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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

Our Section has been dedicated to educating members of the Bar and the public as well as improving and modernizing the trusts and estates law through affirmative and reactive legislative initiatives. The New York State Bar Association has published two very useful and popular public interest pamphlets through the efforts of our Section, on *Why You Need a Will* and *Health Care Proxies*. We are now developing two additional pamphlets. Louis Pierro will chair a subcommittee of our Estate Planning Committee to prepare a pamphlet on the use of revocable trusts, and Warren Heilbronner, Chair of the Committee on Elderly and Disabled, will work with his Committee to prepare a pamphlet on powers of attorney. Any member who wishes to assist with the development of these pamphlets is urged to contact these Chairs or me. Pamela Champine of our Multi-state Practice Committee is working on a proposed wrongdoer statute and Gary Freidman of our Estate Litigation Committee and Colleen Carew, a member of the Surrogate's Court Committee and our new Treasurer, are chairing a subcommittee to propose legislation to address the oft-litigated issues relating to joint bank accounts.

I was privileged and pleased to represent our Section at the Fall Meeting of the Surrogate's Association. We will be working with the Surrogates and the Advisory Committees on updating and expand-

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ing the Guidelines for Guardians *ad litem*, which has been a project of our Section's Surrogate's Court Committee chaired by Surrogate Cathryn Doyle.

The Fall Meeting of our Section, held in historic Boston, was enjoyed by all who attended, and our gratitude and appreciation is extended to hard-working Co-chairs Barbara Levitan and Gary Freidman, course book editor Ilene Cooper and our member speakers, Victoria D'Angelo, Surrogate Cathryn Doyle, Stephen Hand, Nicole Marro, Gary Mund, Jonathan Rikoon, Michael Suprunowicz, and Linda Wank, as well as our Boston-based guest speakers, Hansen Reynolds and Albert Fortier, Jr., and our Golf Chair, Magdalen Gaynor, and Tennis Chair, S. Jeanne Hall. A special thank you to our corporate sponsors, J.P. Morgan Chase, Fiduciary Trust International, Brown Brothers Harriman Trust Company, Empire Valuation Consultants and Mellon. We were especially honored to be graced with the presence of the President of the Bar Association, Lorraine Power Tharp, whose welcome address to the attendees was motivational and of great interest.

Our meeting at the Annual Meeting on January 22, 2003, was aptly chaired by Eileen Caulfield Schwab. It covered the topic of Estate Tax Planning in the Low Interest Rate Environment, with presentations by Carlyn McCaffrey on charitable lead trusts, Edward Falk on split dollar and other life insurance issues, Pamela Champine on GRATs and similar techniques, and Kathryn Madigan on New York State tax and legislative updates. Our luncheon speaker was John Rausch of the Internal Revenue Service, who spoke on family limited partnership and LLC current developments. It was a very educational day and deserved the positive comments given by the attendees.

Arlene Harris

Editor's Message

This issue contains Josh Rubenstein's annual review of changes to state laws relating to estate planning and administration. I am happy he agreed to share the article with us. In addition, the Section's Legislation Committee has provided us with a status report on pending bills of interest to our Section. Keeping on the topic of legislative changes, many were made to the Florida Probate Code. John Grall of our Section has included a summary of those in his article.

The fall program in Boston had a large number attending. The material included in "Administering The Problem Estate" was informative. Gary Mund from Kings County Surrogate's Court spoke on various probate issues and his outline is very helpful to the practitioner. It has been reproduced in this issue. The chairs of the program have written on the meeting. Their article provides a summary of topics covered as well as social gatherings. For those of you who did not attend this meeting, I hope the summary will encourage you to attend our next meeting. The dates are listed in this issue.

Ira Harris was the primary "Inquiring Photographer" at the Boston meeting. The results are included in this issue. Brown Brothers Harriman Trust Co. was kind enough to photograph the participants in its golf tournament and those are also included.

Once, again, this Section thanks John Rausch, Esq. of the Internal Revenue Service for giving us the information now found on its Web site. Did you know that the Internal Revenue Service received 123,500 estate tax returns in 2000 and examined six percent of them?

Barbara Gerrard has written an informative and understandable article on the IRS Regulations regarding Electing Small Business Trusts which can be eligible shareholders of S corporations.

Ilene Cooper, who keeps us up-to-date on current cases in our area of law, has done so again. She also was the editor of the course book for the Fall Meeting, which was two volumes and included all relevant case material in the various lectures.

Various lawyers of the Baker & McKenzie firm have written on the topic of the IRS policy regarding disclosure of holders of credit cards issued by tax haven banks. As described fully in the article, it is one way in which the IRS is trying to locate bank accounts used to conceal taxable income.

When I became editor of this *Newsletter*, my goal was to provide varied topics in each issue so that there was at least one article that would benefit each reader. I believe I have succeeded in this issue. I thank all of the authors who donated their energy, time and talent in providing the articles. I also thank those who, behind the scenes, review the submissions to make certain they are suitable for inclusion in each issue.

This issue marks the retirement of John C. Welsh who has been the Recent Decisions Editor for this *Newsletter* for over a quarter century. This Section acknowledged this great contribution at our Annual Meeting. As present editor and on behalf of the past editors, I want to thank Professor Welsh for providing the summaries of pertinent cases in an informative and understandable format for these past many years. It has been an important part of the success that the *Newsletter* has enjoyed.

Magdalen Gaynor

Upcoming Meetings of Interest

May 21-June 4, 2003	New York State Bar Trusts and Estates Law Section. Estate Planning for the Middle-Class Client Full day program. Presented in eight locations throughout the state
September 11-14, 2003	New York State Bar Trusts and Estates Law Section. Fall Meeting. Fairmont Empress (Inner Harbour), Victoria, British Columbia.
October 2004	New York State Bar Trusts and Estates Law Section. Fall Meeting. Savannah, Georgia.
October 2005	New York State Bar Trusts and Estates Law Section. Fall Meeting. New Orleans, Louisiana

Extensive Amendments to Florida Elective Share, Probate Code

By John G. Grall and Richard N. Matties

Significant changes to the Florida elective share became effective for decedents dying after October 1, 2001, and many other changes to the Florida Probate Code took effect for decedents dying after December 31, 2001.

This article will provide an overview of the major changes made that are most likely of general interest to New York practitioners.

1. Florida Elective Share Strengthened

The changes to the Florida elective share are designed to extend the scope of the elective share right to some property previously not included, and to make the right to the elective share more difficult to avoid.

Property Subject to Elective Share. Classes of property subject to the elective share right are expanded. Pay on death accounts, jointly owned property, revocable transfers, individual retirement accounts and most other retirement benefits, retained life estates and income interests all may be part of the elective estate. Also, most gifts made by the decedent during the one-year period before death are included in the elective estate, other than gifts qualifying for the federal gift tax exclusion as medical or educational expenses, and gift tax annual exclusion gifts up to $10,000 to each donee (*not* up to the currently applicable federal gift tax annual exclusion of $11,000, as indexed for inflation).

Property Not Subject to Elective Share. Property irrevocably transferred by the decedent before October 1, 1999, or after that date but before the date of decedent's marriage to the electing spouse, is not included in the elective estate. Life insurance proceeds in excess of net cash surrender value, general power of appointment property, transfers made with the written consent of the spouse, community property and "qualifying special needs trust property" also are not included in the elective estate, nor is any transfer made for adequate consideration in money or money's worth.

Elective Share Rate. The rate for calculation of the surviving spouse's elective share remains unchanged at thirty percent (30%). It should be noted that the Florida legislature apparently intends to continue to study possible future enactment of a sliding scale based upon length of marriage, which is a concept that was included in the legislation as originally introduced.

Trusts for Surviving Spouse. A very significant and interesting change in the Florida elective share law allows certain trusts to satisfy, or partly satisfy, the decedent's elective share obligation. To qualify, a trust must provide the surviving spouse with mandatory distributions of all trust income at least annually, and no distributions may be made from the trust to any person other than the surviving spouse (unless the distribution is made by the surviving spouse). Such a trust providing for mandatory payment of income and a limitation of distributions to persons other than the surviving spouse may count fifty percent (50%) of its value toward satisfaction of the elective share. If a trust also allows for principal distributions to the spouse for health, support and maintenance, the trust may count eighty percent (80%). A trust that also grants the spouse a lifetime or testamentary general power of appointment may count one hundred percent (100%). In cases where special needs planning may be appropriate, a qualifying special needs trust can satisfy the elective share obligation. Such a trust is not required to provide for mandatory distribution of income. However, court approval is required unless the trust is less than $100,000, and certain other restrictions apply.

2. Other Major Changes to the Florida Probate Code

The changes to the Florida Probate Code effective for decedents dying after December 31, 2001, are numerous (185 sections are amended). The following is intended only as a brief summary of the new provisions most likely of general interest.

Section 732.503, Fla. Stat., Self-proof of will. A new suggested form of self-proof is provided that is completely rewritten, intended to be less awkward and allow for easier compliance with the statutory requirements. The new form removes the requirement of an oath by the testator, in favor of a simple declaration ("publication") of the testator to the officer, and separately, oaths of the witnesses.

Section 733.2121, Notice to creditors; filing of claims. This new provision separates notification procedures relating to creditors from those procedures relating to beneficiaries and other interested

persons. It also creates a notice to creditors, which is the required publication. The changed provision explicitly incorporates a requirement previously imposed by case law that all reasonably ascertainable creditors, including those who are contingent, are entitled to notice.

Section 733.310, Personal representative not qualified. This new provision imposes a continuing duty upon a personal representative to notify the court if he or she becomes disqualified (e.g., is convicted of a felony). A penalty for noncompliance may be imposed, which is assessment of attorney's fees incurred to accomplish removal of the disqualified personal representative.

Sections 733.502 through 733.509, Resignation and removal of personal representative. A number of statutory changes are made to make consistent and less confusing the procedures relating to removal or resignation of a personal representative, and procedures after the death of a personal representative.

Section 733.6065, Opening safe deposit box. The new statute expands the individuals who may participate in the initial box opening, by providing the opening may be conducted in the presence of any two of the following: an employee of the institution where the box is located, the personal representative, or the personal representative's attorney of record. This change makes it now possible to avoid fees imposed by banks for the presence of a bank employee. There is a new requirement that both individuals who enter the box and sign an inventory to verify the box contents must sign the inventory under penalties of perjury. Also, a copy of the box entries for the preceding six months must be filed with the court. This change is intended as a means of revealing possible entries made in fraud of beneficiaries, creditors and taxing authorities.

Section 733.609, Possession of homestead property. A new provision allows the personal representative to take possession of protected homestead property when necessary for the purpose of preserving, insuring and protecting it for the heir or beneficiary, pending the determination of homestead status. The personal representative may, but is not under a duty to, rent or otherwise make the property productive, during the personal representative's possession of the property.

Section 733.612, Prudent Investor Rule. This section is changed to clarify that the personal representative is required to take the prudent investor rule into account in investing estate funds.

Section 733.613, Personal representative's right to sell real property. This section is intended to resolve title companies' reluctance to insure title before the creditor period has ended. This change clarifies that a purchaser or lender takes title free of claims of creditors of the estate and the estate beneficiaries, provided the sale or mortgage occurs under a specific power to sell or mortgage real property in the will or under a court order authorizing or confirming the act.

Sections 735.101-735.107, 735.201, 735.206, Family Administration and Summary Administration. These changes eliminate the seldom-used mechanism of Family Administration, and expand Summary Administration to increase the limit on the size of estates eligible for summary administration from $25,000 to $75,000. To reduce the risk that qualifying larger estates for Summary Administration might lend itself to fraud on omitted creditors, there is a new requirement that the petitioner conduct a diligent and reasonable inquiry for any known or reasonably ascertained creditors, and to provide those creditors with notice of the petition. In addition, omitted creditors may be entitled to recover attorney fees against petitioners, and a mechanism is provided for pro rata apportionment of omitted creditor claims among recipients of estate property.

John G. Grall and Richard N. Matties are partners in the law firm of Levene Gouldin & Thompson, LLP, of Vestal and Binghamton, New York. Mr. Grall is serving as Sixth District Representative to the New York State Bar Association Trusts and Estates Section Executive Committee, and Mr. Matties, a former member of the Executive Committee, is serving on the Estate and Trust Tax Planning Committee of the Florida Bar Real Property, Probate and Trust Law Section.

Probate Issues

By Gary R. Mund

1. Will Execution Issues

a. Due execution. Due execution includes proper execution by the testator, acknowledgment and publication to the witnesses, and proper execution by the witnesses.

i. Testator's signature. Every will must ". . . be signed at the end thereof by the testator or, in the name of the testator, by another person in his presence and by his direction . . ." EPTL 3-2.1(a)(1).

• PRACTICE TIP •

A weak or irregular signature, which sometimes raises an issue of testamentary capacity, often can be explained and resolved by affidavit.

ii. Added matter.

(1) Matter appearing after testator's signature. "No effect shall be given to any matter, other than the attestation clause, which follows the signature of the testator . . ." EPTL 3-2.1(a)(1)(B). "The presence of any matter following the testator's signature, appearing on the will at the time of its execution, shall not invalidate such matter preceding the signature as appeared on the will at the time of its execution . . ." EPTL 3-2.1(a)(1)(A).

• PRACTICE TIP •

While a will must be signed by the testator "at the end thereof," this statutory provision should not be construed as a proscription to having a testator's initials (or even signature) in the margin or at the foot of each page of the instrument; this is actually good practice and may help to establish which pages actually form a part of the will in the event this becomes an issue, e.g., in the case of a detached (or unattached) instrument.

(2) Matter added prior to execution. There is no restriction on altering or revising the content of a will at any time prior to execution, even if such alterations are different in appearance from the underlying instrument (e.g., interlineations in pen made on a typewritten instrument).

• PRACTICE TIP •

Last-minute alterations should be avoided if possible; when such alterations are unavoidable, it is wise to have them initialed by the testator and all witnesses, and to acknowledge all pre-execution changes in the attestation clause and self-proving affidavit.

(3) Matter added subsequent to execution. "No effect shall be given to any matter . . . preceding [the signature of the testator] which was added subsequently to the execution of the will." EPTL 3-2.1(a)(1)(B).

• PRACTICE TIP •

Because the text of a will with post-execution alterations necessarily contains extraneous language, the court will typically direct that the decree admitting such will to probate recite the entire text of the will as originally constituted; in effect, the body of the decree becomes the will itself.

iii. Attesting witnesses.

(1) Requirements. A valid will requires at least two attesting witnesses, who shall sign the will after having had the testator declare the instrument to be his or her will (publication), and having witnessed the testator affix his or her signature in their presence, or having had the testator acknowledge a previously-affixed signature to them. EPTL 3-2.1(a)(2),(3),(4).

• PRACTICE TIP •

It is advisable to include a provision for having attesting witnesses print their names, as well as signing, to facilitate identifying and locating them at a later time.

(2) Absent/forgetful/hostile witnesses. It is possible to prove a will with fewer than two witnesses. Circumstances specifically mentioned in the statute are a witness' death, absence from the state, and incompetency. SCPA 1405. Testimony of forgetful or hostile witnesses may be overcome by the testimony of one or more other witnesses. SCPA 1405(3).

(a) Some witnesses unavailable. Where there are more than two attesting witnesses, there is no requirement dictating which two witnesses must be used to prove the will, and the unavailability of one witness will not alter the proof requirement if two other witnesses are available. Where only one witness is available, the court may dispense with the testimony of a second witness. SCPA 1405; *but see* SCPA 507 regarding testimony taken outside the court.

• PRACTICE TIP •

Typically, the court will require proof of unavailability by affidavit supported by, e.g., a death certificate for a deceased witness. See also Official Form No. P-8.

(b) All witnesses unavailable. If none of the attesting witnesses is available, a will may be admitted to probate by proving the handwriting of both the testator and at least one of the attesting witnesses, together with ". . . such other facts as would be sufficient to prove the will." SCPA 1405(4).

