or whether the decedent's belief about her daughter's failure to make visits was the reason for the change to her will. The appellate court remanded for the trial court to make findings on the issue based on the existing trial record or after an evidentiary hearing.

Levin v. Levin, 2011 WL 1772245 (Fla. 4th DCA 2011).

David Pratt is a partner in the Personal Planning Department of Proskauer Rose LLP and the head of its Boca Raton office. His practice is dedicated to estate planning, trusts and fiduciary and individual income taxation. Jonathan Galler is a litigator in the firm's Probate Litigation Group, representing corporate fiduciaries, individual fiduciaries and beneficiaries in trust and estate disputes. The authors are members of the firm's Fiduciary Litigation Department and are admitted to practice in Florida and New York.

Trusts and Estates Law Section
Visit on the Web at www.nysba.org/trusts

Surrogate's Court Seeks Volunteer Attorneys for Article 17-A Proceedings

By Lori J. Perlman

The court system has suffered from the economy in the same way that many government agencies have and has lost staff in the process. In New York County (and probably others as well), guardianship proceedings for mentally and developmentally disabled persons were previously handled by the court attorney staff, but they are no longer in a position to do so. The Surrogate's Court is in need of attorneys to volunteer to handle these matters.

Attorneys do not have to be qualified as certified GALs to serve. The Surrogate's Court has discretion to select attorneys who are not on the certified GAL list when there is a need to do so, and Surrogate Nora Anderson has indicated that this is one of those circumstances. Attorneys also do not have to have prior experience with Article 17-A cases.

These types of guardianship proceedings typically involve speaking with the petitioner to obtain the facts regarding the case, meeting with the incapacitated person, confirming that he or she is in need of a guardian and reporting conclusions to the court. The court should be in a position to provide sample reports that attorneys can use as a guide to the services that they should be providing and the substance of reports. In cases where the proposed guardian is a parent, no hearing is required. In other cases, there may be a hearing before a judge. Attorneys can specify whether they are in a position to handle a hearing, but prior litigation experience is not required.

While these are true pro bono cases in the sense that they will likely not involve any compensation, serving as a GAL can provide valuable in-court experience, particularly for more junior attorneys.

If your law firm has a pro bono coordinator, please feel free to pass this request along to him or her. If you are interested in serving as an Article 17-A GAL, please send a letter to Surrogate Anderson indicating that you are interested (and whether you prefer to start with a case that does not require a hearing) to the following address:

Surrogate Nora S. Anderson
New York County Surrogate's Court
31 Chambers Street
New York, New York 10007

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Trusts and Estates Law Section
Program Reception and Luncheon

Wednesday, January 25, 2012

Save the Dates

Contradictory Beneficiary Designations in Will and IRA Form

Subject: Testator names one child as beneficiary of IRA in Will but different child on IRA form

Date: Friday, June 10, 2011 9:32 a.m.

To: Trusts and Estates Law Section

Dear Colleagues:

I am looking for your opinion or reference to any law on this one to confirm what I think is true.

Testator names Child A as the sole beneficiary of her IRA on the IRA form. However, Testator names Child B as the sole beneficiary of the same IRA in her Will. Therefore, she names two different children to be the sole beneficiary of her IRA: one on her IRA form and one under her Will. I believe that the beneficiary of the IRA "trumps" the designation in the Will and therefore Child A would receive the IRA, not Child B.

Any thoughts are greatly appreciated.

Thanks.

Very truly yours,

Bosco Law Firm, LLC
By: Damien Bosco, Esq.
110 Wall Street, 11th Floor
New York, New York 10005
(212) 709-8203
dbosco@boscolegal.com
www.boscolegal.com

Subject: Re: Testator names one child as beneficiary of IRA in Will but different child on IRA form

Date: Friday, June 10, 2011 10:05 a.m.

To: Trusts and Estates Law Section

Damien,

I had a case similar to these facts a couple of years ago with IRA designations being inconsistent with the overall testamentary plan and the bequests in the will—a year of litigation. Although it seems to me that the IRA is a contract and the designation, unless procured by fraud or undue influence, should arguably stand against the bequest to the child named in the Will, the child named in the Will now has at least a toehold for a will contest or action against child A regarding the IRA beneficiary designation. Who's to say that there isn't a later or earlier IRA beneficiary designation form naming child B, that child A by nefarious means got the decedent to change the designation, or that child A destroyed the other designation form?

Ian

Ian W. MacLean
The MacLean Law Firm, P.C.
100 Park Avenue, 20th Floor
New York, NY 10017
T: 212-682-1555
F: 212-682-6999

Subject: Re: Testator names one child as beneficiary of IRA in Will but different child on IRA form

Date: Friday, June 10, 2011 12:03 p.m.

To: Trusts and Estates Law Section

Damien,

You may want to look at EPTL section 13-3.2(a). It states in relevant part that the rights of the beneficiaries named on a retirement plan "shall not be impaired or defeated by any statute or rule governing the transfer of property by will, gift or intestacy." Thus, you are correct to say the beneficiary named on the IRA "trumps" that of the person named on the will.

Best Regards,

Angelica M. McKessy
Attorney at Law
Garden City, New York

Subject: Re: Testator names one child as beneficiary of IRA in Will but different child on IRA form

Date: Friday, June 10, 2011 5:17 p.m.

To: Trusts and Estates Law Section

One might attempt an argument under EPTL 7-5.2 if the Will had a later date that the designation was revoked.

I agree with Ian that the IRA is a contract and should prevail but obtaining the history of changes, dates, notes of Will drafter, etc. might permit an attack. As with so many of these—how much $$$$ is at stake will drive the decision.

John J. Wadlin, Esq.
RUSK WADLIN HEPPNER & MARTUSCELLO LLP
PO Box 3356
255 Fair Street
Kingston, NY 12402
Tel 845-331-4100
Fax 845-331-6930

Subject: Re: Testator names one child as beneficiary of IRA in Will but different child on IRA form

Date: Friday, June 10, 2011 6:58 p.m.

