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Trusts and Estates Law Section Newsletter

A publication of the Trusts and Estates Law Section
of the New York State Bar Association

A Message from the Section Chair

"You can go to heaven if you want to. I'd rather stay in Bermuda."—Mark Twain

Carl T. Baker

Following our Spring Meeting, there may be several of our members who would share that sentiment. Aside from a beautiful island and a welcoming resort, we were treated to an excellent program on asset protection and sophisticated trust planning. Co-Chairs Phil Burke and Mike Suprunowicz assembled an outstanding panel of speakers for our benefit. The speakers' materials, supplemented with content from the course book editor Ilene Cooper, produced a two-volume set of valuable resource materials and information. If you were not able to attend the program, you should consider obtaining the course books from NYSBA.

Now it's on to Binghamton for our Fall Meeting, October 10 and 11. Hon. Eugene Peckham, past Section Chair, has also gathered an incredibly strong panel of speakers and outlined a practical program that will benefit most all T&E practitioners—planning for the middle and upper middle class estate, estates in excess of a million dollars but less than ten million for couples. In other words, estates that are not likely to owe any federal estate tax (at least under the current law) but are taxable by New York State. These are the clients that many of us see most often. Watch for notice of this program and be sure to register early to secure a room in our reserved block.

As I compose this report, we are hanging fire on our legislative initiatives. The legislative term has drawn to a close and we are awaiting the final reports on which parts of our affirmative agenda have been passed by both houses. Legislation and Governmental Relations Committee Chairs Ian MacLean and Rob Harper inform us about the current status of these initiatives in this *Newsletter*. Updates will continue in future editions.

Inside

NYSBA

The State Bar has created a "2013 NYSBA Mentors Council," the goals of which include not only developing "future leadership for your section, but future long-term NYSBA leadership as well, creating a 'win-win' scenario for sections and for NYSBA." The first project of the new Council is a mentoring program in support of the Association's diversity initiatives by pairing an experienced practitioner with a lawyer having an interest in our practice area and "an eagerness and willingness to further the work of your section." Three of our members, Eve Rachel Markewich, Michael Ryan and Patricia Shevy, have offered their time to mentor four applicants. If anyone else would like to become involved in this program, please contact me.

And as for the Bar's diversity initiatives, our Section was one of several honored with the Diversity Champion Award as a result of the planning and programs of Ashwani Prabhakar and Anta Cisse-Green, our Diversity Committee Chairs. This is the second year in a row that our Section has received this award. Credit also goes to past Chairs, Anne Bederka and Lori Douglas.

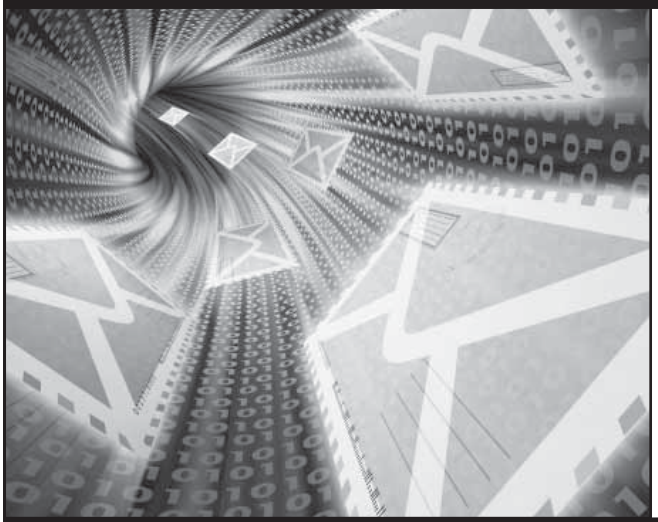
In addition, the Diversity Committee has planned and scheduled a special CLE to be presented this fall, targeting young attorneys who may want to pursue a career in trusts and estates. They are currently seeking volunteers to help support their efforts, and to participate in our mentoring program. If you would like to help guide and bring young, diverse practitioners into our fields of law, please contact either Ashwani Prabhakar (APrabhakar@gss-law.com) or Anta Cisse-Green (acissegreen@akingump.com).

Continuing with membership matters, our Member and Membership Relations Committee, chaired by Jennifer Weidner, recently met by phone conference to "brainstorm" membership initiatives. While promoting our Section to the Bar in general to attract new members is important and something the committee is pursuing, it is clearly just as important that we retain our current members by ensuring we provide value and benefits to meet their needs. Our dues are modest at $40 per year, and the targeted legal education programs that our CLE Committee supports and organizes more than justify that minor cost. Add to that the exclusive regular content of this *Newsletter*, the networking available at our meetings, and the support of our members through our portal of the NYSBA website, and there is a compelling case for joining and remaining a member of our Section. But is there more that we should offer? Are there needs of our members that we are not addressing? We have volunteers willing to contribute time and funds available to support effective initiatives and new programs. Do you have an idea about how our Section can improve your practice and assist you in making you a better T&E practitioner? If so, please let us know. All suggestions are welcomed and needed.

I look forward to seeing and meeting many of you in Binghamton this fall. As always, if you have any questions, ideas, suggestions or concerns regarding our Section and its work, please feel free to contact me directly at any time. I can be reached by phone at (518) 745-1400, or by email at ctb@fmbf-law.com.

Carl T. Baker

Request for Articles



If you have written an article you would like considered for publication, or have an idea for one, please contact the *Trusts and Estates Law Section Newsletter* Editor:

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

www.nysba.org/TrustsEstatesNewsletter

Editor's Message

Always addressing diverse issues relevant to the trusts and estates practitioner, this edition of our *Newsletter* contains particularly thought provoking topics. Pamela Ehrenkranz provides guidance for advising those who wish to make organ and tissue donation a part of their estate plan—a subject that attorneys may not necessarily discuss with their clients on a regular basis. Ravin J. Shah analyzes the Prudent Investor Act and investment theories predating the statute, and Jasmine M. Campirides Hanif presents an in-depth look at practical aspects of charitable donations beyond of the typical categories of cash and publicly traded securities. In addition, Antonia J. Martinez and Robert W. Shaw's article provides insight into mediation and its value to elder law and estate attorneys, and Ian W. MacLean and Robert M. Harper give us a thorough legislative update.

I am pleased to report that submissions to the *Newsletter* have been coming in steadily, and again invite contributions for our next edition. Our next submission deadline is September 6, 2013. Just a reminder to anyone who has contributed, or is contemplating doing so—authors may earn up to 12 CLE credits per reporting cycle for legal research based writing. For information about obtaining credits, please feel free to contact me directly.

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

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Implementing the Wishes of a Client to Donate Organs and Tissue in New York State

By Pamela Ehrenkranz

This article discusses two important components of organ and tissue donation: (i) how to carry out the wishes of a client regarding organ and tissue donation under New York law, and (ii) how to advise the hospital or other medical or research institution of those wishes.

> *A client calls you at your office and tells you that her 70-year-old husband, Neal, has just had a stroke. He had been resuscitated at his apartment and taken to a nearby hospital. You locate Neal's health care proxy and living will and dash off to the hospital emergency room. The health care proxy names Neal's wife as his health care agent to make health care decisions for him in the event that he cannot make those decisions for himself. The living will explicitly states Neal's wish that his organs and tissues be donated for transplantation or research. By the time you arrive at the hospital, Neal is brain dead (there has been an irreversible loss of all function of his brain). You give the living will to Neal's wife but she folds the document and places it in her pocketbook, telling you that no one would be able to use Neal's 70-year-old organs.*[1] *Neal dies the next day and he and his organs are cremated.*

To Whom Should You Have Given the Living Will and Organ Donation Directive?

By giving the living will with the organ donation requests to Neal's wife, as health care agent, the attorney introduces a third party to the situation. The effectiveness of the client's instructions becomes subject to the exclusive actions of the third party. To avoid this, the attorney should give the living will and organ donation request both to the agent and a copy to the attending physician or hospital administrator. Then the procurement of organs and tissue can be addressed directly by the physician, the hospital, and the agent.[2]

The best practice would be for the attorney to advise the client as part of the client's estate planning initiatives to complete a Life Organ and Tissue Donor Registration Enrollment Form with the Donate Life Registry. The Donate Life Registry is an online service that is accessed by an organ procurement organization to determine whether an individual has consented to the procurement of organs and tissues. The procurement agency is notified of a patient's condition when brain death is impending or when ventilator support is being withdrawn (for organ donation), or at the time of death (in the case of tissue donation). It is also accessible to every hospital throughout the United States, which is critical as one never knows when and where someone is going to die.[3] If an individual registers with the New York State Donate Life Registry, as with any valid organ donation document, family members and loved ones will be informed of the registration at the relevant time and given information regarding the donation process, but their permission is *not* required to proceed with the donation.

Registering as a Life Organ and Tissue Donor does not compromise the level of care an individual receives or intimate that a patient will be allowed to die any sooner than if the individual did not register. (The physicians involved with the care of a patient are unlikely to know if a patient is an organ donor and the physicians involved in the procurement process are unlikely to know about the specific treatment of a patient.)[4] This option also bypasses any need to involve a health care agent or family member, and avoids the need to locate the card, drivers' license, living will, or other valid document of donation when time is of the essence.

Organ donation raises complicated issues regarding end of life treatment. A desire to donate organs requires the coordination of all of an individual's end of life care instructions, including, for example, orders not to intubate (DNI), orders not to resuscitate (DNR), orders not to put a patient on a ventilator, or other wishes or instructions routinely contemplated if a client does not want to be kept alive when death is imminent. The client, as patient, will need mechanical ventilator support in order for the option of organ and tissue donation to be preserved. Use of such means may be inconsistent with other instructions. Therefore, inclusion of language in living wills and other documents providing instruction on end of life care must contemplate the care that is necessary to safeguard organs and tissues for donation.[5] Furthermore, the intrusion of life sustaining endeavors may significantly interfere with the precious personal and private moments that family and loved ones have with a patient who is so close to death. There is a delicate balance between medical necessity and intimate personal relations that must be thoughtfully, solicitously, and sympathetically addressed, which makes the topic that much more complicated.

Applicable New York Law on Donations

An anatomical gift of all or any part of a body for any purpose may be made by any individual of sound mind who is at least 18 years of age. The gift is effective at death.[6]

For potential donors, the New York Public Health Law contemplates that a gift of the organs, tissues, and eyes[7] may be made for a number of different purposes as specified by the donor, such as for science, research,

medical teaching and education, and transplantation. A gift may be made either to a specified donee (*i.e.*, to an individual in need of a transplant) or, as is usually the case, without specifying a donee. If the gift is made to a specific donee, delivery of the document to the donee is not necessary to validate the gift.[8]

Although there are many options for effecting the gift, the surest method is the first option listed below, which is to enroll in the New York State Department of Health *Donate Life Registry*.

A. Documents That Can Be Used to Make Organ and Tissue Donations

1. Donate Life Registry

An individual may enroll in the New York State Department of Health *Donate Life Registry* on line at www.nyhealth.gov or www.donatelifeny.org. This enrollment program was created in 2006. In order to donate, the donor signs a form including the donor's name, address, and certain demographics, birthdate, gender, eye color, and height. It also requests the individual to provide his or her driver's license ID number.

2. Last Will and Testament

An individual may make a gift of all or part of the body by a last will and testament, which gift becomes effective upon the death of the testator.[9] If the will is presented as evidence of an individual's direction, the will can be acted on if such actions are taken in good faith. If the will is not actually probated or proved in court to be the valid last will and testament of the decedent or if it is declared invalid for testamentary purposes, the gift, to the extent that it has been acted upon in good faith, is nevertheless valid and effective.[10]

3. Organ Donation Card or Driver's License

An individual may make a gift using a card or other form of documentation "designed to be carried on the person."[11] This would include an organ donor card or driver's license.[12] This card or other document must be signed by the donor. It is not necessary for this form of documentation to be either witnessed or notarized. It is also not necessary for the document to be delivered to the donee of the gift prior to death in order to be effective.[13]

4. Voter Registration

An individual may complete an organ donation form when he or she registers to vote in New York. This form has to be signed and dated by the donor. Completing this form authorizes the Board of Elections to provide the donor's name and identifying information to the Department of Health for enrollment in the *Donate Life Registry*.

5. Living Will

An individual may execute a living will, which should be signed by the individual before two witnesses and signed by the two witnesses, indicating his or her wish to donate organs.[14]

6. Health Care Proxy

An individual may execute a health care proxy indicating his or her wish to donate organs. The agent has an ethical obligation to follow the principal's wishes. The New York health care proxy must be signed by the individual before two witnesses and signed by the two witnesses. The failure to include specific instructions advising the agent of a wish to donate organs shall not be construed to imply a wish not to donate.[15] If an individual has not specifically made a gift in a document, the agent for the individual has the priority to authorize consent to organ and tissue donation. (Priority is discussed further in Section 8.)