• PRACTICE TIP •

The proofs described in SCPA 1405(4) are generally made by affidavit, and such affidavits may come from any one or more individuals having actual knowledge of the handwritings and, e.g., the mental state of the testator at or about the time of the will execution.

• PRACTICE TIP •

The situation involving one or more unavailable witnesses highlights the usefulness of self-proving (SCPA 1406) affidavits executed immediately following the will execution.

(3) Notary-witness. A notary public is not *per se* disqualified from also acting as an attesting witness; he or she may also qualify as an attesting witness if sufficiently involved in the execution ceremony to meet the requirements mandated of an attesting witness.

(4) Beneficiary-witness. A witness who is a beneficiary under the will, and whose testimony is necessary to prove the will, forfeits his or her legacy, unless the beneficiary is also a distributee, in which case he or she may receive the lesser of his or her legacy or intestate share. EPTL 3-3.2.

• PRACTICE TIP •

In a beneficiary-witness situation, SCPA 1405 (dispensing with attesting witnesses' testimony) cannot be used to avoid utilizing the testimony of the otherwise competent beneficiary-witness.

• PRACTICE TIP •

The rule regarding beneficiary-witnesses does not apply to executor-witnesses; although probably not the best practice, a nominated executor may also act as an attesting witness without penalty.

(5) Ancient documents. An ancient document is defined as a document over 30 years old, taken from a natural place of custody, and of an unsuspicious nature. *In re Brittain*, 54 Misc. 2d 965, 283 N.Y.S.2d 668 (Sur. Ct., Queens Co. 1967); *In re Samelson*, 40 Misc. 2d 623, 243 N.Y.S.2d 345 (Sur. Ct., Kings Co. 1963). As a last resort, if witnesses are unavailable, a qualifying will may be proved as an ancient document and admitted to probate without further proof.

iv. Execution Ceremony.

(1) Publication. The requirement of publication is met by the testator's declaration to each of the attesting witnesses, ". . . at some time during the ceremony or ceremonies of execution and attestation . . . that the instrument to which [the testator's] signature has been affixed is his will. EPTL 3-2.1(a)(3).

(2) Timing. The attesting witnesses need not act together, provided the execution ceremony is completed within a 30-day period. Compliance with the 30-day requirement is rebuttably presumed. EPTL 3-2.1(a)(4).

v. Non-New York instruments. "A will disposing of personal property, wherever situated, or real property situated in this state, made within or without this state by a domiciliary or nondomiciliary thereof, is formally valid [valid as to manner of execution and attestation] and admissible to probate in this state, if it is in writing and signed by the testator, and otherwise executed and attested in accordance with the local law of:

(1) This state;

(2) The jurisdiction in which the will was executed, at the time of execution; or

(3) The jurisdiction in which the testator was domiciled, either at the time of execution or of death." EPTL 3-5.1(c).

• PRACTICE TIP •

This statutory provision is one possible method to probate a will in New York, such as a holographic will, which otherwise does not comply with New York's due execution requirements.

b. Testamentary capacity.

i. Age. The minimum age for executing a will is eighteen. EPTL 3-1.1.

ii. Competency requirements. "Every person . . . of sound mind and memory . . ." may execute a will. EPTL 3-1.1. The elements of testamentary capacity are an understanding of the nature and consequences of executing a will, knowledge of the nature and extent of the property being disposed of, and knowledge of those who would be considered natural objects of the testator's bounty. *In re Slade,* 106 A.D.2d 914, 483 N.Y.S.2d 513 (4th Dep't 1984).

c. Fraud. A fraudulent will is one where the testator has been induced to execute an instrument containing provisions which were made based on intentional misrepresentations of fact. NY PJI 7:60.

d. Undue influence. A will procured through the use of undue influence may be denied probate. "Undue influence" is substantially more than mere influence alone; ". . . it must be shown that the influence exercised amounted to a moral coercion, which restrained independent action and destroyed free agency, or which, by importunity which could not be resisted, constrained the testator to do that which was against his free will and desire, but which he was unable to refuse or too weak to resist." *Children's Aid Society v. Loveridge,* 70 N.Y. 387 (1877).

• PRACTICE TIP •

Taken together, the issues of due execution, testamentary capacity, fraud, and undue influence are the classic boilerplate bases for objections to probate. See SCPA 1410 regarding additional requirements for filing probate objections.

e. Multiple/sequential instruments/Revocation.

i. Effect of execution date. In general, where more than one testamentary instrument exists, it is the last in time which controls (provided it disposes of the entire estate). *See generally* EPTL 3-4.1.

ii. Will v. codicil. "A codicil is a supplement to a will, either adding to, taking from, or altering its provisions or confirming it in whole or in part by republication, but not totally revoking such will." EPTL 1-2.1. Generally, a codicil does not stand on its own, but only in conjunction with the underlying will it references; revocation of a will automatically revokes all associated codicils. EPTL 3-4.1(c). Revocation of a codicil, however, does not revoke the underlying will, but may have the undesirable effect of creating a partial intestacy. *Osburn v. Rochester Trust & Safe Deposit Co.,* 209 N.Y. 54, 102 N.E. 571 (1913).

iii. Revocation of prior instruments.

(1) Express revocation. A will or any part thereof may be revoked by express revocation language contained in another will, by a separate revocatory instrument executed in the same manner as a will, or by "[a]n act of burning, tearing, cutting, cancellation, obliteration, or other mutilation or destruction . . ." performed by the testator or at his or her direction as specified by statute. EPTL 3-4.1(a).

(2) Implied revocation. A will (or codicil) which is later in time than a prior testamentary instrument revokes the prior instrument to the extent that the dispositions in the later instrument are inconsistent with those in the prior one. Also, alterations to a will or codicil which are extensive, and which affect the testamentary scheme or the incidents of due execution, may constitute an implied revocation. *In re Lavigne*, 79 A.D.2d 975, *aff'd*, 52 N.Y.2d 1008, 420 N.E.2d 92 (1983); *In re McCaffrey*, 174 Misc. 162, 20 N.Y.S.2d 178 (1940); *see generally In re Cunnion,* 201 N.Y. 123, 94 N.E. 648 (1911).

iv. Revival. Revocation of a will does not automatically revive a prior will which was previously revoked (EPTL 3-4.6(a)), unless the statutory requirements for revival of the prior instrument are met. EPTL 3-4.6(b).

• PRACTICE TIP •

Although it is possible to revive a revoked will by formal instrument expressly reviving such will, in today's world of ubiquitous computers and word processors, it is far better practice to simply redraw and re-execute the previously revoked instrument.

v. Extrinsic documents. New York does not recognize the doctrine of incorporation by reference, unless specifically authorized by statute. Thus, the provisions of an external document referred to in a will are unenforceable unless the provisions themselves are also included in the will. *Booth v. Baptist Church*, 126 N.Y. 215, 28 N.E. 238 (1891).

(1) Pour-over trusts. A major statutory exception to the incorporation-by-reference rule is where a portion of the estate is left to the trustee of a valid *inter vivos* trust; there is very wide latitude in the nature and terms of the trust, provided only that the trust must actually be in existence at the time of death of the testator. EPTL 3-3.7.

• PRACTICE TIP •

The use of pour-over trusts is widespread and quite common. Care must be exercised, however, to insure that the trust actually exists, is valid, and continues past the date of death of the testator; a will provision which pours assets into a previously terminated inter vivos trust or, if such trust is invalid or non-existent, pursuant to the provisions of said trust prior to its termination, would fail as a prohibited incorporation by reference.

(2) Advisory lists. While extrinsic advisory lists (usually, detailed lists of dispositions of specific property to specific individuals) are often useful and expedient, they are advisory only, and not enforceable unless physically incorporated into the body of the will.

vi. Counterpart (duplicate) original wills. Generally, it is necessary to produce *all* counterparts of a will where the testator has executed more than one original, to rebut a presumption that the testator destroyed a missing original with the intent of revoking it. 2 Warren's Heaton on Surrogate's Courts § 41.13[6][a]; *see In re Staiger,* 243 N.Y. 468, 154 N.E. 312 (1926); *In re Fogarty,* 155 Misc. 727, 281 N.Y.S. 577.

• PRACTICE TIP •

It is never good practice to execute more than one original will. If necessary, photocopies should be made of the signed original after execution.

vii. Jurisdictional requirements. Where multiple testamentary instruments are filed in the court, it is necessary to join:

(1) "Any person designated in the will as beneficiary, executor, trustee or guardian whose rights or interests are adversely affected by any other instrument offered for probate that is later in date of execution or which amends or modifies an instrument offered for probate" (SCPA 1403(c)); and

(2) "Any person designated as beneficiary, executor, trustee or guardian in any other will of the same testator filed in the surrogate's court of the county in which the propounded will is filed whose rights or interests are adversely affected by the instrument offered for probate" (SCPA 1403(d)).

2. Jurisdiction Issues

a Subject matter jurisdiction.

i. Original jurisdiction. The Surrogate's Court has jurisdiction ". . . in all matters relating to estates and the affairs of decedents . . . to try and determine all questions, legal and equitable . . . in order to make a full, equitable and complete disposition of the matter by such order or decree as justice requires." SCPA 201(3).

(1) Domiciliary estates. Jurisdiction in domiciliary estates is predicated upon domicile of the decedent in New York at the time of death. Proper venue (which is not jurisdictional) is in the county of domicile. SCPA 205.

(2) Non-domiciliary estates. Jurisdiction in non-domiciliary estates is discretionary, and predicated upon the existence of decedent's property within the state, or a cause of action for wrongful death against a New York domiciliary. Proper venue is in the county where property is located, or the domicile of the putative defendant; where more than one county is proper, the first court to assert jurisdiction retains it. SCPA 206.

• PRACTICE TIP •

Because the locality of certain types of assets is movable under SCPA 208, any proceeding which relies on such property as the basis for venue would allow for some "forum shopping" among various Surrogate's Courts.

ii. Ancillary jurisdiction. Ancillary jurisdiction in New York relies on the validity of the underlying probate (or comparable) proceeding in the jurisdiction of domicile, coupled with the existence in New York of property upon which the will may operate. SCPA 1602(1).

• PRACTICE TIP •

An ancillary proceeding may only be based upon an original proceeding in the jurisdiction of domicile. Thus, it is not possible to bring an ancillary proceeding based upon a nondomiciliary proceeding in another jurisdiction. Similarly, an ancillary proceeding cannot be brought in the jurisdiction of domicile. In either case, the only recourse would be to commence an original proceeding.

While in an appropriate case the parties (or their counsel) may view the convenience of bringing an original nondomiciliary proceeding as a compelling factor, caution should always be exercised when bringing any such proceeding, to insure that no probatable assets exist in the jurisdiction of domicile. Should any such assets be discovered at a later time, it would then be necessary to commence a duplicate original proceeding in the jurisdiction of domicile, possibly requiring arrangements for the transmittal of an original will (or at least exemplified copies of documents) and other substantial inconveniences.

b. Personal jurisdiction.

i. Traditional jurisdiction.

(1) Necessary parties. The general concept of Surrogate's Court jurisdiction is that the necessary parties to any proceeding are all persons who will or might be adversely affected by the grant of the relief being sought. The class of necessary parties in a probate proceeding is, in most cases, fixed by statute. SCPA 1403(1); SCPA 1123(2)(i)(2); SCPA 1215(1)(b); SCPA 316.

(2) Effect of pre-/post-decease. The class of necessary parties is fixed at the instant of death of the decedent. Thus, the issue of a predeceased individual who otherwise would have been a distributee is resolved by statute. EPTL 4-1.1.

In the case of a post-decease, since the post-deceased party was living at the time of death of the decedent, the necessary party now becomes the estate of

the post-deceased party. This is not necessarily the party's issue, but will depend upon who constitutes the class of the post-deceased's distributees, whether the post-deceased had a will, and whether any fiduciary has been appointed in the post-deceased's estate.

• PRACTICE TIP •

Joining the estate of a post-deceased party is generally accomplished by joining the fiduciary of the post-deceased's estate, if one has been appointed and does not have any conflict of interest. Absent that, it would be necessary to join the distributees of the post-deceased and, if he or she had a will not yet admitted to probate, the legatees named in that will as well.

(3) Methods.

(a) Adult, competent parties. Jurisdiction over adult, competent parties may be obtained by acknowledged waiver and consent (SCPA 401(4)), by general appearance (SCPA 401(2)), or by service of citation (SCPA 305-312). Service of citation generally is made by personal delivery within the state, and by registered or certified mail, return receipt requested, or special mail service without the state. SCPA 307(1),(2). Other methods of service may be prescribed by the court when the foregoing methods are unsuccessful. SCPA 307(3).

• PRACTICE TIP •

When in-state service by personal delivery cannot be effected, the court will, on proper application, typically order substituted service ("delivery and mail" or "nail and mail"). When out-of-state service by registered, certified, or special mail cannot be effected, the court will often allow service by regular first-class mailing, provided a reasonable showing can be made that the respondent does, in fact, receive mail at the given address. It is important to remember that any alternative form of service other than personal delivery or mailing, as set forth in SCPA 307(1) and (2), requires a court order in advance of the service.

(b) Persons under disability. "Person under disability" is a statutorily defined term. SCPA 103(40). The manner of service will depend on the nature of the disability: service upon an infant is made upon the parent, guardian, or adult person responsible for his or her care (SCPA 307(4)); service upon an incompetent or incapacitated person is made pursuant to CPLR 309(b) and (c) (SCPA 307(5)); service upon unknowns or persons whose whereabouts are unknown is usually made by publication (SCPA 307(3)(a)); service upon a prisoner typically is made upon the prisoner individually and upon the warden of the prison facility.

• PRACTICE TIP •

It is always advisable to determine if the provisions of virtual representation (SCPA 315) can apply with respect to a person under disability, thus completely avoiding the necessity of separately acquiring jurisdiction over such person.

ii. Multiple testamentary instruments. Because of the need to join potentially adversely affected parties (SCPA 1403(c),(d)), all filed instruments (wills and codicils) must be carefully reviewed to determine their interrelationship and their impact on the interests of the persons interested in the estate.

• PRACTICE TIP •

Where a will is accompanied by multiple codicils, determining their interaction for the purpose of establishing personal jurisdiction can quickly become an overwhelming, nightmarish task. Moreover, all persons adversely affected will need to be joined as parties. For this reason, it is recommended that codicils be kept to a minimum: one, or at most, two, relating to any single will. Executing a totally new will and avoiding the use of codicils altogether, while a bit more effort at first, usually results in far less effort, inconvenience, and expense at the time of probate.

iii. Absent/unknown distributees.

(1) Due diligence. The basis for an order directing service by publication is a

showing (by affidavit) of the exercise of due diligence in attempting to identify and/or locate unknown or missing distributees. The search for distributees need not be exhaustive, but should be commensurate with the size of the estate, the nature and value of the interests sought to be joined, and the proximity or remoteness of the kinship. *See generally* 22 N.Y.C.R.R. § 207.16(d).

• PRACTICE TIP •

It is the quality of the search, not the quantity of papers filed, which helps to determine whether a sufficient amount of diligence has been exercised. Reporting that five responses, yielding no information, have been received from organizations that the decedent dealt with on a regular basis is far more valuable than reporting that no responses at all have been received from 50 randomly-polled organizations, having no relationship with the decedent or his or her family.

(2) Publication. An order of publication will be granted once there is a showing that parties are either unknown or cannot be located, despite the exercise of due diligence. It is a "last resort" technique to afford jurisdictional notice to necessary parties.

• PRACTICE TIP •

The first publication must be made within 30 days after the order is granted (CPLR 316(c)); otherwise the order is stale and a supplemental order must be submitted.

• PRACTICE TIP •

It is tempting to seek to publish early in the proceeding because of the long time frame (once a week for four weeks) involved. Nevertheless, the wiser course is to resist this temptation and delay publication until all other jurisdiction is complete; if it is discovered that an additional party whose whereabouts were believed to be known cannot be located, it is then a simple matter to incorporate that party into the affidavit of due diligence and add him or her to the order of publication. Had the same discovery been made after publication had already been completed, there would be no alternative but to publish again, a time-consuming, costly, and totally unnecessary exercise.