To: Trusts and Estates Law Section

There was a decision in NY Surrogate's Court about 6 years ago where Preminger ruled the beneficiary designation in the will trumped the signed beneficiary designation. The case was *Matter of Trigiboff.*

The judge based her decision on another matter involving life insurance proceeds. That case held that by use of an interpleader and depositing the proceeds with the court, the insurance company waived the terms of the policy. The problem in *Trigiboff* was the brokerage firm was still holding the proceeds.

I believe it was settled without an appeal but another of the key cases the judge relied on was later reversed by the Court of Appeals. There are several law review articles out there.

Steve Silverberg

Refusal by Nominated Executor to Probate Will

Subject: Proposed Executor Refuses to Probate Will

Date: Thursday, May 5, 2011 9:29 a.m.

To: Trusts and Estates Law Section

MATES:

Mother passes in January 2011 leaving 5 adult issue and no spouse. A few months prior to death (long illness with imminent death) she gave copies of will to 2 children and original to sister A, proposed executor. To date sister A unwilling to cooperate with others and has refused to probate will without explanation.

QUESTION: Can others compel probate and/or production of original will? How? Procedure? Statute(s)?

If she denies having will and original not located, can Administration proceeding be commenced despite knowledge will existed and unlikely that testator revoked her will?

Thank you for any feedback.

Jeff

St. Clair & Associates
by Jeffrey A. St. Clair
26 Court Street
Brooklyn, NY 11242
718-596-4466

Subject: Re: Proposed Executor Refuses to Probate Will

Date: Thursday, May 5, 2011 9:33 a.m.

To: Trusts and Estates Law Section

Compel production of Will: SCPA 1401.

Who may petition for probate (propound a will): any legatee, devisee, etc.: SCPA 1402.

If original will not produced, may commence a "Lost Will" proceeding: SCPA 1407.

Scott McBride

Subject: Re: Proposed Executor Refuses to Probate Will

Date: Thursday, May 5, 2011 11:14 a.m.

To: Trusts and Estates Law Section

To expand on Scott's statutory references:

First step is to compel production of the original Will, which is required in order to file for probate. In response, either the sister will file the Will for probate or will be required to file it with the Court.

Then anyone who has an interest can probate the Will.

I would first send the sister a letter informing her that if she does not commence probate or file the original Will in Court, you will be commencing the proceeding to compel production of the Will, in which you will seek to have the costs of the proceeding paid by sister. Also, inform the sister that it is a misdemeanor to intentionally withhold a Will. (It is somewhere in the Penal code, in one of the "unspecified other" offenses section.) Perhaps that will get her moving without needing to commence litigation.

Lori Perlman

Subject: Re: Proposed Executor Refuses to Probate Will

Date: Thursday, May 5, 2011 11:30 a.m.

To: Trusts and Estates Law Section

Just to clarify what Lori said, unlawfully concealing a will is a Class E Felony.

Here is the statute from the Penal Law:

> § 190.30 Unlawfully concealing a will.
>
> A person is guilty of unlawfully concealing a will when, with intent to defraud, he conceals, secretes, suppresses, mutilates or destroys a will, codicil or other testamentary

instrument. Unlawfully concealing a will is a class E felony.

I agree that the first step should be to send a letter to the sister indicating that if she does not file the original will with the Court, you will seek costs against her. If she refuses, the proceeding to compel the production of the will is fairly simple.

Good luck.

John P. Graffeo
Novick & Associates, P.C.
202 East Main Street, Suite 208
Huntington, New York 11743
Ph: (631) 547-0300
Fx: (631) 547-0212

Step Up in Basis for Trust Property

Subject: Step Up of Basis for Defective Grantor Irrevocable Trust

Date: Tuesday, June 21, 2011 2:17 p.m.

To: Trusts and Estates Law Section

Dear Listserve:

I am trying to figure out if a Grantor Irrevocable Trust can receive a 50% step up in basis on real property that was transferred to the Trust by the individual Grantors (H&W), who reserved, in effect, a life estate so long as the property remained their primary residence, until the last Grantor dies.

The H died in 2010 and the Trust is contemplating selling the real property and purchasing a different residence for the survivor. (The trust allows the property to be sold with the proceeds used to purchase personal residence for the Grantors or the survivor of them.) The Trust ends upon the last Grantor's death.

If the house is sold now, can the Trust receive a 50% step up in basis due to the death of the first grantor, even though the second grantor is still alive, and the house is therefore still subject to (in effect) a life estate?

TIA

Regards,
Eileen

Eileen D. Stier, Esq.
Busell & Stier, PLLC
98 Cutter Mill Road, Suite 395N
Great Neck, NY 11021
Tel: 516-829-9595
Fax: 516-829-9617

Subject: Re: Step Up of Basis for Defective Grantor Irrevocable Trust

Date: Saturday, June 25, 2011 3:36 p.m.

To: Trusts and Estates Law Section

Yes, in my opinion you can take the position that the grantor retained a life estate and that the property is thus includable in the grantor's estate under IRC 2036 and thus stepped-up under IRC 1014. In addition if a special power of appointment was reserved the step-up is available under IRC 1022(e) which provides the step-up to trust property to which " the grantor reserves the right to make any change in the enjoyment thereof."

Thomas F. O'Connell, Esq.
144 E. Central Ave.
Pearl River, NY 1 0965
Phone: 845 735 5050
Fax: 845 620 0722

Subject: Re: Step Up of Basis for Defective Grantor Irrevocable Trust

Date: Saturday, June 25, 2011 4:20 p.m.

To: Trusts and Estates Law Section

Eileen—Also, although you only asked about the step up in basis, don't forget that pursuant to IRC 121(b)(4), the exclusion would be $500K if the property is sold within 2 years of the husband's death.

Paul Hyl, Esq.

Transfer to Trust Not Yet Executed by Trustee

Subject: Effective date of deed into a trust

Date: Wednesday, June 8, 2011 4:01 p.m.