7. Appointment of Agent to Control Disposition of Remains

An individual may execute a document appointing an agent to control the disposition of his or her remains. The person given control of the disposition of remains of a decedent can also be given authority to consent to organ or tissue donation (though a health care agent would have priority). Failure to state wishes in the Disposition of Remains document or other instructions shall not be construed to imply a wish not to donate.[16] A Disposition of Remains document must be signed by the individual before two witnesses and signed by the two witnesses.

8. Consent from an Agent, Next of Kin, or Guardian

Where a patient has not properly executed an organ donor card, driver's license authorization, registered, or otherwise given written authorization for a donation, procurement services may be obtained with the consent from an individual's agent, next of kin, or guardian. Consent forms must clearly specify the tissues and/or non-transplant anatomic parts to be retrieved. Consent may be obtained by telephone, but such consent must be recorded or documented in writing by the procurement organization requesting the donation.[17]

Any of the persons, in the order of priority set forth below, may give consent when persons in prior classes are not reasonably available,[18] willing, and able to act, at the time of death, and in the absence of actual notice of contrary indications by the decedent or actual notice of opposition by a member of the same class or prior class specified below, or reason to believe that an anatomical gift is contrary to the individual's religious or moral beliefs.[19]

a) The person designated as the health care agent (subject to any written statement regarding organ or tissue donation included in the health care proxy form).

b) The person designated in a written instrument as the decedent's agent to control the disposition

of the individual's remains. (This agent would presumably only be able to act if the individual is deceased and would be subject to any written statement regarding organ or tissue donation included in the disposition of remains document.)

c) The spouse, if not legally separated from the patient, or the domestic partner.[20]

d) A son or daughter eighteen years of age or older.

e) Either parent.

f) A brother or sister eighteen years of age or older.

g) A guardian of the person of the decedent at the time of his or her death.

h) Any other person authorized or under the obligation to dispose of the body.

B. Revocation of the Gift

The decision to donate is revocable by the prospective donor while the individual is living and competent.[21] A gift made in a will may be revoked by codicil or by revoking the will. Any other document evidencing the gift may be revoked by i) the destruction, cancellation, or mutilation of the document *and all executed copies thereof;* or by ii) the execution and delivery to the donee of a signed statement revoking the gift, iii) an oral statement of revocation made in the presence of two persons, communicated to the donee, iv) a statement during a terminal illness or injury addressed to an attending physician and communicated to the donee, or in a signed card or document, found on his person or in his effects. If the will, card, or other document has been delivered to a specified donee, the donor may amend or revoke the gift only as set forth in ii through iv, above. If an executed original living will, health care proxy, or other document has been delivered to a third party agent, that original must be retrieved and destroyed.

Authorization for organ or tissue donation may not be rescinded by a family member unless the family member knows that the donor has revoked the authorization.[22] In other words, in any case where the donor has properly executed an organ donor card, driver's license authorization, registered in the New York state organ and tissue donor registry, or has otherwise given written authorization for organ or tissue donation, authorization for donation may not be rescinded by the next of kin or guardian except upon a showing that the donor revoked the authorization. If an individual registers with the New York State *Donate Life Registry*, the family will be informed of the registration and given information regarding the donation process, but their permission is ***not*** required to proceed with the donation.

Correspondingly, a donee shall not accept a gift when (a) the donee has actual notice of contrary indication by the decedent, (b) where the donor has not properly executed an organ donor card, driver's license authorization to make an anatomical gift, registered in the New York state organ and tissue donor registry, or otherwise given written authorization for organ or tissue donation, or has revoked any such authorization, and the gift is opposed by a person or persons in the highest priority available of the classes specified above, or (c) the donee has reason to believe that an anatomical gift is contrary to the decedent's religious or moral beliefs.[23]

Conclusion

Research into the area of organ donation raises many questions that are beyond the traditional scope of trust and estate practice. Organ donation is a valuable public health service. It clearly falls within the purview of estate planners, as it is one of the end of life directives on which estate planning lawyers typically focus clients. Albeit important, it can be the forgotten child of estate practitioners. However, if organ donation is desired, it is important that the planner assist the client in executing the requisite documents to facilitate and provide a mandate for those wishes to be fulfilled.

Endnotes

1. Note: organs from an older person are not *per se* unusable; they may be highly useful either for transplantation or research.
2. New York Public Health Law ("PHL") § 4301(7) provides that the rights of the donee created by the gift are paramount to the rights of others except as provided by PHL § 4308 (regarding the prohibition on charging a fee to a donor's estate for any cost incurred in testing or removing a human organ or tissue).
3. PHL § 4310.
4. *See also* fn 8 below. *Racial Disparities in Preferences and Perceptions Regarding Organ Donation*, Laura A. Siminoff, PhD., Christopher J. Burant, MACTM, MA, Said A. Ibrahim, MD, MPH, *Journal of General Intern Medicine* 2006 Sept. 21 (9):995-1000, *Caring for organ donors: The intensive care unit physicians' view*, Maria Lùcia Aruajo Sadala, RGN, PhD, Marisa Lorençon, RGN, Màrcia Cercal, RGN, and Arthur Schlep, PhD, Heart & Lung, May / June 2006. *Two perspectives on organ donation: experiences of potential donor families and intensive care physicians of the same event* Margareta A. Sanner, PhD, Journal of Critical Care (2007) 22, 296-304.
5. Choice of language depends on whether the document is being used to make the anatomical gift:

   Option A

   > "I hereby make a gift of my organs and tissues, including eyes, upon my death, for purposes of transplantation, therapy and research. Notwithstanding any directive contained in any other section of this document, I consent to the commencement and maintenance of any medical procedure necessary to evaluate, maintain or preserve my organs or tissues for purposes of donation, including, but not limited to administration of medication, mechanical respiration and artificial nutrition and hydration."

   Option B

   > "Notwithstanding any directive contained in any other section of this document, I consent to the commencement and maintenance of any medical procedure necessary to evaluate, maintain or preserve my organs or tissues for purposes of donation, including, but not limited to administration of medication, mechanical respiration and artificial nutrition and hydration."

6. PHL § 4301(1). Donations from a living donor are determined using different criteria. *See, e.g., Official Compilation of Codes, Rules and Regulations of the State of New York*, 10 NYCRR Subpart 52-3.

General Technical Standards for Tissue Banks 52-3.3 provides that a comprehensive or limited tissue procurement service must obtain a signed informed consent from a living donor of tissue for clinical use. The acceptability of a donation from a living donor is determined by a physical examination of and health history interview with the donor. 52 3.3(d).

7. Anatomical gifts can be general or specific (e.g., heart, heart valves, lungs, liver, kidney(s), pancreas, small bowel, other abdominal organs, bones, connective tissues, middle ear tissues, skin grafts, saphenous veins, and more recently, hands and faces).
8. PHL § 4303. The statute provides as follows: If no donee is specified, "the gift may be accepted by and utilized under the direction of the attending physician upon or following death. If the gift is made to a specified donee who is not available at the time and place of death, the attending physician upon or following death, in the absence of any expressed indication that the donor desired otherwise, may accept the gift as donee. The physician who becomes a donee under this subdivision shall not participate in the procedures for removing or transplanting a part." PHL § 4304 provides that "[i]f a gift is made by the donor to a specified donee, the will, card, or other document or an executed copy thereof, may be delivered to [the donee] to expedite the appropriate procedures immediately after death." Note, however, that when a donor is determined dead based on irreversible cessation of circulatory and respiratory functions, the time of death must be certified by a physician. In all other cases the time of death must be certified by the physician who attends the donor at his death and one other physician. Any of such physicians may not participate in the procedure to remove or transplant the body part. PHL §§ 4303(4) and 4306(2).
9. Estates, Powers and Trusts Law ("EPTL") 1-2.19 provides that a will includes a written instrument, made as prescribed under the statute, to take effect upon death, whereby a person disposes of property or directs how it shall not be disposed of, or disposes of his body or any part thereof. Property is defined in EPTL 1-2.15 as anything that may be the subject of ownership, and is real or personal property.
10. PHL § 4303(1).
11. PHL § 4303(2).
12. There is no requirement that the driver's license be a New York state license.
13. PHL § 4303(2).
14. *In re Westchester County Medical Center*, 72 N.Y.2d 517, 534 N.Y.S.2d 886 (1988).
15. PHL § 2981(5)(f). This would be consistent with the rules applicable to a disposition of remains document. PHL § 4201(4)(a).
16. PHL § 4201(4-a).
17. PHL § 4303(5).
18. "Reasonably available" is defined in PHL § 4301(3) to mean that a person "can be contacted without undue effort and willing and able to act in a timely manner consistent with existing medical criteria necessary for the making of an anatomical gift."
19. PHL § 4301(2). Note that most organized religions do not prohibit the donations of organs and tissue.
20. Domestic partner is defined in PHL § 4301(4).
21. PHL § 4305.
22. PHL § 4301(2).
23. PHL § 4301(5).

Pamela Ehrenkranz is Chair of the Wachtell, Lipton, Rosen & Katz (New York, NY) Trusts and Estates Practice Group. **With acknowledgement to Susan E. De Wolf for her valuable insights and to Helen M. Irving, Tia Powell, M.D., Christina W. Strong, and Lewis Teperman, M.D., for their valuable input.**

The Prudent Investor Act and the Great Recession

By Ravin J. Shah

Much of the commonly accepted wisdom surrounding investing and the markets derives from two theories: the Modern Portfolio Theory ("MPT") and the Efficient Market Hypothesis ("EMH"). The scope of the influence of these theories is evident in everything from investment valuation to securities regulations.[1] In addition, MPT and EMH serve as the framework for New York's adaptation of the Uniform Prudent Investor Act, as codified by EPTL 11-2.3 ("PIA").

When it was passed, the PIA was perceived as the long-awaited vehicle for change by bringing the antiquated methods of trust management into the modern era. With rules like "no investment is inherently imprudent," trustees viewed the PIA as reflective of the "realities" of the markets. However, given the events of the past ten years—sometimes referred to as the "lost decade,"[2]—which have caused considerable anxiety and loss to countless beneficiaries, scholars and professionals now question the conventional wisdom of the MPT and EMH.

Critics point to the nascent field of behavioral finance when attacking the MPT and EMH, which has provided new insights into investing and the motivations of investors. Critics also attack the PIA by pointing out that the "vague standards…[of the PIA] provide[] trust beneficiaries with little protection against agency costs that…[have] lead trustees to invest too heavily in equities."[3]

This article explains both the MPT and EMH models (Part I), outlines their flaws (Part II), and suggests solutions (Part III). Hopefully, this will stimulate debate among readers to consider the appropriate course of action in light of newly introduced realities.

I. MPT and EMH Models Explained

A. Historical Background: "Legal list" Approach & "Prudent Man" Approach

Historically, there are two approaches to managing trust assets: (i) the "legal list" approach, and (ii) the "prudent man" rule. The New York Court of Appeals laid the foundation for both of these methods in *King v. Talbot*.[4] There, the court said, "…the trustee is bound to employ such diligence and such prudence in the care and management, as in general, prudent men of discretion…employ in their own like affairs."[5] The court further opined that it was not prudent "to place the principal of the fund in a condition, in which, it is necessarily exposed to the hazard of loss or gain…and in which, by the *very terms of the investment*, the principal is not to be returned at all."[6] Thus, investments in equities were per se imprudent. Under this line of reasoning, "states developed, either by statute or case law, a 'legal list' of permissible trust investments…."[7]

The "legal list" approach was predominantly used through the 1930s and 1940s, until a second method, known as the "prudent man" rule—largely emanating from the 1830 case of *Harvard College v. Amory*[8]—was adopted by an increasing number of states. Under this standard, a trustee must "conduct himself faithfully and exercise a sound discretion. He is to observe how men of prudence…manage their own affairs…in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of the capital to be invested."[9] This approach became particularly popular when studies in the 1930s and 1940s "showed that returns on trust investments in 'prudent man' states were almost double the returns in legal list states."[10]

B. Times Change and Dissatisfaction Rises

The conservative and capital preservation driven strategies of the legal list and prudent man comported with the sentiment of the Great Depression era.[11] However, starting in the 1940s, the U.S. economy experienced an unprecedented period of growth that spanned over sixty years. Illustrating this point using the S&P 500 Index as a general marker of the economy, the adjusted close on January 3, 1950 was 16.66, and on January 3, 2000, it was 1,455.22, a 8,600% gain.[12] During the post-World War II era, equities typically generated higher returns than more traditional trust investments like bonds. Additionally, during the "malaise" of the 1970s, inflation was rampant, and it became apparent that "safe" investments like bonds bore a risk of their own—inflation eroding the trust principal.[13]

C. Markowitz, Fama and the Prudent Investor

1. Modern Portfolio Theory (MPT)

Despite the market conditions, trust investing rules did not change until 1990s. These changes were initiated in 1952, when Harry Markowitz wrote his article *Portfolio Selection*[14] and linked the concepts of risk and reward. The basis for his theory is that investors want high returns,[15] are "risk averse,"[16] and thus want dependable returns.[17] In this context, for an investor to choose a high risk investment, the investment must provide the requisite amount of return to "compensate" for the given amount of risk. To think about it another way, for a given level of return, an investor will look for an investment with the lowest level of risk.[18]

Markowitz's true insight came within the realm of diversification as it relates to risk. He stated that there are two basic types of risk: systematic and unsystem-

atic risk. Systematic, or market risk, is the risk that is inherent in the market; the risk that "the return of the *market*…will be less than predicted."[19] Unsystematic, or firm specific risk, deals with the risk that is specific to a given security and / or its industry. This refers to the "possibility that the return of a *particular asset* will be less than expected."[20] As such, firm-specific risk could be diversified away, and systematic risk or market risk could not.[21] Thus, while never eliminating *all* risk, Markowitz argued that a diversified portfolio will have *less* overall risk than an undiversified portfolio.