(3) Guardian *ad litem*. The appointment of a guardian *ad litem* to protect the interests of a person under disability is generally required. SCPA 402(2). Several notable exceptions, where the court may dispense with such appointment in probate, are when:

(a) The proceeding is uncontested and the person under disability receives a share under the will which is greater than or equal to his or her intestate share (SCPA 403(3)(a));

(b) The Public Administrator is joined on behalf of the person under disability (SCPA 403(3)(c));

(c) A surviving spouse receives the entire estate under the will, and total probate assets do not exceed $50,000, provided that the letters testamentary limit the collection of assets to an aggregate of $50,000 (SCPA 403(3)(d)).

iv. Absent/unknown/uncertain distributee class.

(1) **Status issues.** In addition to persons whose identities or whereabouts are unknown, certain status issues will raise jurisdictional questions which must be addressed. Examples of such issues would be a spouse not in good standing (EPTL 5-1.2), non-marital issue (EPTL 4-1.2), putative adopteds (EPTL 2-1.3), and parental disqualification (EPTL 4-1.4).

(2) **Joinder requirements.** Status relating to *in personam* jurisdiction may be a threshold issue, possibly requiring a hearing and determination in order to complete the probate proceeding. Often, the more expedient solution is simply to join all potential distributees as parties, irrespective of whether or not they actually have such status.

In the event uncertain status affects all members of a putative distributee class, it becomes necessary to join the next presumptive class. Thus, for example, where a decedent is survived

only by non-marital or all missing children, it would be necessary to join the parents, if any, or the siblings and their issue, if any, or whichever subsequent class has at least one known member whose status is certain.

• PRACTICE TIP •

Where objections to probate are filed by a distributee having questionable status, there is a dilemma as to whether the status issue should be resolved initially, or the matter simply proceed as a contested probate. While the specific facts will often dictate which course will be followed, it is vital to insure that jurisdiction is complete before any action is taken, so that all necessary parties will be bound by the ultimate result.

v. Other prior/concurrent proceedings.

(1) Probate of prior will. Upon application, the court will vacate a decree probating an earlier will in the event a later will is filed and sought to be probated. *See* SCPA 209(1). In the proceeding on the later will, jurisdiction would likely be required over any person having a pecuniary interest under the earlier (previously probated) will. *See* SCPA 1403(d).

(2) Probate of same will. Cross-proceedings to probate the same will usually result from a dispute over who will be granted letters. In general, a showing of ineligibility must be made to deprive a person who has priority of letters. SCPA 707; *see also* SCPA 711; SCPA 719. *See generally* SCPA 1418 and 1419 regarding priority to receive letters of administration c.t.a.

(3) Probate of later will. Because it is the last valid will which controls the disposition of the estate, the probate proceeding with respect to the last will has priority over other probate proceedings.

• PRACTICE TIP •

In general, the courts will not consider two probate proceedings for two different wills concurrently. If there is a pending proceeding and an earlier instrument is proffered, it will be received by the court for filing only; the court ordinarily will not permit a probate proceeding for that instrument to be filed at that time. Note, however, that the filing of the earlier instrument might change the jurisdictional requirements in the pending probate of the later instrument, necessitating the amendment of that probate petition and the acquiring of any additional jurisdiction.

In the event a probate proceeding is sought to be filed for a will which is later in date than that of the pending proceeding, the new proceeding will be accepted for filing, and the prior proceeding will be suspended pending the outcome of the new proceeding. Here, again, the earlier will is considered to be a will on file for jurisdictional purposes.

(4) Administration or Voluntary Administration. As with a probate proceeding for an earlier will (*supra*), a pending administration or voluntary administration proceeding will be suspended, and a completed administration or voluntary administration proceeding will be vacated, upon the filing of a probate proceeding with a will for the same decedent. Upon admission of the will to probate, the prior letters of administration, if any, must be revoked in the probate decree. SCPA 1413.

3. Fiduciary Issues

a. Ineligible fiduciaries. "Letters may issue to a natural person or to a person authorized by law to be a fiduciary except as follows:

"1. Persons ineligible

"(a) an infant

"(b) an incompetent

"(c) a non-domiciliary alien except one who is a foreign guardian as provided in subdivision four of

section one thousand seven hundred sixteen of [the EPTL], or one who shall serve with one or more co-fiduciaries, at least one of whom is resident in this state. Any appointment of a nondomiciliary alien fiduciary or a New York resident fiduciary [under this provision is] made by the court in its discretion.

"(d) a felon

"(e) one who does not possess the qualifications required of a fiduciary by reason of substance abuse, dishonesty, improvidence, want of understanding, or who is otherwise unfit for the execution of the office.

"2. Persons ineligible in court's discretion. The court may declare ineligible to act as fiduciary a person unable to read and write the English language."

SCPA 707.

• PRACTICE TIP •

The procedure set forth in subdivision (1)(c) may be used where all nominated executors are nondomiciliary aliens. However, the application must then be one for administration c.t.a., since letters testamentary can only issue to executors named in the will.

• PRACTICE TIP •

Frequently, when the proposed fiduciary is alleged to be a resident alien, the court will require proof of resident alien status ("green card") as an indication of the intent and ability to legally remain a New York resident, prior to the issuance of letters.

• PRACTICE TIP •

A person who is ineligible to receive letters is not rendered eligible by a nomination in the will. Therefore, care must be exercised in the original nomination when the will is drafted.

b. Missing fiduciaries. In the event the nominated executor is not the petitioner, he or she must be joined as a party, by whatever method is available. SCPA 1403(1)(b); *see* SCPA 1416(2).

c. Recalcitrant fiduciaries. A fiduciary who will neither qualify nor renounce may be excluded and deemed to have renounced in accordance with the mechanism set forth in SCPA 1416.

• PRACTICE TIP •

An application under SCPA 1416 should not be confused with an application to declare a fiduciary ineligible to serve under SCPA 707; the latter determination by the court constitutes a statutory bar to serving as a fiduciary, while the former is simply a deemed renunciation which, if the nominated executor wishes, may be retracted under SCPA 1417.

• PRACTICE TIP •

If it is anticipated at the outset that the nominated executor will fail to qualify or renounce, the court may entertain an application for SCPA 1416 relief in the original petition, thus obviating the necessity to serve and file separate orders for such relief after the conclusion of the probate proceeding.

d. Co-fiduciaries.

i. Named in will. All executors and other fiduciaries have a right to serve in the order of priority set forth in the will, unless ineligible (SCPA 707) or renouncing, or deemed to have renounced (SCPA 1416). *See* SCPA 1414.

ii. By designation. A person designated as co-fiduciary by a nondomiciliary alien may be appointed in the discretion of the court (SCPA 707(1)(c)); one designated pursuant to a power contained in the will (SCPA 1414(4)) may be appointed subject to the authority granted by, and any contingency specified in the will (SCPA 1414(3)).

e. Qualification problems.

i. Oath and Designation/Domicile. Every fiduciary must execute an acknowledged designation and, unless exempted (e.g., a trust company), an oath. Incident to the fiduciary's qualification is a statement setting forth the fiduciary's domiciliary address. SCPA 708(1),(2); *see* SCPA 708(4).

• PRACTICE TIP •

The address given as the domicile of the fiduciary must be the fiduciary's actual domicile, not an office address or a post office box. In the case of a domiciliary alien, the domicile must be a New York address.

ii. Bond. An executor's bond is normally waived unless required by the will. SCPA 710(1). A trustee's bond (or bond of an executor acting as trustee) is required unless waived in the will. The amount of the bond for each fiduciary capacity is set forth in SCPA 801.

• PRACTICE TIP •

Particular care should be exercised in drafting a will, to insure that bond exoneration clauses are clear, correct, and unequivocal.

f. Limited letters. In appropriate circumstances, the court may limit letters based on particular circumstances, such as difficulty or inability to fix a bond, or for the protection of certain assets not susceptible to bonding.

• PRACTICE TIP •

In recent years, the courts have shown increasing inclination to limit letters testamentary, where a cause of action for wrongful death is or may be brought, to commencement and prosecution, a practice formerly employed only with letters of administration. This necessitates the filing of a "compromise and account," a separate proceeding, at the conclusion of the litigation, for the purpose of having the court approve any settlement and grant additional authority to collect and distribute proceeds.

4. Domicile Issues

a. Effect of domicile. The practical difference between a domiciliary and non-domiciliary estate, aside from the necessity of showing sufficient assets in the jurisdiction to persuade the court to invoke its jurisdiction in a non-domiciliary estate, is the need to join the state tax commission in the case of a non-domiciliary decedent. SCPA 1403(1)(g).

b. Establishing domicile. Because domicile is based on intent, and it is not possible to inquire directly as to the intent of the decedent, his or her intent must be gleaned from secondary evidence, such as voting records, motor vehicle registration, duration of physical presence, and nature and extent of financial and community ties. SCPA 103(15); *In re Newcomb*, 192 N.Y. 238, 84 N.E. 950 (1908); *In re Urdang*, 194 A.D.2d 615, 599 N.Y.S.2d 60 (2d Dep't 1993).

5. Miscellaneous "Gotchas"

a. Lost will. A will may be admitted to probate even if the original instrument has been lost or destroyed, if the petitioner establishes that the will was not revoked and was duly executed, and that all provisions are "clearly and distinctly proved" by each of at least two witnesses or by a copy or draft proved to be true and complete. SCPA 1407. Note that an instrument last in the possession of the testator which cannot be found is presumed to have been destroyed by the testator with the intent of revoking it. *In re Danziger*, 57 Misc. 2d 1014, 293 N.Y.S.2d 979 (Sur. Ct., Nassau Co. 1968); *In re Gray*, 143 A.D.2d 751, 533 N.Y.S.2d 459 (2d Dep't 1988). This presumption may be overcome by a showing of contrary circumstances. *In re Mittelstaedt*, 278 A.D. 231, 104 N.Y.S.2d 378 (1st Dep't 1951), *appeal dismissed*, 304 N.Y. 795, 109 N.E.2d 86 (1952). No such presumption attaches where the instrument was not in the testator's possession. *In re Bly*, 281 A.D. 769, 118 N.Y.S.2d 340 (2d Dep't 1953).

b. Joint wills. The execution of a joint will may, in some circumstances, give rise to the presumption, after the first joint testator dies, that the instrument constitutes a contract to execute a will, essentially making it irrevocable by the surviving testator. EPTL 13-2.1(b).

• PRACTICE TIP •

The execution of joint wills should be considered carefully, to avoid any unintended results.

c. Aliases. When a decedent is known by different names, an asset may be uncollectible if it is held in a name used by the decedent which is not reflected in the fiduciary's letters.

• PRACTICE TIP •

When filing a probate proceeding, be sure to include all aliases used by the decedent as a/k/a's on all filed papers.

d. Distribution scheme.

i. Per capita. "A disposition or distribution of

property is per capita when it is made to persons, each of whom is to take in his own right an equal portion of such property." EPTL 1-2.11.

ii. Per stirpes. "A per stirpes disposition or distribution of property is made to persons who take as issue of a deceased ancestor in the following manner:

> "The property so passing is divided into as many equal shares as there are (i) surviving issue in the generation nearest to the deceased ancestor which contains one or more surviving issue and (ii) deceased issue in the same generation who left surviving issue, if any. Each surviving member in such nearest generation is allocated one share. The share of a deceased issue in such nearest generation who left surviving issue shall be distributed in the same manner as to such issue." EPTL 1-2.14.

iii. By representation. "By representation means a disposition or distribution of property made in the following manner to persons who take as issue of a deceased ancestor:

> "The property so passing is divided into as many equal shares as there are (i) surviving issue in the generation nearest to the deceased ancestor which contains one or more surviving issue and (ii) deceased issue in the same generation who left surviving issue, if any. Each surviving member in such nearest generation is allocated one share. The remaining shares, if any, are combined and then divided in the same manner among the surviving issue of the deceased issue as if the surviving issue who are allocated a share had predeceased the decedent, without issue." EPTL 1-2.16.

• PRACTICE TIP •

See Appendix A for a visual representation of these mind-boggling statutory definitions. A picture is worth a thousand words.

e. Anti-lapse. Unless the will provides otherwise, when a testamentary disposition is made to issue or to brothers and sisters, either individually or as a class, who have predeceased the testator, the predeceased beneficiaries' shares do not lapse, but vest in their respective surviving issue, per stirpes if the will was executed prior to September 1, 1992, and by representation if the will was executed on or after September 1, 1992. EPTL 3-3.3.

• PRACTICE TIP •

Any will provision which overrides the anti-lapse statute should be very clear as to exactly who takes the property in the event of a gift-over.

f. Disposition of non-probate property. Any attempt to dispose of non-probate property (property passing by operation of law, such as joint property or insurance policies with named beneficiaries) by will is an exercise in futility. A limited exception exists in the case of "Totten trusts" (bank accounts in trust form), provided the will contains ". . . an express direction concerning such trust account, which must be described in the will as being in trust for a named beneficiary in a named financial institution." EPTL 7-5.2(2). *See also* EPTL 7-5.2(4),(5).

g. Powers of appointment. Where a will purports to exercise a power of appointment (EPTL 10-3.1(a)), the default takers under the instrument creating the power must be joined as necessary parties. SCPA 1403(1)(e).

• PRACTICE TIP •

Many courts will require production of the instrument creating the power, in order to determine whether the appropriate jurisdictional parties have been listed in the petition.

h. *In terrorem* clauses. In New York, a will provision designed to prevent a disposition from taking effect in case the will is contested by the beneficiary (an "*in terrorem* clause") is effective, subject to certain statutory limitations set forth in EPTL 3-3.5.

• PRACTICE TIP •

As a practical matter, in terrorem *clauses are of limited value; in a will which completely disinherits a distributee, an* in terrorem *clause will be useless to prevent a will contest by that distributee—he or she stands to lose nothing by the contest. The* in terrorem *clause would only be effective in that case if the testator had left a bequest to that distributee of greater than mere nominal value, something most testators probably would be unwilling to do.*

i. Attorney-fiduciary considerations.

i. SCPA 2307-a. "When an attorney prepares a will to be proved in the courts of this state and such attorney or a then affiliated attorney is therein an executor-designee, the testator shall be informed prior to the execution of the will that:

"(a) subject to limited statutory exceptions, any person, including an attorney, is eligible to serve as an executor;

"(b) absent an agreement to the contrary, any person, including an attorney, who serves as an executor is entitled to receive an executor's statutory commissions; and

"(c) if such attorney or an affiliated attorney renders legal services in connection with the executor's official duties, such attorney or a then affiliated attorney is entitled to receive just and reasonable compensation for such legal services, in addition to the executor's statutory commissions." SCPA 2307-a(1).

The statute requires acknowledgment of these disclosure provisions in a written statement executed before at least one independent witness. SCPA 2307-a(2). The penalty for failure to obtain such written acknowledgment is reduction of the attorney-executor's commissions to one-half the statutory rate. SCPA 2307-a(5).

• PRACTICE TIP •

It is important to note that this statute applies to the estates of all decedents dying after December 31, 1996, irrespective of the date of the will. Thus, it has significant retroactive effect, and an attorney who has drafted any wills in the past which may be subject to these provisions would be well advised to obtain appropriate disclosure statements at this time.

ii. Court Rules 16(e); 52 (22 N.Y.C.R.R. § 207.16(e); § 207.52). In conjunction with SCPA 2307-a, a nominated attorney-fiduciary is required to file a statement disclosing that the fiduciary is an attorney, whether the fiduciary or his or her law firm will act as counsel, and whether or not the attorney was the draftsperson of the propounded will. 22 N.Y.C.R.R. § 207.16(e). Additionally, an attorney-fiduciary acting as counsel is required to file an affidavit within 12 months from the issuance of letters (24 months if the estate files a federal estate tax return) disclosing the total commissions paid or to be paid to the attorney, and the total attorneys' fees paid or to be paid to the attorney. 22 N.Y.C.R.R. § 207.52.

j. *Putnam/Weinstock/Satterlee* issues. If a person having a confidential relationship with the testator or a member of that person's family receives a legacy under the will, there may be an inference of undue influence by such legatee. Such confidential relationship may be with the testator's attorney (*In re Putnam*, 257 N.Y. 140, 177 N.E. 399 (1931), or with any other person (*In re Satterlee*, 281 A.D. 251, 119 N.Y.S.2d 309 (1st Dep't 1953) (substantial bequests to testator's lawyer and physician); *In re Collins*, 124 A.D.2d 48, 510 N.Y.S.2d 940 (4th Dep't 1987) (financial advisor-draftsman). In all such cases, the legatee, even in an uncontested proceeding, will be called upon to explain the circumstances of such bequest. Such explanation may take the form of an affidavit, an *ex parte* hearing, or even an investigation by the public administrator, depending upon the situation and the local court practice.