To: Trusts and Estates Law Section

Dear Listmates:

Grantor signs a Trust and Deed on January 1 and the Trustee signs the Trust on January 30—what is the effective date of transfer?

Thanks,
Remo Hammid

Subject: Re: Effective date of deed into a trust

Date: Monday, June 13, 2011 4:26 p.m.

To: Trusts and Estates Law Section

Follow up:

I thought I'd share the responses I received to my query given the divergent points of view that were sent to me privately:

The majority felt that the transfer was valid but on the date the Trustee signed the trust (this was the view of counsel at a title company as well).

A small number thought that the transfer was made as of the date the Grantor signed.

One person, however, questioned whether the transfer was valid at all.

Thank you,
Remo Hammid

Subject: Re: Effective date of deed into a trust

Date: Wednesday, June 15, 2011 1:13 p.m.

To: Trusts and Estates Law Section

I was the sole person who thinks the deed may be ineffective. The deed should be made out to the trustee, as trustee under the NAME OF TRUST dated _____, 20__. If the deed was made out to the trust itself and not the trustee, it is invalid. If in your circumstance, the deed was to JOHN DOE, as trustee under the NAME OF TRUST dated ____, 20__ [which was subsequently filled in], it is still most likely ineffective since the trust was not effective.

I think you should speak with a reputable title company attorney. They should be able to give you a definitive answer.

Christopher D. McDonald, Attorney
Law Office of Mitchell Mund
100-15 Queens Blvd. - Suite #1
Forest Hills, NY 11375-2452
Telephone: (718)261-6863
Facsimile: (718)261-5709
E-mail: MitchellMund@aol.com

Subject: Re: Effective date of deed into a trust

Date: Friday, June 17, 2011 10:03 a.m.

To: Trusts and Estates Law Section

A conclusion to the query:

Counsel at two separate title companies have advised that the transfer would be effective on the date the trustee signs, in this case, January 30. To be clear about the circumstances of the transfer, both advised that the deed be dated "as of January 30, the date of delivery," but the notary provision will remain Jan 1.

The risk that they both saw was if the Grantor were to die after signing the deed but before delivery to the Trustee.

Thanks to all who responded publicly and privately.

Remo Hammid

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Pierce McDowell
(605) 338-9170
piercemcdowell@sdtrustco.com

Al King
(212) 642-8377
alking@sdplanco.com

James Paladino
(212) 642-8377
jamespaladino@sdplanco.com

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Scenes from the
Trusts and Estates Law Section Spring Meeting
April 7-10, 2011
Turnberry Isle, Florida

Parrots were on hand for the cocktail reception

Surrogates Nora Anderson, Barbara Howe and Ava Raphael

Fred Honnold, Section Chair Betsy Hartnett and Ami Longstreet

Christine Dettor, Mary Anne Cody and Marty Schwab

Tennis chair Wally Leinhart, Paul Callaway and Frances Pantaleo

Carl Baker and Meeting Co-Chair Michael Connor

Alan Acker

Carlyn McCaffrey

Victoria Richardson, Surrogate John Czygier and Section Chair-Elect Ilene Cooper

Micky Ordover and Colleen Carew

Meeting Co-Chair Ian MacLean

Ira Bloom, Raymond Radigan, Stacy Zolotin and guest

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Judge Radigan will focus his considerable experience and skills on resolving Surrogate's Court and Trust & Estate disputes, assisting attorneys and litigants to achieve prompt resolution to their complex matters.

Joining Judge Radigan as mediators will be:

- **Michael K. Feigenbaum** - Co-chair of the Trusts & Estates Department and a member of the Executive Committee of the Trusts and Estates Law Section of the New York State Bar Association as well as chair of the NYSBA Committee on Practice and Ethics and former chair of its Government Relations Committee. Mr. Feigenbaum is also former president of the Queens County Bar Association. He is a fellow of the American College of Trust and Estate Counsel, a national association of lawyers skilled and experienced in estate planning and trust and estate administration.
- **Peter K. Kelly** - A former member of the staff of the Nassau Surrogate's Court, Mr. Kelly served as Law Secretary to Judge C. Raymond Radigan and later as a Court Attorney/Referee. Prior to joining the Surrogate's Court, Mr. Kelly was Law Secretary to the Hon. Raymond Harrington, then Acting Nassau County Surrogate. Mr. Kelly was most recently President of the New York State Surrogate's Law Association.

For more information on our T&E Mediation Services, please contact Judge Radigan's office at 516-663-6602 or crayradigan@rmfpc.com

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Recent New York State Decisions

By Ira M. Bloom and William P. LaPiana

Ira M. Bloom

ADOPTION

Precautionary Addendum Does Not Apply Because Adopted Remaindermen Supersede Birth Relations Who Would Take in Intestacy

Decedent died in 1924. His will created five testamentary trusts, one for his wife and one for each of his four children. The trusts for his children provided for the distribution of one-half of the trust principal to each child when he or she reached 45 years of age, payment of all income from the remaining half to the child until death and remainder to the child's issue, per stirpes. If the child died before age 45, the trust principal was to be paid to the child's issue, per stirpes, and if none to the child's surviving siblings and the issue of deceased siblings, per stirpes. The terms of the trust made no disposition of the trust property should a child die after 45 years of age without surviving issue. Eighty-one years after the decedent's death, his last child died at age 96, survived by an adopted child and the children of a predeceased adopted child.

Now-repealed N.Y. Domestic Relations Law § 114, known as the "precautionary addendum," effectively provided that adopted children were not children of their adoptive parents "so as to defeat the rights of remaindermen" who would take "under the provisions of any instrument" should the adopting parent die without heirs. The statute applies only to wills of decedents dying before its repeal on March 1, 1964, and it applied to the testamentary trust at issue because the decedent died in 1924. In deciding the trustee's application for a construction determining the identity of the remaindermen, Surrogate Glen held that the adopted children of the income beneficiary were her issue and remaindermen of the trust. First, the Will had no provisions dealing with adopted persons, and no extrinsic evidence as to the decedent's intent in this regard was offered, so the adopted children were indeed the child's issue for purposes of the Will so long as the precautionary addendum did not apply.