2. Efficient Market Hypothesis (EMH)

In 1960, Eugene Fama introduced his Ph.D thesis that later became the Efficient Market Hypothesis. His theory filled the gap left by Markowitz's MPT, namely "how to determine the expected return of a particular investment."[22] The base premise was that in an efficient market "prices provide accurate signals for resource allocation."[23] If capital markets were efficient, then the "prices of securities would reflect accurately the expected risk and return of those securities,"[24] and thus incorporate the best available information about those securities. On the other hand, if the markets were not efficient and did not incorporate all available information, then there would be a misallocation of capital. Fama engaged in empirical studies and concluded that "securities prices quickly and fully reflected available information about those securities."[25]

The implications of this conclusion were important because it meant that no investment was inherently a "bad" investment since the price already incorporated the firm-specific risk.[26] As such, in its purest or strongest form, it was not possible to "beat the markets" with a proprietary investment strategy. This meant that when investing, one could put his or her money into risky or higher risk stocks and diversify away the firm specific risk by holding a diversified portfolio.

3. The Solution: Prudent Investor Act

As time went on, both the MPT and EMH were increasingly accepted, and pressure increased to change the seemingly antiquated legal list and prudent man standards.[27] Seen as too restrictive, the legal list method banned all equities, and the prudent man approach required the trustee to evaluate the "prudence" of an investment in a vacuum.[28] Additionally, income beneficiaries and remaindermen were at odds with the investment strategies that should be employed. The income beneficiaries often wanted investments that provided the greatest amount of immediate income, while the remaindermen wanted investments that grew the money in a safe and reliable way.

Investment standards ultimately changed in the 1990s with the Uniform Prudent Investor Act and the Restatement (Third), which adopted much of what MPT and EMH held. Multiple states enacted their own versions, including New York with EPTL 11-2.3. Pursuant to the new standards, the tension between the income beneficiary and remaindermen would be alleviated by allowing trustees to invest for objectives other than capital preservation, such as total return. No longer would the trustees bear the liability for investing in securities that were too risky or speculative. The required diversification of investments would reduce risk without compromising return. The only worry that remained was market risk or systematic risk, which could be managed by adjusting the percentage of the portfolio that was invested in the high-risk high-return securities.[29]

II. Flaws of MPT and EMH

A. MPT-EMH and Behavioral Finance

The MPT and EMH provide great insights into risk, but flaws have recently been revealed when applying these principles to the real world. As mentioned above, investors have been described as risk-averse. However, sometimes investors do not act according to this methodology. Robert J. Shiller of Yale has "show[n] that mass psychology, herd behavior and the like have an…effect on stock prices…."[30] Other "studies have established that when investors make significant investment profits, they…[do not sell and]…subject themselves to greater risk with…[their] 'found money' than they would if they ha[d] not enjoyed recent successes."[31] Furthermore, researchers have learned that investors are often "loss averse" and refuse to liquidate an investment in hopes that it will rise again, and thus "expos[e] themselves to greater risks than the expected future return of those stocks."[32]

Additionally, according to the MPT and EMH, firm-specific risk can be diversified away, leaving only market or systematic risk. The foundation of this conclusion lies in Markowitz's risk-return mechanism, which was based on his observation of the correlation that exists between investments. However, the weakness here is the assumption that correlations remain static. Professor Siegel of the University of Pennsylvania noted, "The most serious attack on efficient markets is the change in correlation of asset classes under extreme conditions."[33]

B. Implications for Trust Investing and Management

Given the recent lessons learned from behavioral finance, the PIA does not have provisions to protect against issues like herd mentality and an over-weighted portfolio. Instead, the focus of the PIA was put on the trustee's requirement to diversify and ability to make distributions to the beneficiaries "in accordance with risk and return objectives…[of the] entire portfolio."[34] Additionally, the PIA stated that "no investment was inherently prudent or imprudent." However, even Markowitz's article recognized that not "every invest-

ment would be sensible if appropriately diversified…it acknowledged that more work was needed to develop a strategy for…[calculating risk and return figures for individual securities]."[35]

Furthermore, there is no guidance as to the proper *amount* or percent of a portfolio that an asset class should constitute. In their study, Max Schanzenback and Robert Sitkoff, "demonstrated persuasively that… when states adopted the UPIA, trustees invested a higher percentage of trust portfolio in equities than before the adoption of the statute."[36]

The question of how or why these investments became such a big part of the portfolio is multi-faceted, and may have many explanations. One answer may be related to the agency problem that is created when there is a delegation of investing authority. Agency relationships increase the chance of herd mentality. Considering trustees, such as mutual fund managers, often sell themselves on performance, the likelihood of the money being put into a specific "hot" area is increased. "Once momentum becomes embedded in markets, agents [(in this case a trustee)] logically respond[s] by adopting strategies that are likely to reinforce the trends."[37]

The most significant implication of the PIA is that it does nothing to grapple with market risk. The overall goal should be to fashion a statutory scheme that is manageable and does not sit on the extremes of the spectrum. An overly stringent regime exposes beneficiaries to inflation risk and does not allow the trustee to meet the obligations that the testator intended. Alternatively, a very open policy does not give guidance and can lead to foolhardy investment strategies that harm the testator's intent and beneficiaries. The Prudent Investor Act got it right in some areas, but not all.

III. Possible Solutions

The Model Portfolio Theory and Efficient Market Hypothesis are not the panacea that they were once thought to be. There are issues with how diversification, risk and reward are calculated and implemented into the overall model. Thus, the question becomes, where do we go from here? What model should we follow?

The list of possibilities is wide and varying. Andrew Lo of MIT, for example, has incorporated "evolutionary biology in proposing that markets adapt and evolve over time."[38] Another theory called "Maslowian Portfolio Theory" is premised on Maslow's Hierarchy of Needs.[39] Still others advocate that the MPT and EMH should be expanded to incorporate other models "based on irrational behavior."[40] Even though these theories may touch on some truths, they are still in the early stages of research and the "reliable applications… [to the real world are, by some accounts,] distant."[41]

While researchers continue to figure out the best practical use of these theories, there may be a push for change in the statute to include provisions that limit the amount of the portfolio that may be invested in a particular asset class. If inflation is a big concern, the portfolio could be required to invest in treasury inflation-protected securities (TIPS) as well as other asset classes (like commodities) that often provide a hedge against rising inflation. This way the portfolio would recognize that investors are often *loss* averse by investing in bonds and at the same time providing for meaningful appreciation with the equities portion.

IV. Conclusion

Much has been learned in the past few years, but in reality, there is an element of risk in every investment. Correlations between investments can change, and seemingly "safe" investments can lose all their value overnight. It is an amorphous and frustrating concept that is often dependent on changes in circumstances.

Regardless of a testator's investment literacy, it is vital for every drafter, trustee and portfolio manager to thoroughly and effectively interview that individual regarding his or her intent. Beneficiaries should also be interviewed to understand their needs. Whether a portfolio incurs gains or losses, the statutory design should provide a trust manager with the solace that he or she carried out the testator's objectives with his or her risk level in mind. In the end, there is no substitute for getting to know the client and his or her objectives.

Endnotes

1. John Authers, *Wanted: New Model for Markets*, FINANCIAL TIMES (Sept. 29, 2009), available at http://www.ft.com/cms/s/0/cefa0bfa-ac58-11de-a754-00144feabdc0.html#axzz1J8MOcyYV.
2. *See* Daniel Gross, *The Lost Decade*, SLATE (Nov. 11, 2009), available at http://www.slate.com/id/2235377/ (explaining how in a period from April 2001 to April 2011, the S&P 500 has given back all its gains, and the implications of that reality).
3. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 851 (2010). *See generally* Dimitri Vayanos & Paul Woolley, *Capital Market Theory after the Efficient Market Hypothesis*, VOX (Oct. 5, 2009), available at www.voxeu.org/index.php?q=node/4052.
4. *King v. Talbot*, 40 N.Y. 76 (1869).
5. *Id.* at 86.
6. *Id.* at 88 (original emphasis).
7. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 856 (2010).
8. *Harvard College v. Amory*, 26 Mass. 446 (1830).
9. *Id.* at 461.
10. Martin Begleiter, *Does the Prudent Investor Need the Uniform Prudent Investor Act—An Empirical Study of Trust Investment Practices*, 51 ME. L. REV. 27, 32 (1999).
11. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 857 (2010).
12. Historical prices of the S&P500 are available at http://finance.yahoo.com/q/hp?s=%5EGSPC+Historical+Prices (closing prices were obtained through Yahoo Finance Historical Prices

tool. It is also important to note that the adjusted closing price on Jan. 2 1970 was 93.00, a 458% gain).

13. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 857 (2010).
14. *See generally* Harry Markowitz, *Portfolio Selection*, 7 J. FIN. 77, 77 (1952) (advocating MPT as an alternative investment theory).
15. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 858 (2010).
16. Martin Begleiter, *Does the Prudent Investor Need the Uniform Prudent Investor Act—An Empirical Study of Trust Investment Practices*, 51 ME. L. REV. 27, 33 (1999).
17. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 858 (2010).
18. Martin Begleiter, *Does the Prudent Investor Need the Uniform Prudent Investor Act—An Empirical Study of Trust Investment Practices*, 51 ME. L. REV. 27, 33 (1999).
19. *Id.* (emphasis added).
20. *Id.* (emphasis added).
21. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 859 (2010) (Markowtiz used correlation between individual investments to show the effects of diversification).
22. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 859 (2010).
23. Eugene Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383, 383 (1970).
24. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 860 (2010).
25. *Id.* at 859; *see* Eugene Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FIN. 383, 414–16 (1970) (noting that there was evidence to support the EMH and sparse contrary evidence).
26. *See* John H. Langbein, *The Uniform Prudent Investor Act and the Future of Trust Investing*, 81 IOWA L. REV. 641, 649 ("[MPT] teaches that the risk intrinsic to any marketable security is presumptively already discounted into the current price of the security").
27. *See generally* John H. Langbein and Richard A. Posner, *Market Funds and Trust-Investment Law*, 1 AM. BAR FOUNDATION RESEARCH J. 1 (1976) (advocating the MPT and EMH and recommending index funds as appropriate investments).
28. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 861 (2010).
29. This was helped in part by the power given to the trustee to adjust between income and principal as per EPTL 11-2.3(b)(5) and EPTL 11-2.3-A.
30. Joe Nocera, *Poking Holes in a Theory on Markets*, NEW YORK TIMES, June 6, 2009.
31. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 870 (2010).
32. Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 870 & n. 101 (2010). *See* Terrance Odean, *Are Investors Reluctant to Realize Their Losses?*, 53 J. FIN. 1775, 1775 (1998).
33. John Authers, *Wanted: New Model for Markets*, FINANCIAL TIMES, September 29, 2009 (cites Siegel who goes on to give an example of the change in the correlation between oil and equities from negative to positive).
34. EPTL 11-2.3(b)(3)(A).
35. *See* Stewart Sterk, *Rethinking Trust Law: How Prudent is Modern Prudent Investor Doctrine?*, 95 CORNELL L. REV. 851, 874 (2010).
36. *Id.* at 893 (2010); *see* Max M. Schanzenbach & Robert J Sitkoff, *Did Reform of Prudent Trust Investment Laws Change Trust Portfolio Allocation?*, 50 J.L. & ECON. 681, 687 (2007).
37. Dimitri Vayanos & Paul Woolley, *Capital Markets Theory After the Efficient Market Hypothesis*, VOX, available at http://www.voxeu.org/index.php?q=node/4052.
38. John Authers, *Wanted: New Model for Markets*, FINANCIAL TIMES, September 29, 2009.
39. Phillipe J.S. DeBrouwer, *Maslowian Portfolio Theory: An Alternative Formulation of the Behavioral Portfolio Theory*, 9 J. OF ASSET MGMT. 359, 359 (2008) (In this theory the financial needs of the client are categorized and then put in order of importance so that the objective of investing is always clear.).
40. Dimitri Vayanos & Paul Woolley, *Capital Market Theory after the Efficient Market Hypothesis*, VOX, available at www.voxeu.org/index.php?q=node/4052.
41. John Authers, *Wanted: New Model for Markets*, FINANCIAL TIMES, September 29, 2009.

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Charitable Gifts of Alternative Assets—Tax and Practical Considerations for Donors and Donees

By Jasmine M. Campirides Hanif

With fewer individuals owning highly appreciated marketable securities and excess cash, more consideration has been given to contributing assets other than publicly traded securities and cash to charities. Prior to making such gifts, donors should consider deductibility limits for income and gift tax purposes, the need for appraisals, the practicality of making partial-interest gifts and the reality of parting with real and tangible assets and whether the donee will want the asset intended for donation at all.