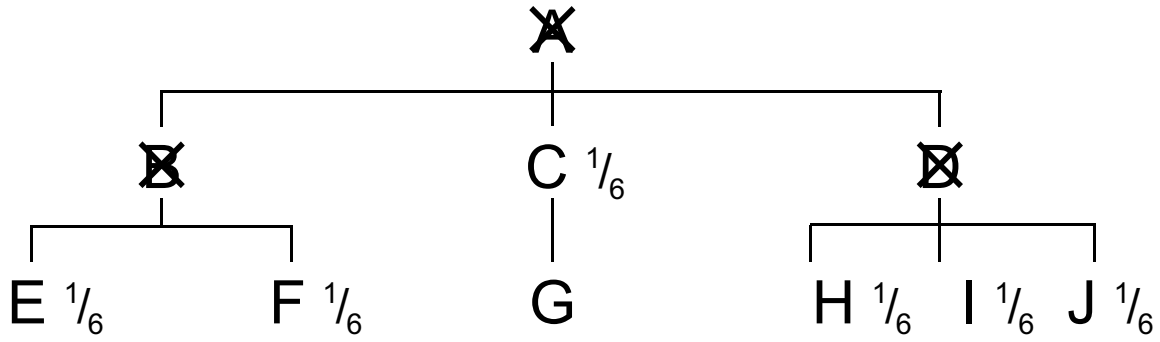
• PRACTICE TIP •

To prevent delay in the probate proceeding, it is best in these situations to have the will drafted by an independent, disinterested lawyer.

Gary R. Mund is the Probate Clerk of Kings County Surrogate's Court, Brooklyn, New York, and a member of this Section's Expanded Executive Committee.

APPENDIX A

PER CAPITA



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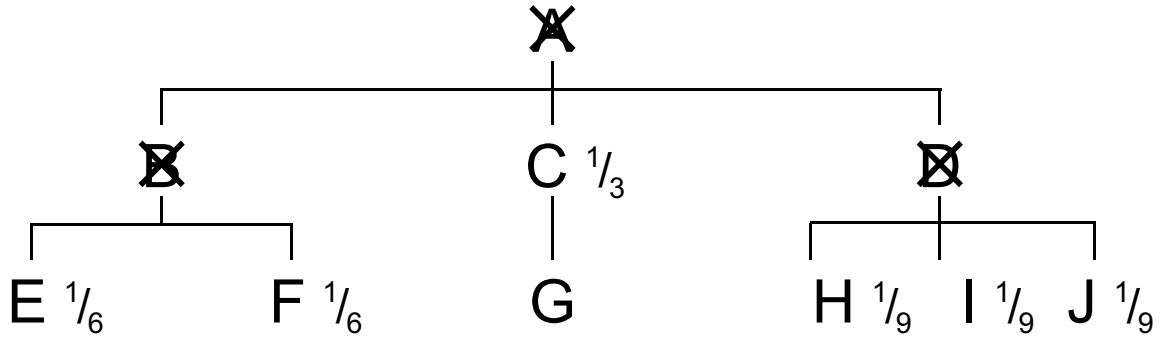

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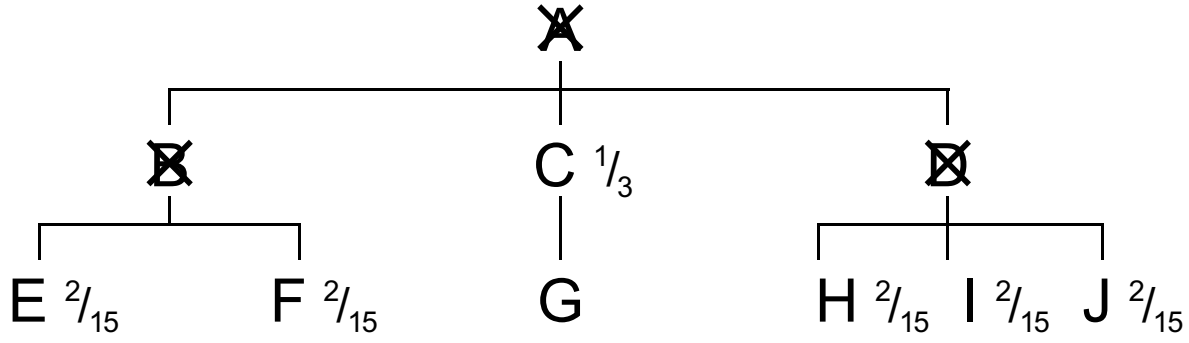

2002 New York State Legislative Session Changes Affecting Estate Planning and Administration

By Joshua S. Rubenstein

The 2002 legislative session brought numerous substantive and procedural changes to the laws affecting estate planning and administration. Many of the changes were designed primarily to provide relief to victims of the terrorist attacks of September 11, 2001. The other changes were largely procedural, affecting adoptions, guardianships, charitable trusts, contested accounting proceedings and the attorney-client privilege. The following is a review of each such change.

Surrogate's Court Procedure Act

Jurisdiction and Powers

1. Surrogate's Court Procedure Act 205 has been amended by adding a new subdivision 3, which provides that the Surrogate's Court of any county has jurisdiction over, and is a proper venue for, the proceedings of any decedent who died as a result of wounds or injuries incurred as a result of the terrorist attacks on September 11, 2001, and was a domiciliary of the state at the time of his or her death. This change is effective immediately.[1]

Letters

2. A new subdivision 12 has been added to Surrogate's Court Procedure Act 711 to provide that a fiduciary's letters may be suspended, modified or revoked if he or she fails to account in the time and manner directed by the court. This change is effective November 1, 2002.[2]

3. Subdivision (1) of Surrogate's Court Procedure Act 719 has been amended to provide that the letters of a fiduciary, or the powers of a lifetime trustee, may be modified, suspended or revoked if he or she fails to account in the time and manner directed by the court. This change is effective November 1, 2002.[3]

Guardians and Custodians

4. Paragraph 4(a) of Surrogate's Court Procedure Act 1725 has been amended to change the word "natural parent," wherever it is found in that paragraph, to "birth parent." Paragraph 4(a) now provides that, in a temporary guardianship proceeding brought by an adoptive parent prior to an adoption, a consenting "birth" parent must be informed of the occurrence of any the following events, if such event occurs within 45 days of the execution of the consent: (1) a court denial of an application for temporary guardianship, or removal of a child from the physical custody of the petitioners; (2) the expiration of temporary guardianship without the entry of a final order of adoption; or (3) the withdrawal or denial of a petition for adoption. This change is effective immediately.[4]

5. Section 1750 of the Surrogate's Court Procedure Act has been amended to provide that every professional who certifies a person's mental retardation must also certify the person's capacity to make health care decisions. This change is effective March 16, 2003.[5]

6. A new section 1750-b has been added to the Surrogate's Court Procedure Act to provide that unless specifically prohibited by the court, every guardian of a mentally retarded person shall have the authority to make any and all health care decisions on behalf of a mentally retarded person who is incapable of doing so for himself or herself. The decision-making standard shall be the best interests of the mentally retarded person and, if reasonably knowable, the person's wishes. The guardian shall have the right to receive all relevant patient information and may decide to withdraw or withhold life-sustaining treatment, subject to the right of certain individuals to object. A guardian may commence a special proceeding to resolve any dispute under this section. Immunity is granted to any health care provider or guardian who acts in good faith. This change is effective March 16, 2003.[6]

Miscellaneous Proceedings

7. Both houses passed, but the Governor vetoed, a bill that would have added a new subdivision 5 to Surrogate's Court Procedure Act 2110 providing that in any proceeding in which the court determines the compensation of an attorney, the court shall allow the attorney reimbursement for certain expenses that are necessarily and appropriately incurred,

including, but not limited to: (1) photocopying and binding; (2) computerized legal research; (3) same day or express courier or messenger service; (4) postage, including certified, registered, or express mail; (5) telecopy; (6) long-distance telephone; and (7) service of process and other papers. To be reimbursable, the expenses: (1) must have been paid to outside providers, or have been actual direct costs (excluding overhead) incurred by the attorney or his or her firm; (2) must have been traced and allocated separately to the client; and (3) must not have been considered in determining the attorney's billing rates. This change would have been effective immediately and applied to all pending or future proceedings involving the determination of attorney compensation, irrespective of when the services were performed or when the expenses were incurred.[7]

Accounting

8. Surrogate's Court Procedure Act 2205 has been amended to authorize the court to make an order (a) requiring a fiduciary to account in such time and manner as the court may direct, (b) suspending letters of a noncompliant fiduciary, (c) appointing a successor to a fiduciary whose letters have been suspended, (d) fixing a trial date for a removal hearing, (e) fixing a trial date to take and state an account of a noncompliant fiduciary and (f) granting such other and further relief as the court may direct. This change is effective November 1, 2002.[8]

9. Subdivision (1) of Surrogate's Court Procedure Act 2206 has been amended to permit a petition for a compulsory accounting to request (a) the suspension and/or removal of a fiduciary who fails to account in the time and manner directed by the court, (b) the appointment of a successor to the fiduciary whose letters are suspended and/or revoked and (c) the taking and stating of an account of a noncompliant fiduciary. This change is effective November 1, 2002.[9]

10. Subdivision (2) of Surrogate's Court Procedure Act 2206 has been amended to permit the order compelling account to (a) suspend the letters of a fiduciary who fails to account in the time and manner directed by the court, (b) appoint a successor to the fiduciary whose letters are suspended, (c) schedule a hearing for the modification and/or suspension of the letters of the noncompliant fiduciary and (e) schedule a hearing to take and state an account of a noncompliant fiduciary. This change is effective November 1, 2002.[10]

Costs, Allowances and Commissions

11. Subdivision 2 of Surrogate's Court Procedure Act 2307 has been amended to provide that the recovery of awards from the September 11thVictim Compensation Fund of 2001 will not be considered as money in computing commissions, and that such awards shall be valued at zero for purposes of that section. This change is effective immediately.[11]

Estates, Powers and Trusts Law

Charitable Trusts

12. Paragraph (a) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that, for purposes of that section, "trustee" means any individual, group of individuals, executor, trustee, corporation or other legal entity holding and administering property for charitable purposes, whether pursuant to any will, trust, other instrument or agreement, court appointment, or otherwise pursuant to law, over which the attorney general has enforcement or supervisory powers. Previously, executors, trustees, and legal entities holding and administering property for charitable purposes pursuant to a trust were not included in the meaning of the term. This change is effective on August 1, 2002.[12]

13. Subparagraph (b)(2) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that the registration and reporting requirements of that section do not apply to any trustee which is required by any other provision of law to render a full, complete, and itemized annual financial report to the United States Congress or to the New York State legislature, provided that such report contains the information required of trustees pursuant to article 8 of the Estates, Powers and Trusts Law. Previously, that subparagraph did not specify that the itemized annual report be a financial report, and did not require that the report contain the information required of trustees pursuant to article 8. This change is effective on August 1, 2002.[13]

14. Subparagraph (b)(9) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that the registration and reporting requirements of that section do not apply to any person who, in his capacity as an officer,

director, or trustee of any corporation or organization mentioned in section 8-1.4(b), holds property for the religious, educational, or charitable purposes of such corporation or organization, so long as such corporation or organization is registered with the attorney general pursuant to section 8-1.4. Previously, that subparagraph did not require that the corporation or organization be registered with the attorney general. This change is effective on August 1, 2002.[14]

15. Paragraph (e) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that in all cases where a person holding property or an income interest that may be required to be devoted to charitable purposes files a petition for instructions regarding the administration, construction, disposition, distribution, or accounting of such property or interest, that person must give the attorney general due notice together with a copy of any petition, accounting, will or trust instrument. Previously, notice was required only in certain circumstances. This change is effective on August 1, 2002.[15]

16. Paragraph (f) of Estates, Powers and Trusts Law 8-1.4 has been amended to: (1) require that every trustee must file, with the attorney general and all identified current charitable beneficiaries, annual financial reports and a notice of the termination of the interest of any party in a trust that would cause all or part of the trust assets or income therefrom to be applied to charitable purposes; and (2) provide that trustees required to report to the attorney general under article 7-A of the Executive Law shall comply with paragraph (f) by filing copies of the financial reports required by section 172-b of the Executive Law, unless such reports have been filed previously. Although, prior to the amendment, that paragraph did require reports, it did not: (1) list the attorney general and charitable beneficiaries as required recipients; (2) specify the required frequency of the reports; (3) require notice of the termination of an interest; or (4) provide that the reports required by section 172-b need not be filed with the attorney general where they have been filed previously. This change is effective on August 1, 2002.[16]

17. Paragraph (g) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that, in all cases, the first report of any trustee shall be filed no later than six months after the end of the fiscal year of the trustee during which he or she becomes subject to section 8-1.4. Previously, if a trustee was authorized by the attorney general, he or she was permitted to file his or her first report after the six-month period lapsed. This change is effective on August 1, 2002.[17]

18. Paragraph (h) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that the attorney general may classify trusts, estates, corporations, and other trustees as to purpose, nature of assets, duration, amount of assets, amounts to be devoted to charitable purposes, or otherwise, and may establish different rules for different classes as to time and nature of the reports required, to the ends that he or she shall receive current financial reports as to all such trusts, estates, corporations, or other trustees which will enable him or her to ascertain whether they are being properly administered. Previously, this section: (1) covered trusts and corporations, but not estates or trustees; and (2) stated that an additional end of the statute was to provide that periodic reports did not unreasonably add to the expense of administration. Paragraph (h) was also amended to provide that a trustee's written application to suspend the filing of financial reports for a reasonable, specifically designated time be signed by the trustee under penalties for perjury. These changes are effective on August 1, 2002.[18]

19. Paragraph (o) of Estates, Powers and Trusts Law 8-1.4 has been amended by replacing the words "corporation, trust or similar relationship" with the word "trustee." That paragraph now requires that officer agencies, boards, or commissions of New York or political subdivisions thereof receiving applications for exemption from taxation of any trustee subject to section 8-1.4: (1) annually file with the attorney general a list of all applications received during the year; and (2) notify the attorney general of any suspension or revocation of a tax-exempt status previously granted. This change is effective on August 1, 2002.[19]

20. Paragraph (p) of Estates, Powers and Trusts Law 8-1.4 has been amended by replacing the words "department of law" with "attorney general." That paragraph now provides the means by which the attorney general shall collect a fee for a trustee's filing of periodic reports required by section 8-1.4. This change is effective on August 1, 2002.[20]

21. The sentence in paragraph (q) of Estates, Powers and Trusts Law 8-1.4 that defines "gross receipts" for purposes of that paragraph has been amended by replacing the word "annual" with "financial." That paragraph now provides that "gross receipts" means the total received during the financial reporting period of gifts, grants, contributions, gross income, etc. This change is effective on August 1, 2002.[21]

22. Paragraph (s) of Estates, Powers and Trusts Law 8-1.4 has been amended to provide that a trustee is not qualified to make application for funds or grants or to receive such funds from any department or agency of the state without certifying compliance with paragraphs (d), (f), and (g) of section 8-1.4 and all applicable registration and reporting requirements of article 7-A of the Executive Law. Previously, that paragraph did not require certification of compliance with article 7-A. This change is effective on August 1, 2002.[22]

23. Paragraphs (b), (c), (d), (g), (h), (i), (k), (m), and (r) of Estates, Powers and Trusts Law 8-1.4 have been amended to make those paragraphs gender neutral. Those paragraphs substitute "he or she" for "he," "him or her" for "him," and "his or her" for "his." These changes are effective on August 1, 2002.[23]

Actions By or Against Personal Representatives

24. A new paragraph (e) has been added to Estates, Powers and Trusts Law 11-4.7. This paragraph provides special rules for personal representatives of victims of the terrorist attacks on September 11, 2001.