Second, the Surrogate determined that the lack of a provision dealing with the death of a child after age 45 without surviving issue did not justify the creation of a gift by implication to the issue of the child's deceased siblings. The existing provisions did not indicate that the testator necessarily intended to make the same distribution if the child died after age 45 without surviving issue or before that age without surviving issue. Therefore the trust property would pass in intestacy if a child died after age 45 but without surviving issue.

William P. LaPiana

Third, the precautionary addendum did not apply because the birth relatives of the decedent would take not under the provisions of the trust but instead through the intestacy distribution resulting from the testator's failure to make any provision for the remainder under these particular circumstances. Therefore, the adopted child and descendants of the predeceased adopted child were entitled to the trust remainder. *Matter of Claman*, 31 Misc.3d 852, 919 N.Y.S.2d 810 (Sur. Ct. New York Co. 2011).

DEAD BODIES

No Liability for Crematorium and Funeral Home Acting Reasonably Under PHL § 4201

Decedent was cremated on the authority of an authorization signed by his apparent surviving spouse. Subsequently the decedent's issue and their mother (Mack), who claimed to be the decedent's lawful spouse at the time of his death, brought an action against the hospital where the decedent died, the funeral home and the crematorium claiming damages for loss of the right of sepulcher. The Supreme Court granted the hospital's motion for summary judgment, citing the New York City Health Code (24 RCNY 205.19), but denied the summary judgment motions of the funeral home and crematorium based on recently enacted N.Y. Public Health Law § 4201 (PHL). The crematorium appealed and the Appellate Division reversed.

The court noted that PHL § 4201(7) protects anyone who acts reasonably and in good faith on the authority of a person representing himself or herself as authorized to control disposition of the decedent's remains. Because the purported surviving spouse presented the crematorium with an authorization which on its face

satisfied PHL §4201(7) and with a certified copy of a certificate of marriage identifying her as the decedent's spouse, the crematorium acted reasonably and in good faith in carrying out her instructions. Moreover, the plaintiffs presented no evidence that Mack's marriage to the decedent had not been dissolved, and their complaint was verified by someone other than Mack without any showing that this individual had personal knowledge of Mack's marital status. Finally, the court noted that it had the authority to search the record and award summary judgment to a nonappealing party with respect to an issue that was the subject of the motions before it. Accordingly, the court searched the record and granted the funeral home's initial summary judgment motion in the interest of judicial economy even though it had not appealed. *Mack v. Brown*, 82 A.D.3d 133, 919 N.Y.S.2d 166 (2d Dep't 2011).

SURROGATE'S COURT

Surrogate Court Had Jurisdiction over Action Involving Lifetime Trust Property

Decedent created a lifetime trust and funded it with her condominium and a brokerage account. At her death, the trust was to terminate and the trust property to be distributed equally to her son and daughter, who were also co-trustees. After the decedent's death, her daughter obtained voluntary letters of administration. Previously the son had commenced a proceeding in Supreme Court seeking partition of the condominium or alternatively, sale of the decedent's property and division of the proceeds. The daughter's motion to transfer her brother's action to Surrogate's Court was granted on the grounds that the matter was "intertwined" with issues relevant to the administration of the decedent's estate. Almost two and a half years later, the brother moved in Supreme Court to vacate the transfer to Surrogate's Court based on lack of subject matter jurisdiction with respect to the distribution of the assets of the lifetime trust. The motion was denied, and the brother appealed. The Appellate Division affirmed in an opinion thoroughly analyzing the sources of Surrogate's Court jurisdiction over lifetime trusts. *Wagenstein v. Shwarts*, 82 A.D.3d 628, 920 N.Y.S.2d 55 (1st Dep't 2011).

WILLS

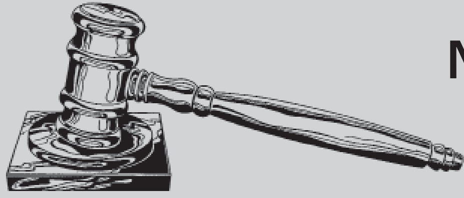
Joint Will Is Binding but Does Not Prevent Probate of Subsequent Will

Decedent and her then-husband executed a joint will which provided that on the death of the first to die all of the decedent's estate and all property over which the decedent had "the power of disposal, whether owned jointly or severally" passed to the survivor. On the death of the survivor, the estate passed into a trust, one share of which was for the benefit of one of the couple's daughters, the other share for their grandchildren. The couple divorced after 50 years of marriage, and in the settlement agreement incorporated into the divorce decree they reaffirmed the joint will. After the divorce, the decedent created an irrevocable trust over the condominium she had received under the settlement agreement. Crucially, she retained a special testamentary power of appointment over the trust. She then executed a will wherein she exercised the power of appointment in favor of her and her ex-husband's four children. This will also affirmed the joint will.

Both the joint will and the subsequent will were offered for probate. Seeking to obtain the condominium pursuant to the terms of the joint will, the ex-husband commenced a turnover proceeding against the surviving trustee of the irrevocable trust and moved for summary judgment, which Surrogate Riordan granted. The Surrogate also denied probate to the later will purporting to exercise the power of appointment.

The Appellate Division affirmed the grant of summary judgment in the turnover proceeding. The court thoroughly analyzed the joint will and concluded that the longstanding marriage and the reaffirming of the joint will in the divorce decree meant that the decedent by retaining the testamentary power of appointment over the condominium did have a "power of disposal" over the condominium even though she did not own it "jointly or severally." The court reversed the denial of probate of the later will, holding that a validly executed will is entitled to probate even though its terms are not enforceable. *Matter of Murray,* 84 A.D.3d 106, 921 N.Y.S.2d 161 (2d Dep't 2011).