As a preliminary point, the general rules regarding the tax consequences of charitable contributions by individuals should be noted. Donors get a triple benefit when contributing appreciated property to charity: (1) a gift or estate tax deduction, (2) an income tax deduction and (3) the avoidance of taxable gain had the property been sold.

While the gift and estate tax charitable deduction is generally equal to the fair market value of the property at the time the gift is completed (other than in the case of certain gifts of partial interests, which are discussed below), is unlimited and does not require that the donee be a U.S. charity,[1] the income tax charitable deduction is more complicated. The income tax charitable deduction requires that the taxpayer itemize his deductions (which are subject to phase-out by as much as 80% at higher income levels)[2] and generally requires that the gift be made to a U.S. charity.[3] For any one tax year the deduction is limited to a percentage of the individual taxpayer's adjusted gross income.[4] The percentage limitation is determined by two factors—the type of organization receiving the donation and the type of property donated.[5]

With respect to the type of organization receiving the gift, generally a gift to a public charity affords the donor the greatest income tax deduction.[6] The income tax deduction is generally equal to (a) the full fair market value of the property limited to 30% of the donor's adjusted gross income or (b) fair market value less unrealized long-term capital gain limited to 50% of the donor's adjusted gross income (AGI).[7] Income tax deductions for donations to a private foundation are less advantageous. Although deductions for cash donations are limited to 30% of AGI, deductions for gifts of long-term capital gain property (with the exception of certain publicly traded stocks) are limited to the donor's cost basis and 20% of the donor's AGI.[8] Deductions are available for the full fair market value of certain publicly traded stocks but these deductions are also limited to 20% of the donor's AGI.[9]

The type of property donated is an important consideration as it affects both the income tax deduction limitation and whether a charity will accept the asset at all. The following highlights some of the income and transfer tax consequences as well as certain non-tax considerations for both donors and charitable donees presented by gifts of various non-cash assets.

LLCs and Partnerships

- Donors may deduct the fair market value of LLC and partnership interests contributed to public charities reduced by the amount of any gain that would not be treated as long-term capital gain if the donor had sold the property instead.[10] The donor's deduction may be further reduced by the donor's proportionate share of the liabilities of the partnership as a result of deemed bargain sale rules which may result in the recognition of capital gain by the donor.[11]

- If a donor has suspended passive activity losses from a partnership, he may be better off selling his partnership interest and donating the net proceeds to charity. This is because the donor will then be able to take the passive activity loss as a deduction on his personal return and get a charitable deduction for the donated proceeds. Otherwise, the passive activity losses are simply added to the donor's basis and may effectively be useless to the donor. Depending on the liabilities of the partnership and the donor's unrealized gain, selling the partnership interest first may produce a better tax result to the donor.

- The donor must give the charity an undivided portion of his entire interest in the entity including a pro rata share of all attributes of the interest such as capital, allocation of income, and expense and distributions.[12]

- The admission of a new partner is generally governed by the partnership agreement or the operating agreement and thus may require consent of the other partners or compliance with other provisions mandated by the governing instrument.

- A charity may be unwilling to accept a contribution of an LLC or partnership interest if it will produce unrelated business taxable income (UBTI) to the charity without assurance that the charity will receive sufficient cash from the interest to cover the resulting UBTI tax.[13]
- Contributions of partnership interests in excess of $5,000 will require a qualified appraisal.[14]

Closely Held C-Corp Stock

- Donors may deduct the fair market value of closely held C-corp stock held for more than one year donated to a public charity.
- If the charity does not really want to own illiquid securities or the other owners do not want an outsider involved in the business, the shares may later be redeemed by the corporation. However, the contribution and the redemption must not have been prearranged. Otherwise, the contribution will be treated as a sale of the stock by the donor and a subsequent contribution of the proceeds, which means the donor will realize and pay tax on the gain. Gifts of closely held shares to charity are especially useful if the business is being sold or merged so that the gain is passed on to the charity. However, again, these gifts should be made before any formal decisions are made by the shareholders regarding the sale or merger.
- The IRS requires a qualified appraisal for donations of closely held stock in excess of $10,000.[15]
- Deductions for donations of closely held stock to private foundations are limited to the donor's basis in the shares and such gifts may trigger the excess business holding rules applicable to private foundations, making them less desirable than gifts to public charities for both the donor and donee.

S-Corp Stock

- The income tax deduction for gifts of S-corp stock to a public charity is equal to fair market value reduced by the shareholder's share of the ordinary income that the donor would have recognized had the assets of the S-corp been sold (i.e., gain on sale of appreciated inventory, unrealized receivables, and depreciation recapture).[16]
- If a gift of the stock is made, all items of income and gain passed through to the charity during the period it holds S-corp stock will constitute UBTI to the charity.[17] Furthermore, any gain recognized by the charity on the sale of the S-corp stock will also be taxable as UBTI.[18] Charities may therefore be unwilling to accept gifts of S-corp stock. Donors considering making gifts of S-corp stock should consider instead having the S-corp itself make a donation of its own assets to charity. Gifts by the S-corp of its own assets do not present these same UBTI issues for the charity.
- The excess business holding rules applicable to private foundations generally require private foundations to dispose of S-corp stock within five years of receipt.[19] The self-dealing rules and excess benefit rules applicable to private foundations and public charities may also make receipt of S-corp stock by charitable donees less desirable.

Restricted Securities

- Restricted securities may be donated to charity but the charity will be subject to the restrictions. Such restrictions will affect the fair market value of the securities and whether the securities will be treated as qualified appreciated stock for purposes of a contribution to a private foundation.[20]
- Charities should weigh restrictions on transfer against the anticipated net benefit of receiving the property.
- The IRS requires a qualified appraisal for gifts of restricted securities in excess of $10,000.[21]

Stock Options

- Donors may only make testamentary gifts of incentive stock options[22] and only if the option plan allows for such gifts. If the donor wants to make a lifetime gift of the options, the donor would have to exercise the options and then, after a requisite holding period, donate the shares. To get a fair market value deduction for the shares and avoid income and capital gain recognition, the shares must first be held for at least two years from the date the option was granted and one year from the date the option was exercised.[23]
- Nonqualified stock options, on the other hand, may be donated during the donor's lifetime if the option plan permits. However, when the options are exercised by the charity, the donor must recognize the income at that time.[24] This means the donor may not know exactly how much income he will recognize and because these types of options don't generally have an ascertainable value at the date of grant, the donor may also not know the value of the charitable deduction. So again, it may be better for the donor to first exercise the options and then donate the shares.

Retirement Accounts

- Lifetime Gifts of IRA Assets: The Pension Protection Act of 2006[25] gave taxpayers the ability to

make direct contributions of IRA assets to a qualified charitable organization. Donors over the age of 70½ could contribute up to $100,000 directly from an IRA to a charitable organization. While the donor did not get a charitable deduction for the contribution, the donor avoided ordinary income taxes on the funds.[26] For the tax benefit to apply, the IRA assets must have been transferred to a qualified charity, which does not include most private foundations (other than those meeting the conduit rules) nor donor advised funds. While the initial provisions expired on December 31, 2007, they have been extended several times, most recently through December 31, 2013 by the American Taxpayer Relief Act of 2012.[27]

- Testamentary Gifts of Retirement Assets: Individuals seeking to make testamentary charitable gifts with considerable retirements assets should consider leaving such assets to charity. Upon death, both income and transfer taxes are assessed against assets remaining in retirement accounts. By leaving such assets to charity, both are avoided. Testators can save up to $0.80 on the dollar by specifically leaving retirement assets to charity and leaving other appreciated assets to noncharitable beneficiaries.

Real Estate

- Donors may receive an income tax deduction for contributed long term capital gain real property equal to fair market value. However, depreciation recapture rules may reduce the deduction if the donated property was depreciated using an accelerated depreciation method.[28]

- Donors who want to spread out the tax deduction may make gifts of undivided fractional interests in real property over multiple years.[29] By doing so, donors may get the benefit of any appreciation in the property during the period over which the fractional gifts are made. Fractional interests gifts however should be accompanied by a specific agreement between the donor and donee regarding the complexities of co-ownership.[30] Charities will often require that the donor agree to donate the remainder of the donor's interest in the property at death. Gifts of fractional interests in real property to the donor's private foundation are not practical because of self-dealing rules.

- Charities may be unwilling or hesitant to accept gifts of real property for a variety of reasons, including management and carrying costs, environmental and other statutory liabilities, lack of liquidity and marketability, and ability to produce income.

- A qualified written appraisal is required substantiating the value of contributed real property in excess of $5,000.[31]

Tangible Property

- Donors may deduct the fair market value of long-term capital gain tangible property contributed to public charities or operating foundations if the charity will use the property in a manner consistent with its charitable purposes.[32] If the charity will simply sell the contributed property, the donor's deduction will be limited to the lesser of the donor's basis and fair market value.

- Works of art or patents created by the donor or received by the donor as a gift from the creator are considered ordinary income property and therefore subject to lower deductibility limits.[33]

- Tangible property sold within three years of the contribution is subject to deduction recapture by the donor.[34]

- Fractional interest gifts of tangible property may be made. However, the property must be owned solely by the donor or by the donor and the charity.[35] If there are other owners, all owners must make a proportional contribution to the charity. The charity must also have the right to possess the property for an amount of time equal to its pro rata ownership share.

- If a gift of a fractional interest in tangible property is made to a charity in one year and the use of the property by the charity is related to such charity's exempt purposes, the taxpayer may take a deduction for the fair market value of the contribution. However, the deductible value of any fractional gifts of the same tangible property made in future years will also be determined as of the date of the initial year contribution if the value on that date is lower than the fair market value on the date of subsequent contributions.[36] This effectively prevents the donor from realizing a charitable deduction on the appreciation in the value of the property upon subsequent fractional gifts and may result in the imposition of a gift or estate tax upon subsequent contributions. Furthermore, 100% of the property must be received by the charity within the earlier of 10 years or the donor taxpayer's death. Otherwise, the donor will be subject to recapture of the income and gift tax charitable deductions (with interest) and to a 10% recapture penalty.[37]

- Donors of art who own both the physical work and the copyright must donate a proportionate interest in both in order to receive an income tax deduction[38] or, in the case of a gift to a charity for an unrelated use, a gift or estate tax deduction.[39]

- Donations of tangible property in excess of $5,000 require a qualified written appraisal.[40] If the donor is seeking a deduction for art valued at $20,000 or more, the donor may be required to submit with the appraisal an 8x10 color photo, a color transparency or (as more recently offered by the IRS) a high resolution digital photograph.[41]

Intellectual Property

- Initial deductions for gifts of patents or other intellectual property (including certain copyrights, trademarks, trade names, trade secrets, know-how, certain software, etc.) are limited to the lesser of the donor's basis in the property and the fair market value.[42]
- Additional deductions may be available in subsequent years based on the income, if any, from donated intellectual property.[43] A certain amount of record-keeping and reporting is required of the charity which may be burdensome for smaller entities.
- Taxpayers wishing to assign royalties must assign both the royalties and the source of the royalties to the charity. Otherwise the royalties will be includible in the donor's taxable income even though they are paid to the charity.[44] The donor would then get a deduction for the amount of the royalties actually paid to the charity but the charitable deduction limitations will likely be lower than the amount taken into income.

In sum, non-cash assets present unique issues that both the donor and the donee must consider prior to making and accepting a gift. For the donor, gifts of alternative assets should be structured properly to maximize tax deductions and minimize any income or gain recognition. For the donee, considerations such as the production of unrelated business income, restrictions on transfer, environmental liability, lack of marketability, carrying costs, record-keeping and reporting requirements should also be weighed before a gift is accepted.