    - Any such personal representative who files a claim with the September 11th Victim Compensation Fund of 2001 ("the Fund") shall have no liability to any person resulting from any actions taken reasonably and in good faith under the Federal Air Transportation and Air Stabilization Act (Public Law No. 107-42), including but not limited to: (1) the submission or prosecution of a claim to the Fund; (2) a decision not to submit such a claim, or to withdraw a claim previously submitted; (3) the waiver of the right to file a civil action for damages sustained as a result of the terrorist attacks; (4) the failure to identify or locate any person designated for receipt of notice, provided that the personal representative made a reasonable and good-faith effort to identify and locate such person; and (5) the payment or distribution of any award received from the Fund. This change is effective immediately.[24]

    - Any such personal representative is authorized to file and prosecute a claim with the Fund, and the filing of such a claim, and the resulting compromise of any cause of action pursuant to the Act, shall not violate any restriction on the powers granted to the personal representative relating to the prosecution or compromise of any action, the collection of any settlement, or the enforcement of any judgment. This change also is effective immediately.[25]

Tax Law

Procedure and Administration

25. Section 696 of the Tax Law has been renamed "Income taxes of members of armed forces and victims of certain terrorist attacks," and a new subsection (h) has been added, providing that any "specified terrorist victim" (a decedent who dies as a result of wounds or injuries incurred from the terrorist attacks on September 11, 2001, other than an individual identified by the attorney general to have been a participant or conspirator in any such attack or a representative of such individual) dying on or after September 11, 2001, but before January 1, 2002, is generally exempt from the New York State, New York City, and Yonkers personal income taxes for both the 2000 and 2001 taxable years. Surviving spouses, personal representatives, or executors of specified terrorist victims may file amended personal income tax returns for 2000 and 2001 to claim a refund of tax paid. This change is effective immediately.[26]

Estate Tax

26. Section 696 of the Tax Law (which is made applicable to the estate tax via section 990 of the Tax Law) has been amended to provide estate tax relief for the estates of specified terrorist victims. For estates of victims dying in 2001, relief is provided by conforming to the provisions of the federal Victims of Terrorism Tax Relief Act of 2001. The federal Act provides a reduced estate tax rate schedule for victims under Internal Revenue Code § 2201(c). Using this schedule, a taxable estate of $2,936,818 or less is exempt from federal

and New York State estate tax because the federal unified credit of $220,550 offsets the tax. Estates of victims dying in 2002 or after are exempt from New York estate tax; however, these estates are still required to file a New York State estate tax return if a federal estate tax return is required (generally when the gross estate exceeds $1 million). These changes are effective immediately.[27]

27. Section 951 of the Tax Law has been amended to provide that, for purposes of the New York State estate tax, any reference to the internal revenue code means the United States Internal Revenue Code of 1986, not only with all amendments enacted on or before July 22, 1998, but also with all amendments enacted by the federal Victims of Terrorism Tax Relief Act of 2001 (Public Law No. 107-134) insofar as the Act relates to the estate of a specified terrorist victim. This change is effective immediately.[28]

28. The unified credit for New York State estate tax purposes has been increased to $345,800, an amount equal to the estate tax due on a taxable estate of $1 million. The increase appears to be the result of federal, rather than state, legislation. Section 951(a) of the Tax Law specifies that the amount of the unified credit allowed against the New York State estate tax is the amount allowed under the applicable federal law in effect on the decedent's date of death. On June 7, 2001, President George W. Bush signed into law the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law No. 107-16), which increased the federal unified credit to $345,800 for estates of those dying in 2002 and 2003. Therefore, because the New York State unified credit is tied to the federal unified credit (with a ceiling of $1 million), the unified credit for New York State estate tax purposes for estates of those dying in 2002 and 2003 is $345,800. This change is effective immediately.[29]

September 11th Victim Compensation Fund

29. Effectively immediately, no state or local tax of any kind, including but not limited to income and estate taxation, may be imposed on any payment from the September 11th Victim Compensation Fund of 2001.[30]

Civil Practice Law and Rules

Evidence

30. Subdivision (a) of Civil Practice Law and Rules 4503 has been amended to provide that, for purposes of the attorney-client privilege, if the client is a personal representative,[31] and the attorney represents the personal representative in that capacity, then in the absence of an agreement between the attorney and the personal representative to the contrary: (1) no beneficiary of the estate is, or shall be treated as, the client of the attorney solely by reason of his or her status as beneficiary; and (2) the existence of a fiduciary relationship between the personal representative and a beneficiary of the estate does not by itself constitute or give rise to any waiver of the privilege for confidential communications made in the course of professional employment between the attorney or his or her employee and the personal representative who is the client. This change is effective immediately.[32]

Domestic Relations Law

Effect of Adoption

31. Subdivisions 1 and 2 of Domestic Relations Law § 117, have been amended to change the phrase "natural parent," wherever it is found in those sections, to "birth parent." Subdivisions 1 and 2 set forth the inheritance and succession rights of adopted children, and that of their adopted parents and birth parents. This change is effective immediately.[33]

Public Health Law

32. A new section 4368 has been added to the Public Health Law, establishing a program for the annual public recognition of organ, tissue and bone marrow donors. This change is effective immediately.[34]

Workers' Compensation Law

33. A new section 4 has been added to the Workers' Compensation Law, extending death benefits to domestic partners of persons who perished as a result of the terrorist attacks on September 11, 2002. This change is effective immediately and is deemed to have been in effect after September 10, 2002.[35]

Social Service Law

34. Social Service Law section 209(b) has been amended to clarify that the recipients of medical assistance who may establish irrevocable trust funds for their funeral and burial may reside in any state. This change is effective immediately.[36]

Endnotes

1. 2002 N.Y. Laws ch. 73, S7356, A11290, signed May 21, 2002. For a complete listing of all state tax relief available to terrorist victims, and the applicable procedural rules, see Publication 59.
2. 2002 N.Y. Laws ch. 457, S6934, A10756, signed Aug. 20, 2002.
3. 2002 N.Y. Laws ch. 457, S6934, A10756, signed Aug. 20, 2002.
4. 2002 N.Y. Laws ch. 312, S7203, A4739, signed Aug. 6, 2002.
5. 2002 N.Y. Laws ch. 500, S4622B, A8466D, signed Sept. 17, 2002.
6. 2002 N.Y. Laws ch. 500, S4622B, A8466D, signed Sept. 17, 2002.
7. S2938, A10737, vetoed Aug. 6, 2002.
8. 2002 N.Y. Laws ch. 457, S6934, A10756, signed Aug. 20, 2002.
9. 2002 N.Y. Laws ch. 457, S6934, A10756, signed Aug. 20, 2002.
10. 2002 N.Y. Laws ch. 457, S6934, A10756, signed Aug. 20, 2002.
11. 2002 N.Y. Laws ch. 73, S7356, A11290, signed May 21, 2002.
12. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
13. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
14. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
15. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
16. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
17. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
18. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
19. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
20. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
21. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
22. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
23. 2002 N.Y. Laws ch. 43, S5611, A871, signed Apr. 30, 2002.
24. 2002 N.Y. Laws ch. 73, S7356, A11290, signed May 21, 2002.
25. 2002 N.Y. Laws ch. 73, S7356, A11290, signed May 21, 2002.
26. 2002 N.Y. Laws ch. 85, S6260, A9762, signed May 29, 2002; TSB-M-02(3)M (July 9, 2002). In order to claim such relief, a form IT-59 must be filed.
27. 2002 N.Y. Laws ch. 85, S6260, A9762, signed May 29, 2002; TSB-M-02(3)M (July 9, 2002).
28. 2002 N.Y. Laws ch. 85, S6260, A9762, signed May 29, 2002.
29. TSB-M-02(2)M (March 21, 2002).
30. 2002 N.Y. Laws ch. 73, S7356, A11290, signed May 21, 2002.
31. For purposes of section 4503(a), "personal representative" means (1) the administrator, administrator c.t.a., ancillary administrator, executor, preliminary executor, temporary administrator, or trustee to whom letters have been issued within the meaning of subdivision 34 of Surrogate's Court Procedure Act 103, and (2) the guardian of an incapacitated communicant if and to the extent that the order appointing such guardian under Mental Hygiene Law § 81.16(c) or any subsequent order of any court expressly provides that the guardian is to be the personal representative of the incapacitated communicant for purposes of section 4503(a).
32. 2002 N.Y. Laws ch. 430, S2784, A5658, signed Aug. 20, 2002.
33. 2002 N.Y. Laws ch. 312, S7203, A4739, signed Aug. 6, 2002.
34. 2002 N.Y. Laws ch. 497, S2820-A, A10753, signed Sept. 17, 2002.
35. 2002 N.Y. Laws ch. 467, S7685, A11307, signed Aug. 20, 2002.
36. 2002 N.Y. Laws ch. 317, S7412-A, A11391-A, signed Aug. 6, 2002.

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Estate and Gift Information Added to IRS Web Site

The IRS Web site now offers a section on estate and gift tax. Besides a primer on basic taxation, it includes a "Frequently Asked Questions" area and downloadable forms for estate and gift tax. This page can be located by typing "estate and gift tax" in the search window at www.irs.gov/.

The customer support number in Cincinnati is (866) 699-4083. This number can be used to find out the status of filings. If the preparer signed the Form 706 as the representative (Page 2, Part 4), he or she may call for information without the need of Form 2848.

On December 2nd, the IRS opened a new Business and Specialty Tax Line. It is (800) 829-4933. It is available for persons applying for a new Employer Identification Number or who need help with employment taxes; partnership, corporation, estate, gift, trust and excise returns, federal tax deposits; and other small business issues. This line will eliminate some of the traffic on the traditional individual line (800) 829-1040 and will provide more specialized service to customers.

Pending Bills in the State Legislature

By Ronald J. Weiss

As of mid-October 2002, there were over 90 bills pending in the New York State Senate and Assembly that affect the trusts and estates practice. A resource for keeping track of pending bills is the Assembly's Web site (assembly.state.ny.us/leg), which is searchable both by bill number and keyword. The following is a summary of these bills.

Bill Number	Description
A13 (similar to S227)	Prohibits a service charge or minimum balance requirement for attorney trust or IOLA accounts.
A126 (same as S1913)	Prohibits persons found guilty of homicide by reason of mental disease or defect from receiving a decedent's property by will or intestate succession.
A212 (same as S438)	Includes the value of all property received, real or personal, other than specifically bequeathed/devised property, in computing the commissions of fiduciaries other than trustees. (Passed the Senate 2/26/01; died in Assembly 1/9/02; returned to and passed the Senate 3/12/02)
A307	Provides a $1,000 credit against the New York estate tax for organ donors.
A377 (same as S2858)	Broadens the information to be supplied from the statewide register of child abuse and maltreatment when applying for letters of guardianship. (Passed by the Assembly 4/15/02)
A765	Relates to the legal rights of a child conceived after the death of his or her parent through artificial means.
A871 (same as S5611-D)	Makes extensive changes to EPTL 8-1.4 with respect to the registration and reporting requirements for fiduciaries and others holding property for charitable purposes. Signed 4/30/02, ch. 43.
A1165 (same as S192)	Authorizes guardians of incompetent persons and fiduciaries appointed by a Surrogate's Court to be included as qualified persons under Public Health Law § 18 eligible to request access to medical records. (Passed by the Assembly 2/11/02)
A1330 (same as S3366)	Makes provision for orders for the purpose of performing paternity testing on a decedent.
A1437 (same as S1083)	Enacts fiduciary privilege bill relating to the effect of death or disability on certain privileges and requires disclosure to courts of certain communications. Vetoed 11/13/01.
A2261 (same as 5219)	Creates a rebuttable presumption in civil actions and in civil actions for larceny that a disabled principal does not consent to certain transfers pursuant to a power of attorney.
A2419	Enacts the "qualified dispositions in trust act" (would permit the creation of perpetual and creditor protection trusts).

Bill Number	Description
A2911 (same as S2348)	Provides that certain supplemental needs trusts may be established without the payment of any medical assistance lien attached to the amount to be held in trust. (Passed by the Assembly 3/25/02)
A2956	Establishes certain trusts as void as against public policy where beneficiary's interest ceases if beneficiary needs medical, hospital or nursing care.
A2995	Authorizes provision of support for a decedent's child under age 21 where decedent's will makes no reasonable provision for a child's maintenance and child's other parent is deceased.
A3135	Authorizes disclosure of death of biological parents and of adoptive children by adoption registry.
A3222	Provides that certain procedural requirements be met in order for a spouse to waive or release his or her right to a distributive share of the other spouse's estate.
A3318	Authorizes a court to compensate guardians from amounts appropriated to the Department of Mental Hygiene if court finds that insufficient funds exist.
A4037	Provides for the revocatory effect of divorce on dispositions by will, death benefit or under lifetime trusts.
A4221 (same as S2320)	Relates to the rights of domestic partners, spouses, parents, siblings and close friends to control the disposition of a decedent's remains.
A4242 (same as S2310)	Permits the certification of a photographic reproduction of a will by an attorney for purposes of proving a will by affidavit of attesting witness out of court.
A4317	Relates to the registration of charitable organizations with the Attorney General's office, requires a clear description of an organization's purpose and use of funds.
A4440	Requires prior disclosure of income, assets and financial obligations of decedent to enforce a surviving spouse's waiver of his or her right of election; waives the dead man statute in such circumstances. (Passed by the Assembly 4/22/02)
A4447 (same as S4782)	Relates to the commissions of corporate fiduciaries of charitable trusts. (Passed by the Assembly 3/13/02)
A4554 (same as S261)	Amends NPCL § 720-a to limit the civil liability of directors and officers of not-for-profit corporations.
A4608	Allows court to determine reasonable compensation for an attorney selected by an allegedly incapacitated person. (Passed by the Assembly 6/4/01; died in the Senate 1/9/02; returned to and passed by the Assembly 3/18/02)
A4743	Provides that for settlements that require a court order, the order shall provide for the payment of interest on the settlement amount at the statutory interest rate on judgments. (Passed by the Assembly 4/23/01; died in the Senate 1/9/02; returned to and passed by the Assembly 3/13/02)

Bill Number	Description
A5523	Enacts the "Family Health Care Decision Act," establishing procedures for making health care decisions on behalf of patients unable to decide about treatment for themselves.
A5658 (same as S2784)	Makes provision preserving attorney-client privilege when the client is a "personal representative" vis-a-vis the beneficiaries of an estate. Signed 8/20/02, ch. 430.
A6768 (same as A9840 and S1853)	Permits wrongful death action on behalf of child in utero.
A7016	Excludes an individual's elective share of a deceased spouse's estate as an available resource for purposes of Medicaid eligibility.
A7317 (see also S794)	Makes changes with respect to the rule against perpetuities and powers of appointment in relation thereto.
A7670 (same as S1620)	Provides a right of action for persons killed or injured by illegally obtained handguns against the person providing or procuring such handgun.
A7789 (same as S793)	Expands the types of damages that may be awarded to the persons for whose benefit an action for wrongful death is brought to include emotional loss.
A7791 (same as S5461)	Makes provision with respect to the right to a jury trial in a contest of a revocable living trust and in the incorporation by reference in a will of a lifetime trust. (Passed by the Assembly 6/4/01; died in the Senate 1/9/02)
A7792 (same as S795)	Relates to the commissions of a trustee who qualifies on or after 6/5/78 under the will of a decedent dying on or before 8/31/56. Signed 10/23/01, ch. 376.
A7794	Relates to the appointment of guardians for the person/property of certain persons.
A7944 (same as A10245 and S1389; see also A3360)	Enacts the transfer-on-death security registration act. (Passed by the Assembly 6/20/01; died in the Senate 1/9/02; returned to and passed by the Assembly 3/20/02)
A8357 (same as S2936)	Amends SCPA 1411 (3) to limit service of citation in a contested probate proceeding on only those persons named or referred to in a will who have appeared or whose interests would be adversely affected by the outcome of the proceeding. Signed 10/31/01, ch. 393.
A8466 (substituted by S4622)	Enacts "Health Care Decisions Act for Persons with Mental Retardation," authorizing guardian to make health care decisions for such persons lacking capacity. Signed 9/17/02, ch. 500.
A8661 (same as S4781)	Amends the Tax Law to phase out the distinction between resident and non-resident trusts.
A8690 (same as S5218)	Regulates possible conflict-of-interest situations between officers or directors and the not-for-profit corporations they represent.
A8774 (same as S4395)	Provides that an adoptive child will not lose either inheritance rights or the right to receive lifetime dispositions from his or her natural parents. (Passed by the Assembly 6/19/02)