Ira Mark Bloom is Justice David Josiah Brewer Distinguished Professor of Law, Albany Law School. William P. LaPiana is Rita and Joseph Solomon Professor of Wills, Trusts and Estates, New York Law School. Professors Bloom and LaPiana are the co-authors of Bloom and LaPiana, *Drafting New York Wills And Related Documents* (4th ed. LexisNexis).



Case Notes— New York State Surrogate's and Supreme Court Decisions

By Ilene Sherwyn Cooper

Ancient Will

In an uncontested probate proceeding, the court was asked to admit a will that was 19 years old under the common law "ancient document" rule, which allows probate of a will of a certain age where all of the witnesses are unavailable or cannot be located to testify in support of the instrument. The court noted that a will may be admitted to probate as an ancient document only if it is more than 30 years old, or at least more than 20 years old under the more liberal federal rule, and the will in question did not meet these requirements.

Nevertheless, while the propounded will did not qualify as an ancient document, the court held that the will could be admitted to probate upon proof of the signatures of the decedent and one of the attesting witnesses, pursuant to N.Y. Surrogate's Court Procedure Act 1405(4) (SCPA). The court noted that one of the witnesses was the attorney-draftsman of the instrument, who died testate in the county, and thus an exemplar of his signature was on file with the court. The court concluded that an affidavit of a handwriting expert that the two signatures were the same would suffice to prove his signature on the propounded will. In addition, the court concluded that an affidavit of one of the decedent's children or more remote relatives as to her signature would satisfy the court that her signature was genuine.

In re Santoro, 2011 NY Slip Op. 50920U.

Attorney-Client Privilege

In a probate proceeding, the beneficiaries under a prior will of the decedent sought discovery pursuant to the provisions of SCPA 1404. They demanded the production of all drafts and versions of the propounded will, including handwritten notes and markups, copies of prior wills and codicils and all correspondence, memoranda and notes. The attorney-draftsman produced responsive documents and a privilege log of 46 pages of documents that he claimed were protected by the attorney-client privilege or attorney work-product privilege. The respondents moved to compel compliance. The court held that for a document to fall within the attorney-client privilege, it must be shown that a communication was made and retained in confidence, and that it was made principally to assist in obtaining or providing legal advice or services for the client. By comparison, the work-product privilege encompasses documents that naturally would be considered the product of an attorney's work, such as notes reflecting interviews, mental impressions and personal beliefs and statements.

Nevertheless, the court noted that the provisions of N.Y. Civil Practice Law & Rules 4503(b) (CPLR) create an exception to the foregoing precepts in the context of probate proceedings. Based upon these provisions, the court ordered production of some, but not all, of the materials demanded.

In re Kirk, N.Y.L.J., 5/26/11, p. 25 (Sur. Ct., N.Y. Co.) (Surr. Glen).

Confidential Relationship

In *In re Moles,* the preliminary executors of an estate moved for summary judgment dismissing the objections of the decedent's nephew, who was the beneficiary of a prior will executed thirty years earlier than the propounded instrument. The objections alleged that the propounded will was not duly executed, that the decedent lacked testamentary capacity on the date of its execution and that it was procured by the fraud and undue influence of the decedent's longtime companion, who was the sole beneficiary of the estate and the named executor along with the attorney-draftsperson.

The undisputed record revealed that the decedent had a history of alcohol abuse for which she was hospitalized and later treated. Upon completion of her rehabilitation, she returned to New York City, where she retained the services of a personal aide who resided with her until her death twenty years later.

Over the course of her employ, the decedent's aide assisted her with medical issues that arose as a result of her Crohn's Disease, including accompanying her to doctor's appointments and visiting her when she was hospitalized. There was no dispute that the decedent and her aide became inseparable, spending every day together and traveling domestically and overseas. Further, there was no dispute that the decedent was capable of making financial and personal decisions regarding her investments and health care.

The decedent's treating physician testified that she always found the decedent fully responsive and rational. This was substantiated by the attorney-draftsman of the propounded will, who testified that he found the decedent alert, coherent and able to convey detailed information regarding her life situation and family. Specifically the draftsman testified that when discussing the provisions of her will, the decedent expressed strong affection for her aide and wanted her to be the sole beneficiary of her estate.

Notably, the will execution was videotaped and supervised by the draftsman's colleague.

In granting the proponents summary relief, the court found that sufficient proof had been submitted to establish a prima facie case on the issues of due execution and testamentary capacity. On the issue of testamentary capacity, the court relied upon the self-proving affidavits of the attesting witnesses, as well as the testimony of the attorney-draftsman and his colleague that the decedent was fully aware and competent at the time the will was executed. Further, the court found compelling the videotaped execution ceremony which revealed that the testator was alert, spontaneous in her responses to questions and cognizant of the identity of her distributees and the dispositive provisions of her will.

The court rejected the notion that the testator's earlier alcoholism impaired her capacity to execute a will, as well as the testimony of the videographer relied upon by the objectant that the testator had difficulty identifying the President of the United States. The court held that this evidence paled in light of the reports and testimony of the professionals who treated and worked with the testator during the period surrounding the execution of the will, all of which indicated that she possessed the minimal capacity required to make a valid will.

The court also rejected the objectant's claims regarding the due execution of the instrument, finding that he had failed to overcome the presumptions of regularity arising from the fact that the execution was attorney-supervised and that the will had an attestation clause.

As to the issue of undue influence, the court concluded that the objectant had failed to submit any evidence that the testator's aide had compelled or constrained the testator to do anything against her free will. In fact, the objectant admitted that he saw the testator at most once or twice a year and that her other family members rarely visited her.

The court found it significant that the attorney-draftsman testified that the provisions of the will were derived from instructions given to him by the testator with no involvement of the testator's aide. To this extent, the court opined that the lack of involvement by the proponent in a will's drafting and execution is inconsistent with an inference of undue influence, even where the disinherited party is a close family member. Further, the court held that even assuming the existence of a confidential relationship between the proponent and the testator, it was counterbalanced by the evidence of the strong affection between the testator and the proponent during their twenty-year relationship, the testator's expressed desire to leave her aide her entire estate and her aide's lack of involvement in the drafting of the will.