Endnotes

1. IRC §2055; Treas. Reg. §20.2055-1.
2. See Schedule A of Form 1040 and IRC §68.
3. IRC §170(c)(2)(A).
4. IRC §170(b)(1)(G); Treas. Reg. §1.170A-8(a).
5. IRC §170(b)(1).
6. While this article focuses on gifts to public charities and private non-operating foundations, numerous other charitable giving options exist including gifts to donor advised funds, private operating foundations, supporting organizations and split-interest trusts.
7. IRC §170(b)(1)(C).
8. IRC §170(b)(1)(D).
9. IRC §170(e)(5).
10. IRC §170(e); Treas. Reg. §§1.170A-1(c) and 1.170A-4.
11. Treas. Reg. §1.1001-2(a)(4)(v); Rev. Rul. 75-194, 1975-1 C.B. 80; *See also Goodman v. U.S.*, 2000-1 U.S.T.C. ¶50,162 (S.D. Fla. 1999).
12. Treas. Reg. §1.170A-7(a)(2).
13. Unlike S-corp stock, only the portion of income attributable to a partnership or LLC's unrelated commercial activities is subject to UBTI tax, not income from passive investments such as interest, dividends and capital gains. *See* IRC §512 (c) and Treas. Reg. §1.512(c)-1.
14. IRC §170(f)(11)(C); Treas. Reg. §1.170A-13(c).
15. Treas. Reg. §1.170A-13(c)(2).
16. IRC §170(e)(1).
17. IRC §512(e)(1).
18. IRC §512(e)(1)(B)(ii).
19. IRC §4943(c)(7).
20. P.L.R. 9247018.
21. Treas. Reg. §1.170A-13(c)(2).
22. IRC §422(b)(5).
23. IRC §422(a)(1).
24. Treas. Reg. §§1.83-1(c) and 1.83-7.
25. P.L. 109-280.
26. IRC §408(d)(8).
27. P.L. 112-240.
28. IRC §170(e)(1); Treas. Reg. §1.170A-4(b)(4).
29. Treas. Reg. §1.170A-7(a)(2).
30. Treas. Reg. §1.170A-7(b)(1)(i).
31. IRC §170(f)(11)(C); Treas. Reg. §1.170A-13(c).
32. IRC §170(e)(1)(B)(i).
33. IRC §170(e); Treas. Reg. §1.170A-4(b)(1).
34. IRC §170(e)(7).
35. IRC §170(o).
36. IRC §170(o)(4).
37. IRC §170(o)(3).
38. Treas. Reg. §1.170A-7(b)(1).
39. IRC §2055(e)(4); Treas. Reg. §20.2055-2(e)(1)(ii).
40. Treas. Reg. §1.170A-13(c).
41. See 1990-8 I.R.B. 25 and Instructions to Form 8283.
42. IRC §170(e)(1)(B)(iii).
43. IRC §170(m).
44. *See Moore v. Comr.*, T.C. Memo 1968-110.

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Mediation: It's Not Just When the Marriage Breaks Up

By Antonia J. Martinez and Robert W. Shaw

Individuals are familiar with the concept of mediation in divorce and child custody disputes. Mediation is often a cost-effective alternative to litigation. It can be an equally effective alternative to litigated guardianship proceedings, or to resolve heated disputes among feuding siblings with opposing views concerning where mom should reside, how much assistance dad really needs, or how money is being spent. The potential for mediation to resolve these sorts of disputes is only beginning to emerge and New York State still has a long way to go.

Mediation should be distinguished from arbitration, another form of alternative dispute resolution. Arbitration utilizes an independent fact-finder to make decisions for the parties based on the facts presented by all involved in the arbitration. The decision of the arbitrator is final and the parties to the conflict are bound to his or her decision. In mediation, the mediator does not make decisions for the parties. Instead, participants make their own decisions under the mediator's guidance.

Diverse Mediation Models

There are different types of mediation and mediator styles. The *evaluative model* focuses on the law and legal questions pertinent to the matter at hand. That is, the legal issues presented will be the primary focus of the mediation. A second model in which law is not used as the means to resolve a dispute is the *transformative model*, where the mediator is there to help the parties reach agreement, but does not necessarily have a background in the subject matter of the dispute. A third and ideal model for the family conflict arena is the *facilitative model*. In the facilitative modality, the law is brought into the mediation not for the purpose of resolving the dispute but rather to guide the parties in how the dispute will be settled in the courtroom if the parties are unable to reach an agreement. In a family dispute scenario, a mediator experienced in the field of Elder Law and Trusts & Estates is an asset to the resolution of the dispute.

Types of family disputes in which mediation should be considered include the following:

a) A parent is suffering from physical decline and / or early stage dementia where the children residing in multiple states are fighting amongst themselves or with the parent about what type of care plan should be initiated;

b) An incompetent senior has a validly executed Power of Attorney appointing two separate agents who disagree about what actions will be taken. This is particularly critical where the document requires them to act jointly;

c) A parent recently died and two adult siblings are fighting over the terms and validity of the Will, resulting in delaying probate and appointment of the Estate's Executor. One of the adult children resides in the deceased parent's house and had lived with decedent until his death. The two argue over whether the house should be sold or a financial arrangement put in place allowing the adult child to continue residing in the home. The sibling who does not reside there wants to initiate a lawsuit to force a sale of the premises since the two cannot agree on the arrangement;

d) The continued effectiveness of a care plan already in existence for a senior is now in dispute. Is a home attendant sufficient or does the senior now need assisted living or nursing home care? The three adult children each have a different point of view and the senior's perspective has not been articulated during the heated arguments that have ensued among bickering siblings.

Underlying Interests

What is each dispute really about? Is it really about settling the estate or is it about the resentment Susie bears towards Bill for all the years mom and dad favored Bill, and bought him expensive gifts, even though he was financially well established? Susie feels unappreciated for everything she did for her parents over the course of many years, as she was the one who lived close by, provided care, arranged medical appointments and gave of herself at the expense of her own family of three children and husband who grew resentful over her involvement. The dispute for her is not about the money in the estate but over the lack of recognition she received throughout her life.

In all of the above examples, there are multiple advantages to avoiding a courtroom as a forum for dispute resolution. Familial "issues" going back to childhood are often the real reasons behind hardened positions. These are relationship conflicts not only between parent and child, but between siblings. Media-

tion offers the opportunity to go beyond the surface issue and explore the family dynamics behind the problem. Mediation gives the parties an opportunity to vent, and when done successfully will go beneath the issues to uncover the real needs of each party, as opposed to each party's announced positions. What can often cause a family crisis and a stalemate on resolution is instead a failure to look at underlying needs and feelings of the parties. The courtroom is not the appropriate forum to address these underlying interests, whereas mediation gives the parties the room and time they need to hear one another's positions. An understanding of the other party's perspective can result in a shift of position once the mediation looks beyond the surface issues.

Efficiency of Mediation in Elder Law and Probate Arena

Mediation is an alternative to putting a case through the court system, where cases may be drawn out for several years, costing many thousands of dollars, and utilizing limited court resources. Time, in particular, is critical to senior citizens and the disabled. Mediation offers a speedier resolution, allows the voice of the senior to be heard, and offers greater privacy than litigation.

Family dispute mediation reduces stress for the individual parties and presents opportunities for creative problem solving. A mediation can be conducted in a less formalized setting than a trial court, and with the help of the mediator, determine the topics of discussion, including what issues to raise and which ones should be limited. It is an opportunity for the parties to vent with greater flexibility of time than on a court calendar.

Elder Law Attorney and Mediation

Many elder law attorneys incorrectly perceive themselves as family mediators. They are not. The role of the elder law attorney is significantly different. An attorney is an advocate who must represent his or her client with reasonable diligence.[1] It is the role of the mediator to facilitate a solution or set of solutions to parties ensnared in a dispute that can arise from competing interests that originate with family dynamics and resentments harbored over the course of many years and sometimes decades. The elder law attorney will make recommendations about particular planning options, whereas the elder mediator offers a forum for each voice to be heard. The role of the elder law attorney is to bring the legal issues to resolution promptly and efficiently, whereas the mediator's role is to oversee a process that allows all parties to fully articulate their positions and exchange their personal views.

Elder Mediation: Is It in New York State's Future?

In New York State, given the current state of the overloaded court calendars, the climate is ripe for a greater role for mediation in guardianship proceedings and contested probate matters. Should New York State create a specific framework and methodology to establish criteria for mediation in certain probate proceedings? What is to be gained by such action? First, significant savings of legal expenses will inure to the benefit of the litigants. Second, mediation will conserve limited court resources. Even when mediation fails to resolve all aspects of a dispute, the issues remaining before the Court for resolution typically are more narrowly focused as a result of the mediation process. Third, the parties to the mediation, no longer constrained by the Rules of Evidence and eager to be heard, will have a forum to talk about the underlying issues that resulted in the conflict. Even in situations where mediation fails, the litigants return to Court with a better understanding of the court process.

Mediation has been an important part of alternative dispute resolution in other states throughout the United States for many years. It is time to bring mediation to the forefront in New York for the many areas of conflict one encounters in Elder Law and in Trusts and Estates practice. Should New York follow other states that have initiated mediation programs such as Texas, Florida, California, Georgia, Hawaii, Arizona, Michigan, New Hampshire, Utah, and Washington? Given that New York was the very last state in our country to authorize no-fault divorce, one cannot be hopeful. At a Symposium at Albany Law School in March 2012, New York's Chief Judge Jonathan Lippman noted the courts were contemplating strategies to reduce expenses, increase efficiency and lighten calendars.[2] The climate is ripe for the establishment of criteria in the area of trusts and estates and guardianship matters to permit litigious parties to resolve disputes with better long term results through mediation. It is the responsibility of the bar to inform and educate the public about the opportunity and advantages afforded parties to a mediation.

Endnotes

1. New York Rules of Prof'l Conduct, R. 1.3 (2010).
2. *State Bar News*, NYSBA at p. 28 (May / June 2012).

Antonia J. Martinez, Esq., is a principal of Elder & Family Mediation Services of New York, LLC and devotes substantially all her professional time to Trusts and Estates and Elder Law matters. Ms. Martinez is a member of the Executive Committee of the New York State Bar Association Elder Law Section and serves as Vice Chair of its Veteran's Affairs and

Mediation Committee. Ms. Martinez is a speaker at Continuing Legal Education programs as well as community programs. Her articles in *The Elder Law Times, Professional Planning for Wealth & Lifestyle Preservation* are distributed to the general public. Antonia J. Martinez is a 1982 graduate of Harvard Law School.

Robert W. Shaw, Esq. is an attorney in White Plains, New York and a principal of Elder & Family Mediation Services of New York, LLC. He focuses his practice in the areas of elder law and estate planning. Mr. Shaw received his J.D. from The University of Toledo College of Law and his B.A. from Lycoming College. He is a member of the National Academy of Elder Law Attorneys (NAELA) and the Elder Law and Trusts and Estates Law Sections of the New York State and Westchester County Bar Associations. He is a member of the Mediation Committee of the NYSBA Elder Law Section.

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Upcoming Events

Fall Section Meeting
October 10-11, 2013
Binghamton Riverwalk Hotel
Binghamton, New York

The Basics of the Trusts and Estates Field for Young and Newly Admitted Attorneys
September 17 and September 24, 2013
New York Law School
New York City

11th Annual *Sophisticated Trusts and Estates Institute*
November 2013
New York City

For more information visit our website at:
www.nysba.org/trusts

2013 Legislative Update and Summary

By Ian W. MacLean and Robert M. Harper

The New York Legislature had a particularly busy 2013 legislative session—so busy, in fact, that it ended in the early morning of June 22, rather than the typical close of business on June 21. The Trusts and Estates Law Section and the members of its several committees were busy proposing several legislative initiatives and commenting on (and usually supporting) initiatives introduced independently by legislators or by other trusts and estates-related entities.

There were more than a dozen legislative proposals and bills that bore on the trusts and estates laws of New York. Six important initiatives passed and (as of this writing) await delivery to the Governor for signature. Many equally important amendments to improve existing law—either by providing clarity, removing the basis for differing interpretations by the Surrogates, or adding entirely new sections—failed to pass both houses. A summary of the legislative proposals and bills with relevant bill numbers follows.

- Not for Profit Corporation Law—A8072 / S5845. Enacts the "Non-Profit Revitalization Act of 2013," which relates to the reform of charitable organizations and adds a new Estates Powers and Trusts Law ("EPTL") Section 8-1.9. The New York State Bar Association supported this bill. The bill passed both houses and awaits delivery to the Governor.
- Anti-Lapse Statute—A6555 / S4852. The Section reviewed and offered a memorandum in support of a proposal by the Office of Court Administration that clarifies the application of the anti-lapse statute in relation to multi-generational gifts and the issue of a testator's siblings. The bill passed both houses of the Legislature and awaits delivery to the Governor.
- Decanting—A7061 / S3790. The Section reviewed and offered a memorandum in support of a proposal by the Office of Court Administration that modifies and expands the authority of a trustee to decant a trust to another trust and the authority of a trustee to exercise a power of appointment and invade trust principal. The bill passed both houses and awaits delivery to the Governor.
- Interest on Legacies—A1185 / S4952. The Section proposed legislation that clarifies the application of interest on legacies not paid within seven months of the issuance of letters and establishes an interest rate in tune with current economic conditions and tied to an understandable economic indicator interest rate. The proposal was supported by the Office of Court Administration, the New York City Bar Association and the New York Bankers Association. This is the third year that this proposal has been put before the Legislature. The bill, introduced in both houses after careful review by the respective Judiciary Committees, again passed the Assembly and yet failed again to pass in the Senate.
- QDOT Trusts & New York Estate Tax—A6556 / S4851. The Section issued a memorandum in support of an initiative concerning the tax treatment of trusts created for surviving spouses who are not U.S. citizens. The bill passed both houses of the Legislature and awaits delivery to the Governor.
- Abatement for Certain Residential Property—A6658 / S4600. This bill was issued by the New York City Bar Association and relates to partial tax abatements for certain residential real property held in trust. The bill passed both houses of the Legislature and awaits delivery to the Governor.
- Right of Election Disclosure Requirements—A0855. This bill would require prior disclosure of a decedent's income, assets and financial obligations to enforce a surviving spouse's waiver of the right of election. The bill was reviewed by the Assembly Judiciary Committee, but did not progress any further in the Legislature.
- Resignation of a Fiduciary—A7062 / S4272. This bill relates to settlement of an account by a resigning fiduciary and clarifies what is the existing practice in most, if not, all counties. The bill passed both houses of the Legislature and awaits delivery to the Governor.
- Computation of Trustee Commissions and the Power to Adjust. The Section issued a memorandum in support of and lobbied for a bill that clarifies the computation of a trustee's commissions following the exercise of the trustee's power to adjust between income and principal under the existing New York Prudent Investor Act. The New York City Bar Association and the New York State Bankers Association both supported the proposal. The proposal was reviewed by the Judiciary Committees of both houses of the Legislature, but was not introduced.