Bill Number	Description
A8794 (same as S5513)	Allows renunciation of property on behalf of a person under a disability to be made by a guardian or by an attorney-in-fact pursuant to a duly executed power of attorney. (Passed by the Assembly 6/11/01; died in the Senate 1/9/02; returned to and passed by the Assembly 3/18/02)
A9167 (see also A7791)	Establishes a party's statutory right to trial by jury on a controverted question of fact in any proceeding for the determination of the validity of a lifetime trust.
A9762 (same as S6260-B)	Amends and renames section 696 of the Tax Law to provide that a "specified terrorist victim" dying on or after September 11, 2001, and before January 1, 2002, is generally exempt from New York State, city of New York and Yonkers personal income taxes for 2000 and 2001; provides estate tax relief to specified terrorist victims by conforming New York law to the provisions of the federal Victims of Terrorism Tax Relief Act of 2001. Signed 5/29/02, ch. 85. (*See also* TSB-M-02(3)M (July 9, 2002).)
A9987 (same as S6350)	Requires charitable organizations to file a statement with the Attorney General and to disclose on any solicitation the percentage of their funds used for administrative purposes.
A10660 (same as S2937)	Amends EPTL 10-10.1 to authorize the grantor of a trust to confer upon trustees the power to make discretionary distributions to themselves as beneficiaries and to make discretionary allocations. (Passed by the Assembly 4/22/02)
A10661 (same as S6506)	Provides that a nominated co-fiduciary has standing to file objections to the grant of letters to a co-fiduciary or to the appointment of a lifetime trustee. (Passed by the Assembly 4/22/02)
A10737 (same as S2938)	Amends SPCA 2110 to permit certain expenses of attorneys in addition to compensation for legal services. Vetoed 8/6/02.
A10753 (same as S2820-A)	Amends the Public Health Law to establish a program to publicly recognize organ, tissue and bone marrow donors and their families. Signed 9/17/02, ch. 497.
A10756 (same as S6934)	Amends SCPA sections 711, 2205 and 2206 to provide for multiple relief in connection with a petition for compulsory account where the fiduciary defaults by failing to appear or account within the time ordered. Signed 8/20/02, ch. 457.
A11037 (same as S6912)	Amends EPTL 8-1.8 to harmonize its provisions with those of section 4947(b) of the Internal Revenue Code.
A11290 (same as S7356)	Enacts the September 11 Victims and Families Relief Act; amends SCPA 205 to provide that the Surrogate's Court of any county has jurisdiction over and is proper venue for the proceedings of the estate of any decedent who died in or as a result of terrorist attacks of September 11, 2001, and was a domiciliary of New York State at the time of death; amends SCPA 2307 to provide that recoveries from the Victim Compensation Fund of 2001 (VCF) are not commissionable; provides protections to personal representatives who file or choose not to file a claim with the VCF; provides that awards from the VCF are not subject to state or local taxation, including income and estate taxation. Signed 5/21/02, ch. 73.

Bill Number	Description
A11307 (same as S7685)	Makes domestic partners of persons dying as a result of the terrorist attacks of September 11, 2001, eligible for workers compensation benefits due a surviving spouse. Signed 8/20/02, ch. 467.
A11391-A (same as S7412)	Amends the Social Service Law to clarify which recipients of medical assistance or SSI can establish irrevocable funeral or burial trusts with a New York funeral home. Signed 8/6/02; ch. 317.
S669	Prohibits postmortem retrieval of sperm from a decedent unless the deceased gave written consent for such procedure prior to his death.
S794	Enacts the Perpetual Trust Act of 2001.
S3367	Makes amendments to the statutory short form of durable general power of attorney.
S3431	Relates to recognizing the legitimacy of children born to married couples by means of in vitro fertilization or any other assisted reproduction.
S3698	Relates to the manner of investigation when decedent is a donor of an anatomical gift and the coroner or medical examiner deems the death suspicious.
S4387	Provides that real property with a value of $50,000 or less may be included within the voluntary administration (SCPA article 13) of a small estate.
S4783	Relates to the liability of a trustee, other than a corporate trustee, for decisions of a delegee under the Prudent Investor Rule.
S4894	Establishes legal rights in grandparents who act as guardians and custodians of their grandchildren.
S5173	Provides for the indemnification of officers and directors of not-for-profit corporations and establishes the terms and conditions under which such indemnification may be accomplished.
S7085	Permits the modification and reformation of wills and trusts under certain circumstances to more accurately reflect the creator's intent or to accomplish a tax objective.
S7203 (substituted for A4739)	Amends relevant provisions of the SCPA, Domestic Relations and Social Services Laws by replacing the phrase "natural parent" with "biological parent." Signed 8/6/02, ch. 312.

Ronald J. Weiss is a partner of Skadden, Arps, Slate, Meagher & Flom LLP, and is Chair of the Legislation Committee of the Trusts and Estates Law Section.

The Internal Revenue Service Issues More Summonses for Offshore Credit Card Data

By William Garofalo, Val Albright and Marnin Michaels

Estate planning lawyers are oftentimes the primary contacts that clients deal with in discussing financial matters. From time to time, the practitioner will learn that a client has an account in a bank secrecy jurisdiction in which the income has not been reported on the client's U.S. tax return. Oftentimes, an attorney will learn after the death of an estate planning client, in the course of estate administration, that a client had a "secret account." This raises pitfalls for the trusts and estates lawyer. While dealing with undeclared taxpayer funds has always been an issue, it has risen in visibility due to the new Internal Revenue Service (IRS) credit card initiatives, which threaten to uncover accounts in tax secrecy jurisdictions. Trusts and estates lawyers should keep abreast of these developments to further help convince clients of the risks associated with such accounts. These initiatives obviously may threaten U.S. residents and citizens who fail to declare all of their funds. These initiatives also may impact non-U.S. residents, by either subjecting them to IRS scrutiny or through treaty disclosures to their home jurisdictions.

"While dealing with undeclared taxpayer funds has always been an issue, it has risen in visibility due to the new IRS credit card initiatives, which threaten to uncover accounts in tax secrecy jurisdictions."

The IRS recently issued another summons to MasterCard for data pertaining to certain credit or debit cards issued by banks in 30 perceived tax haven countries. This summons follows similar summonses issued to American Express and VISA and a more limited summons previously issued to MasterCard. The IRS also has issued a series of summonses to vendors who accept MasterCard, to identify additional persons with tax haven credit or debit cards. The IRS is intent on finding taxpayers with offshore bank accounts, and has focused on credit card companies as potential sources of information. Both United States and non-U.S. taxpayers with tax haven credit cards and unreported income may face substantial difficulties and need to explore their options.

The IRS credit card summonses demand that MasterCard (and VISA and American Express in prior cases) turn over names or transaction information for certain credit or debit cards issued by tax haven banks. The vendor summonses follow up on the transaction information to obtain names not directly available from the credit card companies. Between the credit card and vendor summonses, the IRS hopes to identify many of the U.S. taxpayers with tax haven credit cards.

Once the IRS identifies the holders of these tax haven cards, agents may investigate the cardholders for potential criminal and/or civil penalties. Many U.S. taxpayers owning tax haven credit or debit cards also own tax haven bank accounts used to conceal taxable income and pay the credit card balances. These taxpayers face potentially severe criminal penalties, largely based upon the amounts of unpaid taxes. Additionally, they face potential civil penalties that include a penalty of 75 percent of the unreported tax for fraud, and other severe penalties for failing to report interests in any foreign bank account, trust or corporation.

These U.S. taxpayers also may face difficulties if they attempt to belatedly report the omitted income. The IRS may still prosecute taxpayers who report omitted tax haven income, on the grounds that the taxpayer's disclosure was not "voluntary," but rather was caused by the likelihood of an eventual IRS investigation. In these cases, the taxpayer may actually make their case far worse by attempting to cooperate than if they had done nothing. The facts for each individual taxpayer need to be carefully considered before any action is taken that may worsen their situation.

A Critical Issue: Will the IRS Summonses Actually Uncover the Taxpayer?

If the IRS summonses are likely to lead to the discovery of the taxpayer, disclosure of the U.S. taxpayer's unreported income may make a criminal prosecution more likely. But if the IRS summonses will not discover the taxpayer's identity, the IRS may be willing to forgo criminal prosecution, in return for a voluntary reporting of the previously unreported income. Therefore, it is critical to analyze the taxpayer's specific circumstances to determine whether the

IRS summonses will actually lead to the IRS knowing the taxpayer's identity.

Frequently the credit card companies do not know the identity of the credit and debit cardholders. The banks issuing the cards, of course, know who the cardholders are, but these banks are often outside the jurisdiction of the IRS if they are located in a tax haven. The Internal Revenue Service seeks to avoid this problem by requiring the credit card companies to produce transactional data and then summonsing the vendors in the transactions to provide the names of the taxpayers associated with the transactions.

"United States taxpayers with offshore credit cards and unreported income should carefully review their situation in view of the IRS demands for credit card information, and the potential for criminal and civil penalties."

For example, the credit card summonses require production of certain airline transaction data. If the taxpayer purchased airline tickets with their tax haven credit card, the IRS could go to the airline and demand that it reveal the name of the taxpayer that purchased the ticket. The airlines keep identity information for their customers, and require those customers to verify their identity before boarding the airplane. Thus, a taxpayer who purchased airline tickets with a tax haven credit card may eventually have their identity revealed to the IRS. To date the IRS has issued summonses to about 40 vendors, including airlines, stores, Internet vendors, and Internet service providers.

The IRS summonses have detailed criteria as to which transactions should be handed over by the credit card companies. These criteria attempt to eliminate data pertaining to non-resident aliens. Even though a taxpayer has a tax haven credit card, they may not come within the summons criteria. Each taxpayer's transactions and circumstances must be evaluated to determine whether the summons will ultimately identify them. This analysis is critical to determining the future actions taxpayers with tax haven credit cards should take. A lawyer can only assist taxpayers in this analysis if the taxpayer plans to fully legitimize their tax affairs.

Other Key Considerations for U.S. Taxpayers

U.S. taxpayers with offshore credit cards face difficult decisions. The IRS may eventually use the John Doe summonses for credit card data to identify them. If the taxpayers attempt to amend their returns, the IRS may use the amended return against them in a criminal prosecution or to obtain severe civil penalties. While every taxpayer has unique facts that must be considered in these cases, some key factors include:

1. The IRS has not demanded the credit card information for all offshore credit cards. Taxpayers whose cards are outside the IRS demands should be able in most cases to avoid criminal penalties.
2. The IRS cannot identify many taxpayers even after receiving their credit card information. Unidentified taxpayers again may avoid criminal prosecution through voluntary disclosure. Determining which taxpayers will be identified is extremely complex and requires a detailed analysis of the taxpayer's transactions.
3. The IRS criteria for criminal prosecutions consider many factors, which make disclosures far more risky for some taxpayers than others.
4. The IRS has targeted certain types of transactions for more severe penalties and enforcement action.
5. Certain IRS offices may treat taxpayers more leniently.
6. Taxpayers may be able to take steps to comply with the law short of filing amended returns, and therefore decrease the likelihood of criminal or civil penalties.

United States taxpayers with offshore credit cards and unreported income should carefully review their situation in view of the IRS demands for credit card information, and the potential for criminal and civil penalties. They must consider all relevant facts before embarking on a course of action that could have substantial consequences.

Issues for Non-U.S. Taxpayers

The IRS credit card summonses are directed in part at identifying persons who frequently use tax haven credit cards in the United States. Two potential dangers arise for non-U.S. taxpayers who are identified by the credit card summonses. First, will the IRS

recognize that they are not subject to U.S. tax? Second, will the IRS pass data on to the nonresident's home jurisdiction?

Several of the credit card summonses demand data concerning persons charging expenses in the United States during six different months. While non-residents could charge items in the United States without actually being present there, the IRS may scrutinize such persons to ensure that they actually are not residents under the "substantial presence" test and they are not engaged in a U.S. business. Thus, the credit card summonses may result in wasteful or unwanted scrutiny as to the non-resident. In such cases, it may be advisable to immediately present the IRS with strong evidence of non-resident status, before any full investigation can begin.

The United States has tax treaties for exchange of information with many other countries. In virtually all of these treaties, the other jurisdiction may request information about specific taxpayers if the information is in the IRS's possession or reach. Most treaties also permit the IRS to forward suspicious data on its own. Even if the credit card data is not of interest to the United States, information about tax haven credit cards and accounts may be of interest to a taxpayer's home country. In view of this concern, care must be taken as to what evidence is provided to the IRS in proving non-resident status to avoid U.S. taxation. Thus, even people not subject to U.S. taxation may have reasons to be concerned about the credit card summonses.

Conclusions for the Estate Planning Attorney

Most estate planning lawyers are not trained to properly deal with the issue of undeclared funds. As the IRS further attempts to prosecute individuals in these circumstances, the estate planning lawyer needs to be fully versed on these clients to properly advise the client to regularize their past and refer the matter to a proper tax controversy attorney.

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PCBs Aren't Always Bad for Your Health

By Barbara S. Gerrard

On May 14, 2002, the IRS issued Final Regulations governing Electing Small Business Trusts (ESBT). These trusts were created under the Small Business Job Protection Act[1] in response to the need for more flexibility in permissible shareholders for S corporations. S corporations have traditionally been disadvantaged by the limitation on the number of permissible shareholders (until the 1996 Act enlarged that number to 75), the prohibition on more than one class of stock, and, from the standpoint of "traps for the unwary," the arcane rules and limitations on trusts as eligible S shareholders. It was the desire of Congress to introduce an entity shareholder that would encourage more creative estate planning opportunities and accommodate intrafamily economic realities.

The ESBT is defined by who its permissible beneficiaries are and how their interests were acquired.[2] For a trust to qualify both as an ESBT and as a shareholder in an S corporation, only certain types of persons are permitted to be beneficiaries. Once a trust makes the ESBT election, each potential current beneficiary (PCB—defined below) is treated as a shareholder of the S corporation. An ESBT cannot have any beneficiaries other than individuals, estates, or charitable organizations described in section 170(c)(2), (3), (4) or (5) (relating to various charitable organizations, war veterans organizations, fraternal lodges, and cemetery organizations).[3]

In addition, no interest in an ESBT may be acquired by purchase, i.e., where basis is determined by **cost** under section 1012.[4] Accordingly, it is presumed that the basis of a beneficiary's interest in an ESBT will be stepped-up basis for inherited property under section 1014, or carry-over basis in a gift situation, from donor to donee, determined by section 1015. Under these rules, a net gift of a beneficial interest in a trust, where the donee pays the gift tax, would be treated as a prohibited purchase of a beneficial interest.[5]

The prohibition on "purchases" applies to purchases of a beneficiary's interest in the trust, not to purchases *by* the trust. An ESBT itself may acquire property (including stock of an S corporation) by purchase, including a part-gift, part-sale (bargain-sale) transaction. For these purposes, a net gift to the trust itself, where the trustee of the trust pays the gift tax, is not prohibited.