Finally, the court concluded that the objectant had failed to produce a modicum of proof that anyone induced the testator to execute her will based upon a false statement.

Accordingly, the objections to probate were dismissed.

In re Moles, N.Y.L.J., 4/18/11, p. 23 (Sur. Ct., N.Y. Co.) (Surr. Anderson).

Discovery Proceedings

Before the Appellate Division, Third Department in *In re Curtis* was an appeal from an order and decree of the Surrogate's Court, Rensselaer County (Hummel, S.), which partially granted the petitioner's application to compel the delivery of property from the fiduciary, and from a decree of that court judicially settling the fiduciary's accounting. The parties were the decedent's daughters and co-executors of her estate. Prior to the decedent's death, the decedent moved in with one of her daughters, who became her attorney-in-fact. Acting in this capacity, the daughter transferred assets of the decedent into her own name.

After the decedent's death, the decedent's other daughter compelled her sister to account as attorney-in-fact and as co-executor of the estate. Both accountings were submitted and objections were filed. At the bench trial, the petitioner only pursued objections to the respondent's accounting as attorney-in-fact, alleging that the transfers of assets by the petitioner to herself were the result of self dealing and breach of fiduciary duty. The Surrogate's Court disagreed, concluding that the respondent's actions were undertaken with the express consent of the decedent, who was found to be competent at the time. The Appellate Division affirmed.

The court held that while there was a presumption that the services provided by respondent's husband in connection with the sale of certain realty were gratuitous in nature, that presumption was sufficiently rebutted by the testimony of the respondent and her husband. To this extent, the court deferred to the Surro-

gate's assessment of the witnesses' credibility and expressly noted that the petitioner put forth no evidence to contradict the evidence presented.

Moreover, the court found that the transfer of the decedent's investment account to the respondent, and respondent's inclusion as a mortgagee upon the sale of the decedent's home, constituted valid gifts, albeit made by the respondent as the decedent's attorney-in-fact. The court relied on the language of the power of attorney which authorized the making of the gifts at issue, as well as the testimony of the respondent who stated that the decedent was present when the subject transactions occurred.

In re Curtis, 2011 NY Slip Op. 027773 (3d Dep't).

Precautionary Addendum

In a final accounting proceeding, the issue before the court was whether the adopted child of the decedent's daughter could inherit as a remainder beneficiary of a testamentary trust.

The decedent died in 1934 survived by her daughter. Under her will, she left her residuary estate in trust to her daughter for life and provided that upon her death, the remainder would pass to her daughter's surviving children or their issue. Approximately three years after the decedent's death, her daughter had a child. Ten years later, the daughter adopted a child. The daughter died in 2007, and the trust for her benefit terminated by its terms.

The trustee maintained that the remainder of the trust could be distributed only to the daughter's natural child by virtue of the "precautionary addendum" principle under former Domestic Relations Law § 117. This statute prohibited adoptees from receiving a remainder interest so as to defeat the rights of remainder beneficiaries who would otherwise take under the terms of an instrument. (The repealed statute applies to trusts under wills executed before March 1, 1964.) The adopted child objected, and both parties moved for summary judgment.

In finding for the objectant, the court relied upon the decision in *Matter of Park,* 15 NY2d 413, which held that the precautionary addendum rule applies only in the case of an adoptive parent dying without any natural heirs. The court reasoned that since the decedent's daughter would not have died without issue even in the absence of the adoption in question, any argument based on the precautionary addendum rule had to fail. Further, the court held that there was nothing in the record to offset the presumption that the testator had intended to include adoptees when she directed that the trust remainder pass to her daughter's children.

In re Cook, decided January 19, 2011 (Sur. Ct., N.Y. Co.) (Surr. Glen).

Probate

In *In re Marin,* the Appellate Division, Second Department, affirmed a decree of the Surrogate's Court, Putnam County (DiBella, S.), which, among other things, determined that the propounded will was duly executed and was not the product of fraud or undue influence.

The decedent died at the age of 77 survived by five children—three daughters and two sons. She left a handwritten instrument purporting to be her last will and testament, which she executed before a notary public and two witnesses on June 26, 2000. The instrument appointed her two sons the executors of her estate, bequeathed certain real property to two of her daughters and left the residue of her estate to her two sons and her third daughter. The decedent's two sons petitioned for probate of the instrument, and objections were filed by one of the decedent's daughters on the grounds, among other things, of lack of due execution, fraud and undue influence.

Based on the testimony of the notary public and the witnesses to the instrument, each of whom knew the decedent well, the court held that the propounded will had been duly executed. The court found that although one of the witnesses could not recall whether the decedent's signature appeared on the will at the time she signed it, the Surrogate's Court had properly found that the decedent had acknowledged her signature to the witness.

Further, the court concluded that the objectant had failed to establish that the will was the product of fraud (i.e., that it was the result of false statements made to the decedent that caused her to dispose of her property in a manner differently than she would have), or that undue influence had been exerted by the petitioners upon the decedent.

In re Marin, 2011 NY Slip Op. 02011 (2d Dep't).

Undue Influence

In *In re Carter,* the court found that undue influence required that the propounded will be denied probate. The facts of the case are in stark contrast to those in *Moles* and account for the different outcomes.

In *Carter,* the propounded will left the testator's entire estate, except 25% of any cash due and owing to the testator's sole surviving heir (the decedent's sister), to a complete stranger (Frazier) who was also named the executor. The instrument also directed that in the event the testator's sister was admitted to a nursing home, her share should pass instead to Frazier and that Frazier pay an amount, not to exceed 11% of the residuary estate, to charities of his choice.

The record revealed that Frazier was 40 years younger than the testator, was unrelated to the testator, was her self-described caretaker and was an instrumental force behind the execution of the propounded will. The court held that under these circumstances, as well as events described in its own files and through the testimony of Frazier, an inference of undue influence existed, requiring a hearing. Notably, the court found that Frazier had previously been appointed as fiduciary in a number of other estates of women significantly older than him, and with whom he had no family relationship, that were strikingly similar to the factual situation involving this testator.