(continued on page 22)


Scenes from the
Trusts and Estates Law Section
SPRING MEETING
May 2–5, 2013
Fairmont Southampton • Bermuda









(Continued from page 19)

- Marriage Equality Act Amendments to SCPA & EPTL—A7100. The Section issued a memorandum in support of and lobbied for amendments to Articles 4 and 6 of the EPTL and Articles 10, 13, and 17 of the SCPA. The proposal suggested changes to the EPTL and SCPA to reflect gender-neutral language that is consistent with New York's recently enacted Marriage Equality Act. The Marriage Equality Act legalized same-sex marriage in New York. Although the proposal passed the Assembly, it did not garner a sponsor in the Senate.
- Exoneration Clauses in Inter Vivos Trusts. The Section issued a memorandum in support of and lobbied for amendments to EPTL Section 11-1.7, which provides that exculpatory provisions in testamentary instruments purporting to absolve executors and testamentary trustees from liability for the failure to exercise reasonable care are void and unenforceable. Under the proposal, similar exculpatory provisions in inter vivos trusts, which currently are enforceable (except to the extent they seek to absolve trustees from liability for bad faith, self-dealing, gross negligence, and reckless indifference) are violative of public policy. This proposal was not introduced as a bill.
- Posthumous Annulment and the Right of Election. The Section issued a memorandum in support of and lobbied for amendments to EPTL Section 5-1.2, which addresses the grounds upon which a surviving spouse may be deemed disqualified to take an elective share of a decedent's estate. Although recent case law authorizes courts to disqualify a surviving spouse for "equitable" reasons, the proposed amendment would permit the disqualification of a spouse based upon the posthumous annulment of the spouse's marriage to a decedent. This proposal was not introduced in the Legislature.
- Posthumously-Conceived Children's Inheritance Rights—A7461 / S4779-A. This bill provides that certain posthumously conceived children can inherit as distributees and beneficiaries of class gifts benefiting the "children" of their natural parents. This bill, which was written by the Office of Court Administration, passed in the Assembly, but did not advance to a vote in the Senate.
- Reduced Interest Rate on Taxable Escheated Property—A5960 / S4310-A. This bill provides for a reduced rate of interest applicable to certain additions of tax resulting from discovery after filing an estate tax return of certain assets belonging to the decedent held by the state comptroller as abandoned property. The bill passed both houses and awaits delivery to the Governor.

As the Co-Chairs of the Legislation and Governmental Relations Committee, we wish to thank the committee chairs and many Section members who worked diligently on the Section's initiatives and on the proposals by OCA, the City Bar, the Banker's Association and others. The hard work and expertise of many Section members is evident in the high quality of the analysis and clarity of the proposals and reviews. It is highly rewarding to be part of so many important legislative initiatives and successful legislation.

Ian W. MacLean is the Co-Chair of the Legislation and Governmental Relations Committee of the Trusts and Estates Law Section. He has been an active member of the Section's Executive Committee for nine years and a chair of a various committees for eight years. He is the principal attorney at the MacLean Law Firm, P.C. and concentrates in estate and trust litigation.

Robert M. Harper is the Co-Chair of the Legislation and Governmental Relations Committee of the Trusts and Estates Law Section. He is an associate in the trusts and estates litigation department at Farrell Fritz, P.C. and serves as a Special Professor of Law at Hofstra University's Maurice A. Deane School of Law.

Press Release from New York Bar Foundation

Albany and Brooklyn Law Students Receive New York Bar Foundation Fellowships

David Kober of Brooklyn Law School and Kaivan Mangouri of Albany Law School are the 2013 recipients of The New York Bar Foundation's Trusts and Estates Law Section Fellowships.

David Kober

As the recipients of $5,000 fellowships, Kober this summer will work in the chambers of Richmond County Surrogate Judge Robert J. Gigante in Staten Island and Mangouri will work in the chambers of Schenectady County Surrogate Judge Vincent W. Versaci in Schenectady.

"The fellowship and scholarship programs are one of the many ways that the legal profession gives so much to so many through The Foundation," said Bar Foundation President Cristine Cioffi (Cioffi*Slezak*Wildgrube). "Association section and individual attorney support enable us to provide meaningful opportunities to law students throughout New York."

"The committee was very impressed with the quality and interest of the law school applicants this year, making the committee's decision very difficult," said Carl Baker of Glens Falls, chair of the State Bar Association's Trusts and Estates Law Section (FitzGerald Morris Baker Firth). "We are pleased with the success of this program which seeks to provide a valuable experience in the practice of trusts and estates law to future New York practitioners."

Kober, a graduate of New York University, recently interned at the New York City Surrogate's Court. He previously interned at the Kings County Supreme Court Law Department, Office of the New York State Attorney General and Rosensteel Law. He expects to graduate in June 2014.

Kaivan Mangouri

"I look forward to working in Surrogate Gigante's Chambers and to forging connections amongst my esteemed future colleagues, members of the State Bar Association's Trusts and Estates Law Section," said Kober. "I am optimistic that by familiarizing myself with the inner workings of the Trusts and Estates community by working with the judicial system, as well as a well-established network of professionals, I will start off my career in the best way possible."

A graduate of Arizona State University, Mangouri previously was a law intern with the City of Albany Law Department, as well as Albany Law School's Civil Rights and Disabilities Law and Health Law clinics. He also was a faculty research assistant to Prof. Robert Heverly, interim director of the Government Law Center. He is a member of the State Bar Association's Business Law and Health Law Sections. He expects to graduate in May 2014.

"I am thrilled to have the opportunity to work with Judge Versaci this summer and grateful for the networking opportunities provided by the New York Bar Foundation," said Mangouri. "I hope to build on my current skill set and deepen my understanding of Trusts and Estates law."

The New York Bar Foundation is dedicated to aiding charitable and educational projects to meet the law-related needs of the public and the legal profession. To learn more about The New York Bar Foundation and how you can support its charitable programs, go to www.tnybf.org, phone (518) 487-5651 or e-mail nybarfoundation@tnybf.org.

RECENT NEW YORK STATE DECISIONS

By Ira M. Bloom and William P. LaPiana

Ira M. Bloom

ADOPTEDS

Child Adopted Out After Adoptive Parent's Death Is Still His Child for Purposes of His Instruments

Husband and wife had five birth children and one adopted child, a daughter. Husband created two lifetime trusts, one for the benefit of his "children" who were defined as his then four living birth children, identified by name, and "any additional children born to or adopted by" Husband after creation of the trust, and the other for all six then living children who were identified by name. His will created testamentary trusts, the beneficiaries of which included children "legally adopted" at the date of his death. After his death his widow surrendered her parental rights to her adopted daughter so that she could be adopted by another couple. The child's adoptive parents then petitioned for compulsory accountings in the lifetime and testamentary trusts on the grounds that the child was a beneficiary of all of the trusts created by Husband. The Surrogate ordered the trustees to account and the intermediate appellate court affirmed, holding that under the language of the various trusts the child was either mentioned by name or included in the definition of children and that her subsequent adoption out of the family was irrelevant. *Matter of Svenningsen*, 105 A.D.3d 164, 959 N.Y.S.2d 237 (2d Dep't 2013).

CONTRACTS TO DEVISE

General Disposition in Will Not Substitute for Satisfaction of Promised Gift

Grandfather and son-in-law entered into an agreement requiring them to make certain testamentary gifts to son-in-law's children ("the grandchildren"). Son-in-law died and left his entire residuary estate to the grandchildren, a gift far in excess of his obligation under the agreement. Grandfather's will made general dispositions of cash to the grandchildren who instituted a proceeding to determine the validity of their claims under the agreement. Grandchildren and the executors filed cross-motions for summary judgment. After a thorough review of the law on the satisfaction of decedent's debts by gifts in the decedent's will, the Surrogate granted summary judgment to the grandchildren because the executors presented no evidence that

William P. LaPiana

grandfather intended the testamentary dispositions to satisfy the grandchildren's claim under the agreement. *Matter of Horowitz*, __ Misc.3d __, 961 N.Y.S.2d 854 (Sur. Ct., Nassau Co. 2013).

DOCUMENTS

Prenuptial Agreement Void for Improper Acknowledgment

Plaintiff in divorce action moved for summary judgment determining that the parties' prenuptial agreement was void because not properly acknowledgement as required by Domestic Relations Law § 236(B)(3). The trial court agreed that the certificate of acknowledgment was insufficient. It did not conform to the requirements of Real Property Law § 303 because it failed to state that the person taking the acknowledgment "knows or has satisfactory evidence" that the person making the acknowledgment is the person who executed the instrument. The trial court denied the motion and the Appellate Division affirmed, holding the affidavit of the notary who took the acknowledgment raised a triable issue of fact whether the parties did indeed properly acknowledge the instrument. The Court of Appeals then reversed the Appellate Division, holding that the affidavit of the notary, who did not remember the event, did not sufficiently describe "a specific protocol that the notary repeatedly and invariably used" and therefore was not sufficient to raise a triable issue, assuming the faulty acknowledgment could be cured. *Galetta v. Galetta*, __ N.Y.3d __, __ N.Y.S.2d __, 2013 N.Y. Slip Op. 03871, 2013 WL 233842 (2013).

FIDUCIARIES

Co-Executor Has Standing to Object to Account Filed by Co-Executor

Two of decedent's six adult children qualified as co-executors of her will. One co-executor, a son, received only personal property under the will; the other, a daughter, and three other children were residuary beneficiaries. The daughter filed a petition for judicial settlement of her account and the son filed objections contending that it did not properly list the personal property given to him and, second, that the account did not list all uncollected debts owed the estate, in particular, a debt owed by one of the other beneficiaries. The

Surrogate dismissed the son's objections. The Appellate Division reversed, holding that as a beneficiary, the son's standing comes only from the objection related to the personal property; because he is not a residuary beneficiary he could not benefit from a finding that the objection related to the alleged uncollected debt. The Appellate Division also held that the son has standing as a co-executor to file both objections because he has a duty to collect the decedent's assets and cannot be prevented from fulfilling that duty, even though all of the residuary beneficiaries have approved the account. *Matter of Schultz*, 104 A.D.3d 1146, 961 N.Y.S.2d 618 (4th Dep't 2013).

TRUSTS

Surviving Spouse Has Right to Object to Accounting for Revocable Trust Which Is Testamentary Substitute

Husband and wife created a joint revocable trust in 1991. After wife's death in 1995, their two children became co-trustees with their father who remarried and was survived by his second spouse. After husband's death in 2005 the two children filed a petition for judicial settlement of the trust along with an accounting from the creation of the trust to 2006. Surviving spouse objected and following trial the Surrogate surcharged the co-trustees, finding that the accounting was not complete and accurate, that they had failed to exercise diligence in managing the trust and that son had engaged in self-dealing. Son appealed on the ground that surviving spouse lacked standing because she was only a contingent beneficiary of the trust until husband died. The Appellate Division affirmed the Surrogate, finding that surviving spouse was not a beneficiary at all, but because the trust was a testamentary substitute for elective share purposes and surviving spouse therefore was entitled to a portion of the trust "by operation of law," she has standing to object to the accounting for the period beginning with the son and daughter becoming successor co-trustees in 1995. *Matter of Garrasi Family Trust*, 104 A.D.3d 990, 961 N.Y.S.2d 594 (3d Dep't 2013).

Surcharge Not Warranted for Delay in Distribution of Stocks Where Beneficiaries Did Not Request Sale of Shares

Trust beneficiaries objected to trustee's accounting because of long delay following request that trusts be distributed in kind. The Surrogate imposed surcharges on the trustee in the amount of the difference between the value of the stocks at the time of the respective requests and at the time of distribution, denied objectants' request for legal fees, and awarded commissions and legal fees to the trustee. Trustee and objectants appealed. The Appellate Division reversed the surcharges but affirmed the denial of legal fees and the allowance of commissions. Never having asked the trustee to sell the stock when the stock was finally distributed, the beneficiaries were in the same position they would have been had the stock been distributed sooner; damages cannot be calculated on the assumption that the beneficiaries would have sold the stock once it was distributed to them. It was not improvident to allow the trustee to take commissions because the trustee did not engage in "fraud, gross neglect of duty, intentional harm to the trust, sheer indifference to the rights of others or disloyalty." The delay in distribution did not justify denying the trustee his legal fees and the beneficiaries were not entitled to their legal fees, especially given the elimination of the surcharge. *Matter of Lasdon*, 105 A.D.3d 499, 963 N.Y.S.2d 99 (1st Dep't 2013).