Final Regulations

Final Regulations[6] have been issued which offer guidance concerning the qualification, taxation, and treatment of ESBTs. They replace previous IRS pronouncements,[7] and are referred to herein where relevant.

In order to make the ESBT election, the trust must not be an "*ineligible*" trust. An exempt trust is ineligible to make the ESBT election,[8] as are charitable remainder annuity trusts, charitable remainder unitrusts,[9] and qualified subchapter S trusts.[10]

"It was the desire of Congress to introduce an entity shareholder that would encourage more creative estate planning opportunities and accommodate intrafamily economic realities."

A trust must elect to be treated as an ESBT.[11] An election applies for the taxable year for which made and for all subsequent tax years.[12] Under the Regulations, the trustee of the trust must sign and file the ESBT election.[13] Generally, only one ESBT election is made for the trust, regardless of the number of S corporations whose stock is held by the ESBT. However, if the ESBT holds stock in multiple corporations that file in different service centers, the ESBT election must be filed with all the relevant service centers where the S corporations file their income tax returns.[14]

Coordination with Election to Be an ESBT or a QSST

An ESBT election cannot be made if the trust has an election in effect to be a "Qualified Subchapter S Trust" (QSST).[15] The IRS has provided a mechanism to convert from a QSST to an ESBT without requesting consent. Regulation section 1.1361-1(j)(12) requires, among other items, that both the trustee and the current income beneficiary of the trust must sign the election, and the election must be filed with the Service Center where the S corporation files its income tax return.[16]

The Final Regulations provide that the ESBT election and the election to convert from a QSST to an ESBT (or from a ESBT to a QSST) are all filed with the Service Center where the S corporation files its income tax returns.[17]

Unlike the QSST election, there is no "protective" ESBT election available.[18] In the Preamble to the Final Regulations, the IRS indicated why they had rejected a commentator's suggestion that a protective ESBT election be available where the trust fails to qualify as a wholly-owned grantor trust. According to the IRS, such "conditional" election would be inappropriate because the ESBT election must have a fixed effective date.

If, during the taxable year of an S corporation, a trust is an ESBT for a part of the year and an eligible shareholder under section 1361(c)(2)(A)(i) through (iv) for the rest of the year, the S corporation items are allocated between the two types of trusts under section 1377(a).[19]

Definitions

Regulation section 1.1361-1(m)(1) offers definitional guidance regarding ESBT terms, as follows:

> (1) A "distributee trust" is a trust that is receiving or may receive a distribution from an ESBT, whether the rights to receive the distribution are fixed or contingent, immediate or deferred.[20]
>
> (2) A "beneficiary" includes a person who has a present, remainder, or reversionary interest in the trust.[21]
>
> (3) A person in whose favor a power of appointment could be exercised is not a "beneficiary" of an ESBT *until* the holder of the power of appointment actually exercises the power in favor of such person.[22]

An attempt to *temporarily* waive, release or limit a power of appointment would not be effective to limit the number of potential current beneficiaries because of the uncertainty as to the effectiveness of a temporary waiver, release, or limitation on the power of appointment under state law, and the potential to manipulate a temporary waiver, release, or limitation to avoid the S corporation shareholder limitation rules. However, a *permanent* release thereof which is effective under local law *may* reduce the number of potential current beneficiaries.

Potential Current Beneficiary

Under the statutory scheme, for a trust to qualify as an ESBT, *and* as a shareholder in an S corporation, only certain types of persons are permitted to be beneficiaries of the trust. Once a trust makes the ESBT election, each potential current beneficiary of the trust is treated as a shareholder of the S corporation. Thus, the identity of the beneficiaries affects whether a trust can be an ESBT, while the identity and number of the potential current beneficiaries affect whether the corporation can be an S corporation.

The "potential current beneficiary" is defined as, with respect to any period, a person who, at any time during such period, is entitled to (or at the discretion of any person, may) receive a distribution from the principal or income of the ESBT.[23] No person is treated as a potential current income beneficiary *solely* because that person holds any future interest in the trust, including a person who, after the exercise of a power of appointment, nonetheless receives only a future interest in the trust.

Each potential current beneficiary will be treated as a shareholder of the S corporation for purposes of the 75 shareholder limitation. If a potential current beneficiary (or the spouse thereof) is also a direct shareholder in the S corporation, such person will not be counted twice for these purposes.[24]

A person who is entitled to receive a distribution only after a specified time or upon the occurrence of a specified event (such as the death of the holder of the power of appointment) is not a potential current beneficiary *until* such time or the occurrence of such event.[25]

A person to whom a distribution is or may be made during a period pursuant to a power of appointment is a potential current beneficiary. Thus, if any person has a lifetime power of appointment that would permit distributions from the trust to be made to more than 75 persons, the corporation's S election will terminate because the number of potential current beneficiaries will exceed the 75-shareholder limit. Also, the S corporation election will terminate if the currently exercisable power of appointment allows distributions to be made to an ineligible shareholder.

Some commentators to the Regulations as proposed were concerned that existing ESBTs with currently exercisable broad powers of appointment have resulted in certain S corporations exceeding the 75-shareholder limitation, and may have resulted in the termination of the related S corporations' S elections. The Final Regulations make it clear that, for purposes of the definition of potential current beneficiaries, *the applicable Regulations are effective for taxable years of*

ESBTs that begin on or after May 14, 2002. Therefore, persons who may receive a distribution from an ESBT pursuant to a currently exercisable power of appointment will not be considered potential current beneficiaries of the ESBT until the first day of the ESBT's first taxable year that begins on or after that date (and the S corporation's election will not terminate before that date.) Furthermore, if the trust disposes of all of its stock in the S corporation within 60 days after that date, the persons (who would first meet the definition of potential current beneficiaries on that date) will not be potential current beneficiaries and the corporation's S election will not be affected.[26]

The consent to the S election must be signed by the *trustee* of the ESBT *and* the "owner of any portion of the trust that consists of the stock in one or more S corporations."[27]

If for any period there is no potential current beneficiary, the ESBT itself will be treated as the shareholder.[28] If the ESBT disposes of all of its S corporation stock, then any person who first became a potential current beneficiary during the sixty-day period ending on the date of such disposition will not be a potential current beneficiary and thus is not a shareholder with respect to that corporation.[29]

If a distributee trust becomes entitled to, or at the discretion of any person may receive, a distribution from principal or income of the intended ESBT, then the S corporation election will terminate unless the distributee trust is an eligible shareholder of S corporation stock. In addition, the persons who are the beneficiaries of such distributee trust will be treated as the shareholders of the corporation for purposes of determining whether the restrictions on the number and eligibility of shareholders have been met.

Tax Treatment of an ESBT

For federal income tax purposes, an ESBT consists of an S portion, a non-S portion, and, in some cases, a "grantor" portion. The items of income, deduction, and credit attributable to any portion of the ESBT treated as owned by a person under the grantor trust rules of subpart E, including S corporation stock and other property (the "grantor portion"), are taken into account on that individual's (the "deemed owner's") tax return pursuant to the normal rules applicable to grantor trusts.

The portion of the ESBT which consists of stock in one or more S corporations, and is not treated as owned by the grantor or by another person, is treated as the separate "S portion" for purposes of computing the income tax attributable to such S corporation stock. Other items of income, deduction, and credit are attributed to either the S portion, which includes the S corporation stock, or the non-S portion, which includes all other assets of the trust. The S portion is subject to tax under the special rules of section 641(c), while the non-S portion is subject to the normal trust taxation rules of subparts A through D of subchapter J.

This tri-part system of taxation was introduced in the Proposed Regulations, and was met with a significant number of comments, both favorable and unfavorable. In the Preamble to the Final Regulations, the IRS and Treasury reiterated their support of this methodology, noting the "qualification of" and the "taxation of" ESBTs are two separate issues. The 1996 Act amendments to section 1361(e) expanded the permissible shareholders of an S corporation to include trusts that meet the definition of an ESBT. Because grantor trusts are not excluded from the definition of an ESBT, they are, accordingly, permitted to make the ESBT election.

Tax Treatment of Grantor Trust Portion

Making the election, however, does not alter the long-established treatment of tax items attributable to the portion of the trust treated as owned by the grantor or by another. Section 671 requires that items of income, deduction, and credit attributable to the portion of the trust treated as owned by a grantor or another must be taken into account by that deemed owner. Only remaining items of the trust are subject to the provisions of subparts A through D of subchapter J. With a grantor trust, once the ESBT election is made, the deemed owner is treated as a potential current beneficiary along with the others who meet the definition of a potential current beneficiary.

Tax Treatment of S Portion

The S corporation portion of the ESBT (except for capital gains) is taxed at the highest individual rate on this portion of the ESBT's income. For purposes of the alternative minimum tax, the exemption amount of the S portion under section 55(d) is zero.[30] The taxable income attributable to this S portion is determined by taking into account only the items of income, loss, deduction, or credit as described below, to the extent not attributable to the grantor portion:[31]

1. The items of income, loss, deduction, or credit that are taken into account by an S corporation shareholder pursuant to section 1366 and the Regulations thereunder;[32] if an ESBT owns stock in more than one S corporation, items of income, loss, deduction, or credit from all the S corporations are aggregated for purposes of determining the S portion's taxable income.[33]

If a deduction under this section is attributable to an amount of the S corporation's gross income that is paid by the S corporation *for a charitable purpose*, such contribution will be deemed to be paid out of the S portion pursuant to the terms of the trust's governing instrument.[34] A charitable contribution is deductible by the S portion, if at all, only in the year that it is an item required to be taken into account by the trust under section 1366. The trustee may not make the election to treat a contribution made by the S corporation after the close of the taxable year as being made during the taxable year. (This election is available only for charitable payments actually made by the trust, not for the trust's share of contributions made by another entity.) If S corporation *stock* is contributed to charity, no deduction is available to either the S portion or the non-S portion.[35]

2. Any gain or loss on the disposition of S corporation stock; however, no deduction is allowed for capital losses that exceed capital gains. Gain recognized from distributions in excess of the ESBT's basis in its S corporation stock is taken into account by the S portion.[36] If income from the sale or disposition of stock in an S corporation is reported by the trust on the installment method, the income recognized under this method is also taken into account by the S portion.

3. Any state or local income taxes and administrative expenses[37] directly related to the S portion,[38] and amounts properly allocable to the S corporation stock. Under Regulation section 1.641(c)-1(h), whenever state and local income taxes or administrative expenses relate to more than one portion of an ESBT, they must be allocated between or among the portions to which they relate. These items may be allocated in any manner that is reasonable in light of all the circumstances, including the terms of the governing instrument, applicable local law, and the practice of the trustee with respect to the trust.[39]

ESBT Treatment of Items—Non-S Portion

The taxable income of the non-S portion of an ESBT is determined by taking into account all items of income, deduction, and credit to the extent *not* taken into account by either the grantor portion or the S portion. The items attributable to the non-S portion are taxed under subparts A through D of Subchapter J. The non-S portion may consist of more than one share.[40]

Distributions to the beneficiaries from the S portion or the non-S portion, including a distribution of the S corporation stock, are, to the extent of the distributable net income of the non-S portion, deductible under sections 651 or 661 in determining the taxable income of the non-S portion, and includible in the gross income of the beneficiaries under sections 652 or 662.[41] However, the amount of the deduction or inclusion cannot exceed the amount of the distributable net income of the non-S portion. For these purposes, items of income, loss, deduction, or credit taken into account by the grantor portion or the S portion of the trust are excluded from the calculations in determining the distributable net income of the non-S portion of the trust.

In rejecting a commentator's suggestion that, because the S portion and the non-S portion are treated as separate trusts, the source of the distribution should determine its tax treatment, the IRS noted that section 641(c)(3) provides that section 641(c) does not affect the taxation of any distribution from the trust except for the exclusion of the S portion items from the distributable net income of the entire trust. Thus, the rules otherwise applicable to trust distributions apply to ESBTs.

Where the trust has fiduciary accounting income in the S portion, the non-S portion, and possibly in the grantor portion, the treatment of distributions is determined under the usual rules of trust taxation, as follows:

Under section 641(d)(3), except as otherwise specified, this section (641(d)) does not change the taxation of any distribution from the trust. Because the S portion items are not included in the computation of the ESBT's distributable net income, they will be treated (for purposes of determining the treatment of trust distributions) in the same manner as any other item that does not enter into the distributable net income computation (e.g., capital gains and losses allocated to corpus). For example, for the tax year an ESBT has $40 of distributable net income from the non-S portion and $70 of net fiduciary accounting income from the S portion. If the ESBT makes a distribution of $100, the distribution includes $40 of distributable net income. Accordingly, when a distribution is made by an ESBT, the current distributable net income will be carried out before the S portion (which had been previously taxed at the trust level and would be distributable to the beneficiaries tax-free).

If income from the sale or disposition of stock in an S corporation is reported by the trust on the installment method, the interest on the installment obligation is includible in the gross income of the *non-S portion*.[42] Dividend income (as defined in section 1368(c)(2)), is also includible in the non-S portion of the trust.

Loss Carryovers in the Event of Termination or Revocation of an ESBT Election

If the ESBT election terminates or is revoked, and the S-portion of the ESBT has a net operating loss, a capital loss carryover, or deductions in excess of gross income, then any such loss carryover, or excess deductions, shall be allowed as a deduction to the trust in accordance with the rules of section 642(h), or to the beneficiaries succeeding to the property of the trust if the entire trust terminates.[43]

Trust's Taxable Year

If an ESBT election is effective on a day other than the first day of the trust's taxable year, the ESBT election does not cause the trust's taxable year to close. The termination of the ESBT election (including a termination caused by a conversion of the ESBT to a QSST) other than on the last day of the trust's taxable year, also does not cause the trust's taxable year to close.[44]

Conclusion

The stated intent of Congress in establishing the ESBT in the 1996 Act was to "facilitate family financial planning."[45] Congress believed that a trust that provides for income to be distributed to (or accumulated for) a class of individuals should be allowed to hold S corporation stock, allowing an individual to "spray" income among family members (or others) as beneficiaries of such trust.[46] The IRS, in its Regulations, has fleshed out the requirements for shareholders to achieve these goals, and provided a precise and understandable taxation scheme for the various components of each ESBT, i.e., the grantor portion, the S portion, and the non-S portion.

Attached is a **"Summary Chart of Trusts as S Corporation Shareholders"** outlining the characteristics of the various trusts which are eligible to be S corporation shareholders:

Summary Chart of Trusts as S Corporation Shareholders

Permissible Trust	Taxable Entity	Must Elect To Be An Eligible Trust	Must Distribute § 643(b) Income	Termination of S Shareholder Status
Grantor Trust	Grantor	No	No	Two years after grantor's death
Voting Trust	All owners of a beneficial interest	No	No	None
Testamentary Trust	Estate of testator	No	No	Two years from date of receiving S corporation stock
Section 678 Trust	Deemed owner under § 678	No	No	Two years after deemed owner's death
QSST	Current income beneficiary	Yes, within two months and 15 days of receiving stock	Yes	(1) Failure to comply with QSST provisions; (2) Successor beneficiary affirmatively refuses QSST election
ESBT	The ESBT itself (which consists of an S portion, a non-S portion, and, in some cases, a "grantor" portion)	Yes, within two months and 15 days of receiving stock	No (because ESBT is taxed on all income at the highest individual rate with no deduction for distributable net income)	As for S portion, no requirement to distribute because that portion of trust is taxed on all income with no deduction for distributable income. Non-S portion is taxed under subparts A through D of subchapter J, and "grantor" portion is taxed under grantor-trust rules.