Based on the testimony and evidence adduced at the hearing, the court concluded that Frazier had engaged in a systematic course to take over the personal and financial affairs of the testator, whom he knew had been diagnosed with dementia, much as he did in the case of countless other elderly and frail women with whom he ingratiated himself. He moved into the testator's home, put his name on her bank accounts, monitored her telephone calls, put her under surveillance and held her health care proxy. Significantly, the record also disclosed that in 2006, when the testator was overtly suffering from mental illness and when no attorney would draft a will for her, he acceded to her alleged insistence on executing a new will by retyping a prior will of the testator, with the testator's handwritten changes, and taking the testator to her doctor's office to have it signed and witnessed.

At the conclusion of the hearing, the Attorney General recommended that the propounded will be denied probate. The court agreed, finding that the purported will had not been duly executed, that the testator lacked capacity on the date of its execution and that it was the result of undue influence.

Specifically, the court concluded that Frazier's testimony gave rise to a strong inference of undue influence, based in particular upon his complete insinuation into the testator's life and financial affairs, the testator's dependence upon him for her basic needs and his involvement in the preparation and execution of the instrument that made him the primary recipient of her estate. The court held that Frazier offered nothing to rebut this proof, but rather buttressed the conclusion that the will of the testator was the product of his own decision-making and control over its preparation and execution.

Additionally, the court held that the record failed to support any claim that the testator had the capacity to execute her will, especially given the proof that at or about the time the will was executed she suffered from confusion, was described by her neighbors as acting oddly, allowed a total stranger to have access to her personal finances and her daily most intimate health care needs and that the will was inconsistent in its terms.

Finally, the court found that Frazier had failed to prove that the will had been duly executed, that the testator ever read the will, that she ever declared the instrument to be her will or that the witnesses signed at her request.

Accordingly, probate was denied.

In re Carter, N.Y.L.J., Apr. 18, 2011, p. 25 (Sur. Ct., Kings Co.) (Surr. Torres).

Waiver and Consent

In a probate proceeding, the decedent's son, who was his sole distributee and sole income beneficiary of a testamentary trust, sought, among other things, to withdraw his waiver and consent to probate in order to conduct SCPA 1404 examinations and file objections to probate, if appropriate.

The propounded instruments were a will and a codicil, both of which were drafted by an attorney. The execution of the instruments was attorney-supervised and was witnessed by three persons who executed self-proving affidavits.

Pursuant to the pertinent provisions of his will, the decedent left his tangible personal property to his son and the residue of his estate in trust for the benefit of his son during his son's lifetime, and upon his death, the remainder to his grandchildren. The trustees of the trust had liberal invasion powers for the son's benefit.

In support of his application to vacate his waiver, the son maintained that at the time he executed the waiver and consent he did not have a copy of the will or codicil and was not represented by independent counsel, and that he had a good faith basis for objecting to probate, inasmuch as the decedent had a limited education, could barely read and write English and likely did not understand the terms of his will. In opposition to the application, the preliminary executors of the estate argued that the decedent's son insisted that the decedent execute a codicil to his will upon the birth of his youngest child and arranged for the preparation and execution of the instrument. Moreover, they argued that the son and his wife were present when the codicil, which restated the will, was signed, and had two meetings with the preliminary executors after death at which time the terms of the instruments and the probate process were discussed.

The court held that in order to withdraw a waiver and consent to probate, a party must demonstrate that the potential objections to probate have a reasonable

probability of success on the merits, notwithstanding the more relaxed proof required when the application is made prior to decree. Based upon the record, the court noted that the application by the decedent's son to withdraw his waiver and consent was made seven months after the waiver was signed. Moreover, the court found it significant that the execution of the will was supervised by an attorney, that there were self-proving affidavits, that there was no proof of undue influence or lack of capacity and no other interested person took issue with the probate of the instruments. Furthermore, the son did not dispute the fact that he had met with the preliminary executors and was informed about the probate process and the terms of the instruments.

Accordingly, the court held that the son had failed to demonstrate any merit to or likelihood of success on his potential objections to probate, and therefore the application was denied.

In re Gee, N.Y.L.J., Mar. 1, 2011, p. 27 (Sur. Ct., Bronx Co.).

Ilene S. Cooper is a partner at Farrell Fritz, P.C., in Uniondale, New York.

The Honorable Antonin Scalia

Distinguished Jurist and Honoree

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Contact: Ilene S. Cooper
516-227-0736

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Ad Hoc: Multi-State Practice
William P. LaPiana
New York Law School
185 West Broadway
New York, NY 10013-2921
william.lapiana@nyls.edu

Charitable Organizations
Christine Woodcock Dettor
Green & Seifter Attorneys, PLLC
110 West Fayette Street
One Lincoln Center, Suite 900
Syracuse, NY 13202
cdettor@gslaw.com

Mary Anne Cody
Mackenzie Hughes LLP
101 South Salina St., Suite 600
Syracuse, NY 13202
mcody@mackenziehughes.com

Continuing Legal Education
Jennifer N. Weidner
Boylan Code LLP
The Culver Road Armory
145 Culver Road
Rochester, NY 14620
jweidner@boylanbrown.com

Diversity
Lori A. Douglass
Moses & Singer LLP
405 Lexington Avenue
New York, NY 10174-1299
ldouglass@mosessinger.com

Anne C. Bederka
Greenfield Stein & Senior, LLP
600 Third Avenue
New York, NY 10016
abederka@gss-law.com

Elderly and Disabled
Lisa K. Friedman
Law Office of Lisa K. Friedman
232 Madison Avenue, Suite 909
New York, NY 10016
lf@lisafriedmanlaw.com

Estate and Trust Administration
Natalia Murphy
Day Pitney LLP
7 Times Square
New York, NY 10036
nmurphy@daypitney.com

Estate Litigation
Eric W. Penzer
Farrell Fritz PC
1320 RXR Plaza
Uniondale, NY 11556-1320
epenzer@farrellfritz.com