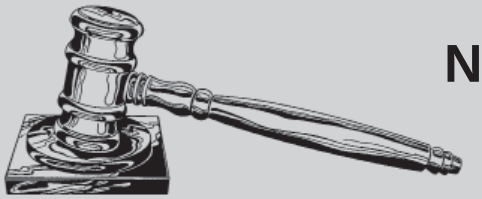
WILLS

Document Lacks Testamentary Intent

Decedent's surviving spouse petitioned for probate of two instruments purporting to be decedent's will and a codicil thereto. Decedent's son cross-petitioned for probate of a document signed by the decedent and two witnesses and a notary public commissioned in Pennsylvania, and dated after the dates on the purported will and codicil. The Surrogate granted the surviving spouse's motion to dismiss the cross petition, holding that the language of the document offered by the son does not evidence testamentary intent: it begins by stating that the instructions it contains are to be "instituted as soon as possible" and does not make any dispositions to take effect at death. *Matter of Wolf*, 38 Misc. 3d 564, 958 N.Y.S.2d 867 (Sur. Ct., Kings Co. 2012).

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. Lexis Nexis).



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

By Ilene Sherwyn Cooper

Construction

In *Matter of Phillips*, the Appellate Division, Fourth Department, modified an Order of the Surrogate's Court, Erie County, which granted respondent's cross-motion for summary judgment, and remanded the matter for further proceedings on the issue of the construction of the decedent's Will.

The record revealed that the decedent's Will left his estate to his three daughters and to his live-in girlfriend. In pertinent part, his estate consisted of his home, the lot on which it was situated, and 88 acres of farmland adjacent to the lot. In Article Four of his Will, the decedent bequeathed his residence, and the "plot of land appurtenant thereto" to his girlfriend, and the balance of his estate in equal shares to his daughters.

In her proceeding for construction of the instrument, one of the decedent's daughters sought a determination that the bequest of the decedent's home included only the land on which it was situated, and not the adjacent farmland. Petitioner attached extrinsic evidence supporting the proposed construction. Respondent / girlfriend of the decedent opposed the petition, and more particularly petitioner's use of extrinsic evidence to support her application, contending that the Will was clear and unambiguous that she was entitled to the decedent's home, lot and farmland. Both sides moved for summary judgment, and the Surrogate found for the respondent, concluding that the decedent's intent could be inferred from the Will, and that reference to extrinsic evidence was improper.

The Appellate Division disagreed. The Court opined that while the best indicator of a testator's intent will generally be found within the four corners of the Will, where a provision in the instrument is ambiguous, extrinsic evidence is properly considered.

The Court noted that while the definition of the term "appurtenant" suggests something incidental that does not have an independent existence, the intent of the testator in utilizing that term in his Will could not be gleaned by reliance on a dictionary, but rather from the context in which the Will was created. To this extent, the Court held that the provisions of the Will were unclear as to what the decedent intended. Indeed, the Court found that the submissions of the parties raised issues of fact concerning the decedent's intent. Specifically, the Court noted that the evidence offered by the petitioner, consisting of the deposition of the attorney-draftsman and a questionnaire completed by the decedent, suggested that the decedent intended his girlfriend to only receive his home and the plot of land on which it stood. However, the evidence submitted by the decedent's girlfriend indicated that when the decedent originally purchased the lot and farmland it consisted of one parcel, and the decedent partitioned the parcel only in anticipation of his impending divorce. Additionally, the respondent asserted that the utilities located on the farmland were attached to the meters located inside the residence.

Accordingly, the Court concluded that the parties should be given the opportunity to present extrinsic evidence at a hearing before the Surrogate regarding the decedent's intended distribution.

Matter of Phillips, 101 A.D.3d 1706, 957 N.Y.S.2d 778 (4th Dep't 2012).

Contempt

Before the Surrogate's Court, Nassau County, in *In re Harvey*, was an application instituted by the decedent's daughter to hold the respondent, her brother, in contempt of court for failing to file an account of his proceedings as trustee of two revocable trusts that had been created by their parents, and to have the respondent's letters of trusteeship revoked. The record revealed that the Court had directed the respondent to account in November, 2010, and that the order had been personally served on him.

Although the respondent opposed the application for contempt with a commitment to file his account within 60 days, the Court noted that said date had long passed without accountings being filed. Moreover, while the respondent argued that the provisions of the trust instruments required application of Florida law to the controversy, the Court discredited respondent's claims, concluding that it had jurisdiction over the subject matter of the proceeding, and that the law of the forum state, i.e. New York, governed the procedural issues raised by respondent regarding the notice provided by the order to show cause seeking to hold him

in contempt. In this regard, the court held that despite typographical errors in the document, the requisite language for contempt required by the Judiciary Law was apparent on the face of the order, and any attempt by the respondent to avoid his obligations to account on this basis was nothing but posturing.

With regard to the choice of law governing the request to remove the respondent, the Court also concluded that New York law, rather than Florida law, applied. The Court found that New York had the most contacts with the trusts inasmuch as the trustee and beneficiary resided in New York, the trust assets allegedly were in New York, the estate of one of the grantors was administered in New York, and the terms of the trusts required that the supplemental needs trust created thereunder for the benefit of the petitioner conform to New York law. Moreover, the Court opined that New York had a vested interest in overseeing the administration of its estates, ensuring the protection of trust assets within its borders, and safeguarding the interests of innocent beneficiaries, by requiring fiduciaries to comply with court orders.

Accordingly, based on the foregoing record, the trustee was found to be in contempt of court, and his letters were suspended. The trustee was granted leave to purge himself of contempt by filing petitions for the judicial settlement of his account, together with accountings for the subject trusts, within thirty days from the date of personal service upon him of a certified copy of the order, or risk having his authority permanently revoked.

In re Harvey, N.Y.L.J., Jan. 14, 2013, p. 33 (Sur. Ct., Nassau Co.).

Removal of Fiduciary

In *In re Antin*, the Surrogate's Court, New York County (Anderson, S.) addressed the issue of hostility as a basis for the removal of a fiduciary, when it granted the executor's motion for summary judgment dismissing a petition for revocation of letters testamentary. The record revealed that the decedent was survived by two children: a son, who was the executor of his estate, and his daughter, who was the petitioner in the proceeding, both of whom were sole beneficiaries under his will. The court noted that since the inception of the estate the parties had demonstrated an unusually high level of animosity towards each other, and an inability to resolve even the simplest of issues without judicial intervention. The application for removal was but one of three proceedings reflective of their acrimony.

In support of her application, the petitioner alleged that the executor removed personal property from a home once owned by the decedent, but which had been deeded by the executor to himself and the petitioner, as tenants in common. The petitioner maintained that her use of the property over the years was sufficient to constitute a distribution of one-half the contents to her, and accordingly, the executor's removal of the property, albeit for safekeeping, constituted a conversion. In opposition, the executor argued that given the hostility between the parties he sought to safeguard the property from becoming a casualty of the animosity he had with his sister. The court agreed with the executor, finding that he had a duty to preserve the assets of the estate, and that the petitioner had failed to create an issue of fact on this issue requiring his removal. Additionally, petitioner claimed that the executor had liquidated estate jewelry and an IRA which she had requested be distributed to her in kind. However, the record reflected that the proceeds of the sale of these assets was utilized to pay the debts and administration expenses of the estate, and accordingly, the court found no basis for the executor's removal on this ground.

In response to the petitioner's claim that the executor's conduct was the result of vindictiveness towards her, the court opined that the friction between the parties was not in itself a sufficient basis for replacing the testator's appointee, particularly where there is no allegation of self-dealing or other clear misconduct, and the bulk of the administration had been completed. Thus, although the apparent animus between the parties was a cause for concern, the court noted that it had not resulted in a loss to the estate, other than the cost of litigation engendered by both parties, and accordingly denied removal on the grounds of hostility.

Finally, the petitioner alleged that the executor had failed to report a Swiss bank account as an asset of the estate on the Federal estate tax return. While the executor had indeed omitted the asset, the record revealed that he subsequently reported the account on the return, and the IRS had determined not to proceed against the estate as a result of the initial omission. The court accordingly held that while the executor had, to this extent, failed to fulfill his fiduciary obligations, not every breach of misconduct justified a fiduciary's removal. In view of the fact that no damage to the estate resulted from the executor's conduct, and the estate was near conclusion, removal was not warranted.

In re Antin, N.Y.L.J., Feb. 1, 2013, p. 38 (Sur. Ct., New York Co.).

Removal of Trustee

In *In re Hammerschlag*, the Surrogate's Court, New York County (Anderson, S.) was confronted with a petition by the beneficiary of a testamentary trust to compel distributions from the trust, and for removal of the trustee. The trustee moved for summary judgment dismissing the application.

The record revealed that the terms of the trust granted the trustee broad discretion to pay so much of the income and/or principal of the trust to the petitioner after due regard of her other available resources as the trustee deemed necessary or proper for her education, health, maintenance or support. The trust mandated distributions of principal to the beneficiary at ages 30 and 35, when the trust terminates.

In support of her application, the petitioner, who was then 26, alleged that she had no assets, no means of support, was homeless, and was living on the generosity of third parties. She requested monthly rental payments for an apartment for herself and her son and monthly expenses for a period of two years, as well as a lump sum payment from the trust of $15,000. The petitioner further alleged that the trustee had made no independent investigation of her needs and had acted in bad faith in rejecting her requests for funds by relying on information supplied to him about her from her mother from whom she was estranged.

The trustee opposed the application, alleging that the petitioner had engaged in various acts of fraud and criminal behavior against her mother and father, that the petitioner had failed to document her request for funds, and that he had exercised his discretion in good faith based on his desire to preserve the trust funds until petitioner was more fiscally responsible.

Based on the record, the Court denied the trustee's motion for summary relief. The Court concluded that although the trustee's discretion was extremely broad, it was not unbounded, and was subject to judicial review in order to prevent any abuse in the exercise of such authority. To this extent, viewing the record in a light most favorable to the petitioner, the Court found that the record was unclear as to whether the trustee had failed to exercise his independent judgment or adequately evaluate the beneficiary's needs before refusing to make distributions to her from the trust, and thus whether he had acted in good faith. Accordingly, the court directed that a hearing be held on the allegations contained in the petition.

In re Hammerschlag, N.Y.L.J., Apr. 24, 2013, p. 22 (Sur. Ct., New York Co.).

Sealing of Record

Before the court was an ex parte application by the preliminary executors to seal the records of the estate. The decedent owned a commercial real estate company and six commercial properties at her death. The petitioners requested that the courts seal all information concerning revenues, expenses and profits of the estate properties, annual financial statements and appraisal, claiming that disclosure of such information would place the estate at an economic disadvantage in any future attempt to sell the assets, and would be detrimental to any request for deferral of estate taxes.

The court held that there is a presumption under New York law that the public is entitled to access to judicial proceedings and court records. As such, a party seeking to seal court records has the burden to demonstrate compelling circumstances to justify restricting public access. Conclusory assertions of the need for confidentiality are insufficient to justify sealing an otherwise public record. On this basis the Court found that the petitioners had only hypothesized about events, potential estate liability and financial transactions related to the estate which had yet to occur.

Accordingly, it held that the request was overbroad and that disclosure with appropriate redaction would more discretely accomplish the ends sought by the estate as well as the interest of the public.

In re Patrick, N.Y.L.J., Apr. 26, 2013, p. 40 (Sur. Ct., Dutchess Co.).

Standing

Before the Surrogate's Court, Queens County, in *In re Buchwald,* was an application by the guardian of the person and property of the decedent to revoke the letters of administration issued to the Public Administrator.

The record revealed what the Court described as a recurrent scenario, when an individual appointed as a guardian pursuant to Mental Hygiene Law Article 81 does not perform her statutorily mandated duties upon the death of her ward. It appeared that the decedent died soon after the commission had issued to the petitioner, an attorney, to serve as guardian, and prior to her collection of the assets of her ward's estate, which included a claim against her ward's former attorney-in-fact. The Court noted that death of an incapacitated person, as a general matter, terminates a guardianship, extinguishes the guardian's powers, but for the duty to pay certain expenses of the ward's estate, and requires the guardian to notify others of the incapacitated person's death.

Nevertheless, in the case *sub judice*, the petitioner failed to recognize that her guardianship had ended with the death of her ward and continued to act as if she had the power to do so. As such, four months after the decedent's death, the petitioner instituted a proceeding in Supreme Court seeking a turnover of $1.2 million from her ward's attorney-in-fact. Soon thereafter, the petitioner negotiated a settlement of the action, and a stipulation of settlement was entered and "so ordered" by the Supreme Court, despite the fact that she was without power to enter such a settlement.

In the interim, the Public Administrator was appointed administrator of the decedent's estate. Thereafter, and regardless of the Court's appointment of a fiduciary, the petitioner marshaled over $3.1 million of the decedent's assets, and contacted the decedent's surviving relatives in Israel in an attempt to persuade them to nominate her as co-fiduciary to serve with the Public Administrator. Indeed, the Court noted that petitioner's conduct since the decedent's death was reflective of her intent to seek commissions as both a guardian and co-administrator c.t.a. in the sum of $106,500. Additionally, the court noted that if the petitioner acted as her own attorney in connection with the estate, she would have sought legal fees.

Subsequent thereto, the petitioner corresponded with the Public Administrator, and copied the Surrogate's Court and the Supreme Court, indicating that she was in possession of the decedent's original Will, and had been retained by the beneficiaries to seek its probate. The Public Administrator then commenced a turnover proceeding against the petitioner, and simultaneously therewith, the petitioner commenced a proceeding to revoke the letters of administration issued to the Public Administrator. Inasmuch as the petitioner was not a beneficiary of the decedent's estate, or a nominated executor in any testamentary instrument, and did not otherwise appear to be a person interested with standing to seek revocation, the Court scheduled a hearing on the issue of whether the petition should be entertained.

Based on the papers submitted at the hearing and the oral argument on the record, the Court rejected the petition, finding that the petitioner lacked standing to institute the proceeding. Moreover, the Court found that even if petitioner had standing, she had failed to assert valid grounds for the revocation of letters. The Court held that although a purported Will of the decedent had been located it did not mandate that the letters of administration issued to the Public Administrator be revoked. Rather, the Court opined that the validity of the instrument could be determined in an accounting, or by way of a separate probate proceeding.

In re Buchwald, N.Y.L.J., Mar. 1, 2013, p. 40 (Sur. Ct., Queens Co.).

Statute of Limitations

The decedent's son, the executor and beneficiary of one-half of the estate, petitioned the Court for, *inter alia*, payment of a personal claim based on pre-death loans to the decedent, pursuant to the provisions of SCPA 1805(2). The application was opposed by the petitioner's brother, the beneficiary of the remaining one-half of the estate, who moved to dismiss the petition alleging that the estate had already been distributed by the petitioner, and that the claim was barred by the statute of limitations.

The Court held that the fact that there may have been insufficient assets available in the estate with which to pay the debt owing to the petitioner did not deprive the petitioner of standing pursuant to SCPA 1805. Nevertheless, the Court held that claims represented by loans pre-dating September 23, 1993 were barred by the statute of limitations.

Specifically, the Court noted that while the provisions of SCPA 1805(3) provide for suspension of the statute of limitations from the death of the decedent until the first judicial settlement of the fiduciary's account, the statute does not create a tolling for a claim that was barred by the statute at the time of the decedent's death. Thus, when the statute of limitations has expired prior to the death of the decedent, it may be raised as a defense to a claim, and, indeed, should be asserted as a defense by the executor in fulfillment of his fiduciary duties.

The Court opined that the statute of limitations for repayment of a loan is six years from the date the cause of action accrues, which in the case of a loan represented by a check, is the date of the execution of each check. As such, the Court granted the motion to dismiss with respect to all checks pre-dating September 23, 1993.

The Court rejected the respondent's defense based upon laches, although the executor had delayed 12 years before instituting the proceeding, finding that the defense does not operate as a bar to an action at law commenced within the period fixed by the statute of limitations. Nevertheless, the Court held that the failure to expeditiously adjudicate a claim under SCPA 1805 would result in a denial of interest on the claim.

Finally, the Court concluded that the failure to institute the proceeding prior to the informal accounting provided by the executor was not a bar to the proceeding, noting that the statute pre-supposes a petition to judicially settle an account, as a personal claim cannot be paid without court approval.

In re Spiritis, N.Y.L.J., Apr. 16, 2013, p. 32 (Sur. Ct., Nassau Co.).

Validity of Trust

In an uncontested proceeding, the petitioners, co-administrators of the decedent's estate, requested a determination that the decedent created a valid revocable inter vivos trust, that they were authorized to act thereunder as successor co-trustees, and that a certain parcel of real property constituted a trust asset.

In connection with the application, the petitioners, who were the decedent's sole distributes, averred that they were unable to locate the original or even a copy of the trust agreement. Nevertheless, they were able to locate an unexecuted copy of the trust agreement, on each page of which appeared a footer reading the name of the revocable trust, an Abstract of Trust, signed by the decedent and acknowledged by his attorney, and copies of two deeds reflecting the transfer of the real property to the trust. Further, petitioners submitted an affirmation of the attorney who drafted and supervised the execution of the trust, stating that the trust had been duly executed, had been attested by two witnesses, and that the decedent had retained the original instrument. Counsel stated that the unexecuted copy of the instrument was identical in every respect to the original, and that he was unaware of any revocation of the trust by the decedent.

The court held that the absence of the executed original of the trust agreement does not prevent a finding that a valid trust exists, where the elements of a valid trust are proven. To this extent, the court found that the unexecuted copy of the trust proffered by the petitioners evidencing the existence of trust beneficiaries and trustees, in combination with the credible affirmation of the attorney-draftsman as well as the deeds transferring the realty to the trust, was sufficient to satisfy the legal requirements of a trust. Accordingly, the relief requested by the petitioners was granted.

In re Estate of Greene, N.Y.L.J., Apr. 1, 2013, p. 23 (Sur. Ct., Kings Co.) (Surr. Torres).

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Florida Update

By David Pratt and Jonathan Galler

David Pratt

CASE LAW UPDATE

Incapacity and Guardianship—Requisite Findings of Fact

Section 744.331(6)(c), Florida Statutes, provides that when a trial court determines "that a person is totally incapacitated, the order must contain findings of fact demonstrating that the individual is totally without capacity to care for herself or himself or her or his property." Florida's Third District Court of Appeal recently reversed a trial court's order determining total incapacity on grounds that the trial court failed to make the requisite findings of fact. The opinion demonstrates the degree of specificity that is expected of the trial court in making such findings. The trial court held an eight-hour hearing over the course of two days, at which twelve witnesses testified and thirty-nine exhibits were admitted into evidence. The trial court's order, however, was primarily a form order, with blank spaces in which the court noted the following concerning the alleged incapacitated person: "Imminent danger that the physical or mental health or safety will be seriously impaired. She suffers from dementia, memory loss and amnesiac cognitive impairments and delusions." The appellate court initially relinquished jurisdiction to permit the trial court to make the requisite, specific findings of fact to support the order, but due to the retirement and unavailability of the trial court judge, the appellate court ultimately reversed the order and remanded the matter for a new hearing before a successor judge.

In re Guardianship of H.K., 2013 WL 1980504 (Fla. 3d DCA May 15, 2013).

Intestate Estates—Discretion in Appointment of Personal Representative

Where a Florida resident dies intestate and leaves no surviving spouse, the person selected by a majority in interest of the heirs is entitled to preference of appointment as personal representative. Fla. Stat. § 733.301(1)(b)(2). The probate court, however, has the discretion to appoint someone *other* than the preferred person if there is record evidence showing that the preferred person is an unsuitable candidate to serve in that capacity. Florida's Second District Court of Appeal recently affirmed a probate court's exercise of its discretion in denying a petition to appoint such a candidate.

Jonathan Galler

The guardian of the minor heirs of the decedent petitioned on their behalf for the appointment of an attorney, Hugh Umsted, as personal representative. The probate court denied the petition because the court determined that Umsted had a conflict of interest that might make it difficult for him to administer the estate in the interest of all the beneficiaries. That conflict arose because Mr. Umsted had previously represented the minor heirs and, as the court noted, the minor heirs' interests with respect to a potential wrongful death settlement were unlikely to be aligned with the interests of the two other heirs. Characterizing these facts as "unusual circumstances," the appellate court affirmed the probate court's rejection of the candidate.

Long v. Willis, 2013 WL 1776705 (Fla. 2d DCA Apr. 26, 2013).

Guardianship—Surcharge Action for Breach of Duty

As Florida's Fourth District Court of Appeal recently and succinctly explained, "[a] surcharge is an adversarial proceeding in guardianship court which allows property to be recovered from a guardian who had breached his fiduciary duty to a ward." *Reed v. Long*, 11 So. 3d 237, 238 (Fla. 4th DCA 2013). In that case, Frances Reed's daughter, who was also the guardian of Reed's person, filed a claim seeking to surcharge Robert Long for breaching his fiduciary duty to Reed while he was acting as the limited guardian of her property. Reed had been in a coma for years as a result of medical malpractice. Long, who claimed to be Reed's husband, had filed a malpractice lawsuit on Reed's behalf and a loss of consortium claim on his own behalf. He obtained a settlement on both. Following those settlements, Reed's daughter filed a petition and obtained a declaratory judgment determining that Long was not, in fact, Reed's husband because she had been previously married and was never divorced. Reed's daughter then sought to surcharge Long for the settlement monies he obtained for the loss of consortium claim. She claimed that Long had breached his duty to Reed by falsely claiming to be her husband and by pursuing a loss of consortium claim for himself that may have left insufficient funds to settle the medical malpractice claim on Reed's behalf. The trial court dismissed the surcharge action with prejudice for failure to state a

claim, but the appellate court reversed on grounds that Reed's daughter should have been permitted to file an amended pleading because she may be able to state a proper surcharge cause of action.

Reed v. Long, 11 So. 3d 237 (Fla. 4th DCA 2013).

Adult Adoption

Like many states, Florida law permits adult adoptions. Fla. Stat. § 63.042. One such adult adoption garnered national attention last year but was recently set aside by the Third District Court of Appeal. Billionaire polo magnate John Goodman, who was facing criminal charges and a wrongful death lawsuit in connection with a car accident that led to the death of a college student, petitioned to adopt his adult girlfriend. The petition was granted by the trial court. Goodman did not give notice to his minor children (or to their mother, Goodman's former spouse) of his petition for adoption. As a result of the adoption, the minor children stood to lose—to Goodman's girlfriend / daughter—a substantial interest in the irrevocable trust that had been created and funded for Goodman's children. The minor children challenged the adoption post-judgment on various grounds, but the trial court denied their motion. The appellate court, however, reversed and set aside the adoption on grounds that Goodman had violated the notice provisions of the statute by failing to give notice to the minor children of his petition for adoption and that this violation constituted a fraud on the court. Interestingly, in a specially concurring opinion, one of the appellate judges also cited the New York case of *In re Robert Paul P.*, 63 N.Y.2d 233 (1984) for the proposition that "the adoption of a paramour is so contrary to the beneficent purposes of such an action that no such judgment can ever be sustained."

Goodman v. Goodman, 2013 WL 1222944 (Fla. 3d DCA Mar. 27, 2013).

Subpoena for Estate Planning File

It is a familiar situation for many estate planning attorneys. A subpoena arrives seeking the production of a deceased client's estate planning file. The rules of procedure governing how the attorney must respond will differ from one jurisdiction to the next. However, a recent decision by Florida's Second District Court of Appeal addressed the most obvious concern of most attorneys when served with such a subpoena: the attorney-client privilege. The subpoena at issue sought the entire estate planning file related to the decedent's estate, including correspondence, memoranda and notes. The attorney who was served with the subpoena served an objection on the basis that the documents requested were protected by the attorney-client privilege. The trial court held a hearing, and, even though the attorney who served the subpoena did not offer any reason why the documents should not be deemed privileged, the court ordered that the file be produced. The appellate court quashed the order and held that a party claiming that that documents sought by an opposing party are protected by the attorney-client privilege is entitled to have those documents reviewed *in camera* by the court prior to being ordered to disclose them.

Patrowicz v. Wolff, 110 So. 3d 973 (Fla. 4th DCA 2013).

Enforceability of Spendthrift Trust

Louis Steinmetz signed a personal guaranty on a loan, representing to the lender that he had over $6.5 million available to him in a trust. The trust, however, was a spendthrift trust, and when the lender sought to collect on the guaranty, the trustee refused to make trust distributions to cover Steinmetz's debt. As the Fifth District Court of Appeal recently explained, the terms of a spendthrift trust prevent the trustee from making distributions if the distributions would be available to creditors. "A valid spendthrift provision prevents a beneficiary from transferring his or her interest in the trust as well as prevents creditors or assignees of the beneficiary from reaching any of the trust funds until they are dispersed to the beneficiary." *Zlatkiss v. All America Team Concepts, LLC*, 2013 WL 2359108, *1 (Fla. 5th DCA May 31, 2013). Steinmetz's lender sought a judicial declaration that Fla. Stat. §§ 736.0501-0507—the statutes recognizing the enforceability of spendthrift trusts in Florida—violate the Florida Constitution by preventing a creditor's access to the courts. The trial and appellate courts rejected that argument on two grounds. First, the spendthrift trust statutes cannot be said to have abolished a common law right (i.e., the usual test for a violation of the right of access to the courts) because spendthrift trusts were themselves recognized in the common law prior to the enactment of the statutes. Second, the Constitutional right of access to the courts protects a party's right to bring a legal action not the party's right or ability to enforce a judgment.

Zlatkiss v. All America Team Concepts, LLC, 2013 WL 2359108 (Fla. 5th DCA May 31, 2013) (not yet final).

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