Estate Planning
Darcy M. Katris
Hodgson Russ
1540 Broadway, 24th Floor
New York, NY 10036
dkatris@hodgsonruss.com

International Estate Planning
Daniel S. Rubin
Moses & Singer LLP
The Chrysler Building
405 Lexington Avenue
New York, NY 10174-1299
drubin@mosessinger.com

Law Students and New Members
Lauren M. Goodman
Katten Muchin Rosenman LLP
575 Madison Avenue, Room 2010a
New York, NY 10022-2511
lauren.goodman@kattenlaw.com

Michelle Schwartz
Fulbright & Jaworski LLP
666 Fifth Avenue
New York, NY 10103
mschwartz@fulbright.com

Legislation and Governmental Relations
Ian William MacLean
The MacLean Law Firm, P.C.
100 Park Avenue, 20th Floor
New York, NY 10017
ianwmaclean@maclean-law.com

John R. Morken
Farrell Fritz PC
1320 RXR Plaza
Uniondale, NY 11556-1320
jmorken@farrellfritz.com

Life Insurance and Employee Benefits
Patricia J. Shevy
The Shevy Law Firm, LLC
7 Executive Centre Drive
Albany, NY 12203
patriciashevy@shevylaw.com

Members and Membership Relations
Thomas J. Collura
Tuczinski, Cavalier, Gilchrist & Collura, P.C.
54 State Street, Suite 803
Albany, NY 12207-2524
tcollura@tcgclegal.com

Stephen B. Hand
Jaspan Schlesinger LLP
300 Garden City Plaza
Garden City, NY 11530
shand@jaspanllp.com

Newsletter and Publications
Cristine M. Sapers
Debevoise & Plimpton LLP
919 Third Avenue
New York, NY 10022-3902
cmsapers@debevoise.com

Practice and Ethics
Lori J. Perlman
9 Victoria Place
Princeton Junction, NJ 08550
loriperlman@yahoo.com

Surrogates Court
Joseph T. La Ferlita
Farrell Fritz P.C.
1320 RXR Plaza
Uniondale, NY 11556
jlaferlita@farrellfritz.com

Taxation
Laurence Keiser
Stern, Keiser & Panken, LLP
1025 Westchester Avenue, Suite 305
White Plains, NY 10604
lkeiser@skpllp.com

Technology
David Goldfarb
Goldfarb Abrandt Salzman & Kutzin LLP
350 Fifth Avenue, Suite 1100
New York, NY 10118-1100
goldfarb@seniorlaw.com

Executive Committee District Representatives

First District
Linda J. Wank
Frankfurt Kurnit Klein & Selz PC
488 Madison Avenue, 10th Floor
New York, NY 10022
lwank@fkks.com

Second District
Marilyn Ordover
Cullen & Dykman LLP
177 Montague Street
Brooklyn, NY 11201
mordover@cullenanddykman.com

Third District
Deborah S. Kearns
Albany Law School
Law Clinic & Justice Center
80 New Scotland Avenue
Albany, NY 12208
dkear@albanylaw.edu

Fourth District
Michael R. Suprunowicz
Higgins, Roberts, Beyerl
& Coan, P.C.
1430 Balltown Rd.
Niskayuna, NY 12309
msuprunowicz@hrbclaw.com

Fifth District
Martin A. Schwab
Bond, Schoeneck & King, PLLC
One Lincoln Center, Suite 1800
Syracuse, NY 13202
mschwab@bsk.com

Sixth District
Hon. Eugene E. Peckham
Levene Gouldin & Thompson LLP
P.O. Box F-1706
Binghamton, NY 13902
epeckham@binghamtonlaw.com

Seventh District
Audrey Patrone Peartree
Harris Beach PLLC
99 Garnsey Road
Pittsford, NY 14534
apeartree@harrisbeach.com

Eighth District
Catherine T. Wettlaufer
Hiscock & Barclay LLP
1100 M&T Center
Three Fountain Plaza
Buffalo, NY 14203-1414
cwettlaufer@hblaw.com

Ninth District
Charles T. Scott
Greenfield Stein & Senior, LLP
600 Third Avenue, 11th Floor
New York, NY 10016-1901
cscott@gss-law.com

Tenth District
Peter K. Kelly
Ruskin Moscou & Faltischek PC
East Tower, 15th Floor
1425 Rexcorp Plaza
Uniondale, NY 11556-1425
pkelly@rmfpc.com

Eleventh District
Madaleine S. Egelfeld
125-10 Queens Blvd., Suite 311
Kew Gardens, NY 11415
madaleinelaw@gmail.com

Twelfth District
Kate E. Scooler
Bronx Surrogate's Court, Law Dept.
851 Grand Concourse
Bronx, NY 10451
kscooler@courts.state.ny.us

Thirteenth District
Paul S. Forster
P.O. Box 61240
Staten Island, NY 10306
psflaw@aol.com

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TRUSTS AND ESTATES LAW SECTION
One Elk Street, Albany, New York 12207-1002

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TRUSTS AND ESTATES LAW SECTION NEWSLETTER

Editor

Cristine M. Sapers
Debevoise & Plimpton LLP
919 Third Avenue
New York, NY 10022
cmsapers@debevoise.com

Section Officers

Chair
Elizabeth A. Hartnett
Mackenzie Hughes LLP
101 South Salina Street
P.O. Box 4967
Syracuse, NY 13221
ehartnett@mackenziehughes.com

Chairperson-Elect
Ilene S. Cooper
Farrell Fritz PC
1320 RXR Plaza, Floor–13 West
Uniondale, NY 11556
icooper@farrellfritz.com

Secretary
Carl T. Baker
FitzGerald Morris Baker Firth PC
P.O. Box 2017
16 Pearl Street
Glens Falls, NY 12801
ctb@fmbf-law.com

Treasurer
Ronald J. Weiss
Skadden Arps Slate Meagher & Flom LLP
Four Times Square, 28th Floor
New York, NY 10036
ronald.weiss@skadden.com