Endnotes

1. Pub. L. No. 104-188, signed into law on Aug. 20, 1996, and referred to herein as the "1996 Act."
2. I.R.C. §§ 1361(c)(2)(A)(v) and 1361(e).
3. For tax years beginning after Dec. 31, 1996, but before Jan. 1, 1998, any such charitable organization could only hold a *contingent interest*, and could not be a *potential current beneficiary.* I.R.C. § 1361(e)(1)(A)(i). After Dec. 31, 1997, there is no limitation on the interests a qualified charitable organization may hold.
4. I.R.C. § 1361(e)(1)(A)(ii).
5. Reg. § 1.1361-1(m)(1)(iii).
6. Reg. § 1.1361-1(m), (T.D. 8994, May 14, 2002, replacing Temp. Regs. issued Dec. 29, 2000). The Regulations also contain other relevant provisions affecting the taxation of ESBTs under I.R.C. §§ 444 and 641(c).
7. Before the Regulations were proposed, the IRS had issued Notice 97-12, (1997-1 C.B. 385), Notice 97-49 (1997-2 C.B. 304), and Rev. Proc. 98-23 (1998-1 C.B. 662), all of which were *superceded* upon the date Final Regulations were published in the Federal Register, i.e., May 14, 2002. Because of perceived abusive transactions concerning ESBTs and the taxation of the grantor portion of the ESBT's income (*see* Notice 2000-61, 2000-49 I.R.B. 1), the Regulations governing the taxation of the grantor portion of an ESBT under Reg. §§ 641(c)-1(a), (b), (c), and Ex. 1 of (*l*) are applicable for taxable years of ESBTs that end on and after the date the Prop. Regs. were published (i.e., Dec. 29, 2000). Reg. § 1.641(c)-1(k).
8. I.R.C. § 1361(e)(1)(B)(ii). However, certain tax-exempt organizations are eligible to hold S corporation stock outright.
9. As defined in I.R.C. § 664(d). Reg. §§ 1.1361-1(m)(1)(iv)(B) and (C).
10. Reg. § 1.1361-1(m)(1)(iv)(A), discussed *infra.*
11. Guidance has been provided regarding the mechanics of the ESBT election. Reg. § 1.1361-1(m)(2)(iii) states that the election must be filed *by the trustee* of the trust seeking ESBT status within the same time limits for filing a QSST election (generally within the two-month, 15-day period beginning on the day the stock is transferred to the trust). For purposes of a testamentary trust which receives S corporation stock by the terms of a will, or a trust which, before the death of the grantor, had been taxed as a grantor trust (pursuant to I.R.C. §§ 1361(c)(2) (A)(iii) or (ii), respectively), the trustee shall have the two-year period *plus* the two-month and 15-day period during which to elect to be taxed as an ESBT. If such trust makes an ineffective ESBT election, it will nevertheless continue to qualify as an eligible S corporation shareholder for the remainder of the statutory two-year period. Reg. § 1.1361-1(m)(2)(iv). Reg. § 1.1361-1(m)(2)(ii) contains these additional requirements:
    1. A statement must be signed and filed with the Service Center with which the corporation files its income tax return containing the name, address, and taxpayer identification number of all potential current beneficiaries, the trust, and the corporation. (In the case of a newly-electing S corporation, the ESBT election may be attached to the Form 2553.);
    2. The statement must identify itself as an election under I.R.C. § 1361(e)(3);
    3. The statement must specify (a) the date on which the election is to become effective (not earlier than two months and fifteen days before the date on which the election is filed); and (b) the date (or dates) on which the stock of the corporation was transferred to the trust;
    4. The statement must provide all information and representations necessary to show that:
        (a) All potential current beneficiaries meet the shareholder requirements of I.R.C. § 1361(b)(1); and,
        (b) The trust meets the definitional requirements of an ESBT under I.R.C. § 1361(e)(1).
12. I.R.C. § 1361(e)(3).
13. Reg. § 1.1361-1(m)(2)(i). If there is more than one trustee, the trustee or trustees with authority to legally bind the trust must sign the election statement. If any one of several trustees can legally bind the trust, then only one such trustee need sign the election.
14. *Id.* This requirement only applies at the time of the initial ESBT election. If the ESBT later acquires stock in an S corporation which files its income tax return at a different Service Center, a new ESBT election is not required. With a QSST, a separate QSST election is made with respect to each corporation in which the QSST trust holds stock.
15. I.R.C. § 1361(e)(1)(B)(i) and Reg. § 1.1361-1(m)(1)(iv). Before the issuance of the Regulations, the IRS declined to rule on requests by QSSTs to revoke their QSST status and convert to ESBTs, instead directing the taxpayers to the requirements of Rev. Proc. 98-23, 1998-1 C.B. 647.
16. Reg. § 1.1361-1(j)(12)(ii). The election must also state at the top: "ATTENTION ENTITY CONTROL—CONVERSION OF A QSST TO AN ESBT PURSUANT TO SECTION 1.1361-1(j)."
17. There is finally consistency here. *See* Reg. § 1.1361-1(m)(2)(i) and Reg. § 1.1361-1(j)(12)(ii).
18. Reg. § 1.1361-1(m)(2)(v).
19. Reg. § 1.1361-1(m)(3)(iv), *and see* Reg. § 1.1377-1(a)(2)(iii). According to the Preamble to the Final Regulations, conversion of a trust to an ESBT or a QSST does not result in the prior trust terminating its entire interest in the S corporation, unless the prior trust was a trust described in I.R.C. § 1361(c)(3)(A)(ii) or (iii). When a trust described in one of these two sections converts to an ESBT or a QSST, the shareholders of the S corporation change from the estate of the deemed owner or testator to the potential current beneficiaries of the ESBT, or the current income beneficiary of the QSST. When a trust changes from a wholly-owned grantor trust or QSST to an ESBT, or from an ESBT to a QSST, the individuals who are shareholders of the S corporation remain the same. *Thus, for these purposes, the election to terminate the taxable year pursuant to I.R.C. § 1377(a)(2) applies to the conversion of a trust described in I.R.C. § 1361(c)(3)(A)(ii) or (iii) to an ESBT or to a QSST as a termination of the prior trust's interest in the S corporation, but it does not apply to other conversions to an ESBT or a QSST.*
20. Reg. § 1.1361-1(m)(1)(ii)(B). A distributee trust is the beneficiary of the ESBT only if such trust is a charitable organization described in I.R.C. § 170(c)(2) or (3). In all other situations, any person who has a beneficial interest in a distributee trust is the beneficiary of the ESBT.
21. Reg. § 1.1361-1(m)(1)(ii)(A).
22. Reg. § 1.1361-1(m)(1)(ii)(C).

23. I.R.C. § 1361(e)(2) and Reg. § 1.1361-1(m)(4)(i).
24. Reg. § 1.1361-1(m)(4)(vii).
25. Reg. § 1.1361-1(m)(4)(v).
26. I.R.C. § 1361(e)(2), and the Preamble to the Final Regulations.
27. Reg. § 1.1362-6(b)(2). If there is more than one trustee, the trustee or trustees with the authority to legally bind the trust must consent to the S election.
28. I.R.C. § 1361(c)(2)(B)(v).
29. Reg. § 1.1361-1(m)(4)(iii).
30. Reg. §§ 1.641(c)-1(d)(1).
31. Reg. § 1.641(c)-1(e)(1) and (2). *See* I.R.C. § 1(h) for the rates that apply to the S portion's net capital gain.
32. In determining the extent to which any loss, deduction, or credit may be taken into account to arrive at the taxable income of the S portion, the rules otherwise applicable to trusts still apply. Reg. § 1.641(c)-1(d)(1). *See* Reg. § 1.1361-1(m)(3)(iv) for the rules for allocating those items in the taxable year of an S corporation in which the trust is an ESBT for only part of the year. *Id.*
33. Reg. § 1.641(c)-1(d)(2)(iii).
34. Reg. § 1.641(c)-1(d)(2)(ii). For what constitutes the "trust's governing instrument," *see*, I.R.C. § 642(c)(1). The limitations contained in I.R.C. § 681, regarding unrelated business taxable income, apply in determining whether the contribution is deductible in computing the taxable income of the S portion.
35. In the Preamble to the Final Regulations, the IRS discussed one commentator's suggestion that, if the trust contributes S corporation stock to a charitable organization, the S portion should be entitled to a deduction with respect to the contribution. In rejecting this suggestion, the IRS noted that deductions available to the S portion are limited by I.R.C. § 641(c)(2)(C) to S corporation items required to be taken into account under I.R.C. § 1366 and the S portion's share of state and local income taxes and administrative expenses. Charitable contributions by the trust are not items included in that list.
36. Reg. §§ 1.641(c)-1(d)(3)(i) through (iii).
37. If an ESBT incurs interest expenses in connection with the acquisition of S corporation stock, such expenses are allocated to the S portion of the ESBT, but they are not allowable deductions for purposes of determining the taxable income thereof. Reg. § 1.641(c)-1(d)(4)(ii). Any such interest expenses incurred to acquire S stock would be deductible by the S portion only if they are "administrative expenses" under section 641(c)(2)(C)(iii). Pursuant to the Final Regulations, "administrative expenses" include the traditional expenses necessary for the management and preservation of trust assets, but do not include expenses incurred to acquire additional assets. Accordingly, interest expenses incurred by an ESBT to purchase S corporation stock will be treated as a non-deductible expense allocable to the S portion. In response to comments to the Regulations as proposed suggesting that the non-deductible expenses be used to increase basis of the assets so acquired (i.e., the S corporation stock), the IRS noted that there is no statutory authority to permit such an increase in basis. *See*, the Preamble to the Final Regulations under I.R.C. § 641(c).
38. I.R.C. § 641(c)(2)(C)(iii) and Reg. § 1.641(c)-1(d)(4)(i).
39. The Preamble to the Final Regulations makes it clear that the Regulations governing the treatment of state and local taxes and administrative expenses (Regs. §§ 1.641(c)-1(d)(4) and (h)) may be applied to taxable years beginning after Dec. 31, 1996.
40. Pursuant to I.R.C. § 663 and the Regulations thereunder. Reg. § 1.641(c)-1(g)(1).
41. Reg. § 1.641(c)-1(i).
42. Reg. § 1.641(c)-1(g)(3). Under Reg. § 1.641(c)-1(d)(3)(ii), the *income* from the sale or disposition of stock in an S corporation sold using the installment sale method is recognized by the S portion of the trust.
43. Reg. § 1.641(c)-1(j).
44. Reg. § 1.1361-1(m)(3)(iii). In either case, the trust files one tax return for the taxable year.
45. Joint Comm. on Taxation, Gen'l Explanation of Tax Legislation Enacted in 104th Cong, JCS-12-96 ("Blue Book") at 113 (Dec. 18, 1996).
46. *Id.*

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The Effect of Recent Federal Estate Tax Legislation on the New York Estate Tax: Part II Calculating the New York Estate Tax

By Philip L. Burke

Background

In the Fall 2002 issue of this *Newsletter*, Part I of this article addressed the changes to the New York estate tax brought about as a result of the passage of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). The passage of EGTRRA was a "good news/bad news" situation. The good news, as determined by the New York State Department of Taxation and Finance, is that the applicable estate tax exemption for New York estate tax filing purposes for 2002 and 2003 is the same as the federal exemption of $1 million for these years.[1] However, the "bad news" comes in two parts. First, the $1 million estate tax exemption will not increase, for New York estate tax purposes, in the same manner as the scheduled increases in the federal estate tax exemption. Consequently, starting in 2004 New Yorkers will still be subject to a $1 million estate tax exemption (unless changed by the state legislature) while, for federal estate tax purposes, the estate tax exemption will increase to $1.5 million (with further increases scheduled through 2009). Secondly, EGTRRA adjusted the calculation of the Credit for State Death Taxes for federal estate tax purposes. EGTRRA reduces the amount of the State Death Tax Credit for 2002 by 25%, with further reductions in 2003 (50%) and in 2004 (75%). In 2005, the State Death Tax "Credit" is eliminated and is replaced by a deduction that will be used in determining the federal estate tax through 2009.

"The passage of EGTRRA was a 'good news/bad news' situation."

Also, as indicated in Part I of this article, New York State remains an "SOP" tax state and will still calculate the amount of tax payable to New York State under the Credit for State Death Tax tables that were in effect in 2001, prior to the passage of EGTRRA.[2] The calculation of this tax, for New York purposes, will not be subject to the percentage reductions in the calculation of the federal State Death Tax Credit discussed above. Consequently, while the tax available as a credit to offset the federal estate tax is reduced, the amount of tax payable to New York State is not.

Estate Tax Relief?

As can be seen by the following "Relevant Rates" chart,[3] the much-publicized decrease in estate taxes that was supposed to be realized as a result of the passage of EGTRRA actually results in an increase in estate taxes in states (such as New York) where the Credit for State Death Taxes is "frozen" at 2001 levels. As indicated above, New York's "SOP" or "pick-up" tax is equal to the amount of the Credit For State Death Taxes calculated without the percentage reductions mandated by EGTRRA.

"[W]hile the tax available as a credit to offset the federal estate tax is reduced, the amount of tax payable to New York State is not."

The chart compares the relevant tax rates under EGTRRA (which also calls for an annual reduction in the highest federal estate tax brackets) with the "frozen" State Death Tax Credit applicable in New York. For example, in 2002, the highest federal estate tax rate is 50%, and the federal State Death Tax Credit is reduced from the 2001 rate of 16% to 12% (the mandated 25% reduction), resulting in a net federal rate of 38%. However, with New York's tax still calculated at a maximum of 16%, the actual percentage applicable to New York State taxpayers in the highest bracket is 54%. While this may represent a 1% reduction from 2001 rates, as the chart indicates the actual tax rate *increases* to 57% in 2003 with a maximum of 63% in 2005, and a 61% rate through 2009. Since the estate tax is scheduled to be repealed in 2010, the rate then drops to the 16% maximum rate under the Credit For State Death Tax tables currently in effect. Also, in 2011, when the "repeal of the estate tax" is itself repealed, the rate again bounces to 2001 levels, or 55%.

Relevant Rates					
	Gross Federal Rate	Conforming Credit	Net Federal Rate	Frozen Credit	Frozen Pick Up State
2001	55	-16	= 39	+16	= 55
2002	50	-12	= 38	+16	= 54
2003	49	-8	= 41	+16	= 57
2004	48	-4	= 44	+16	= 60
2005	47	-0	= 47	+16	= 63
2006	46	-0	= 46	+16	= 62
2007	45	-0	= 45	+16	= 61
2008	45	-0	= 45	+16	= 61
2009	45	-0	= 45	+16	= 61
2010	0	-0	= 0	+16	= 16
2011	55	-16	= 39	+16	= 55

Calculation of New York Estate Taxes

As the following calculations will illustrate, for the 2002 and 2003 tax years the change in the calculation of the State Death Tax Credit for federal estate tax purposes will result in the payment of increased estate taxes even though the amount of the taxable estate is unchanged.

For Example:

2002 Taxable Estate	$2,000,000
Gross Federal Estate Tax	$780,800
Federal Applicable Credit Amount	(345,800)
Federal Credit for State Death Taxes	(74,700)
Net Federal Tax	$360,300
New York Estate Tax ($74,700 ÷ .75)	$99,600
Total Tax	$459,900
2003 Taxable Estate	$2,000,000
Gross Federal Estate Tax	$780,800
Federal Applicable Credit Amount	(345,800)
Federal Credit for State Death Taxes	(49,800)
Net Federal Tax	$385,200
New York Estate Tax ($49,800 ÷ .50)	$99,600
Total Tax	$484,800

In 2004, when the federal estate tax exemption increases to $1.5 million, and the New York estate tax exemption remains fixed at $1 million, we again run into the situation encountered by estates of decedents dying prior to February 1, 2000, of paying a New York estate tax in situations where no federal estate tax (or even a federal estate tax return) was due. New York estate tax returns will be required to be filed (and, potentially, estate tax paid) for taxable estates falling between the $1 million New York estate tax exemption and the $1.5 million federal estate tax exemption. Also, since the Credit for State Death Taxes is reduced for federal purposes by 75% in 2004, New York will continue to collect taxes substantially in excess of that which is allowed as a credit against the federal estate tax.

"[S]ince the Credit for State Death Taxes is reduced for federal purposes by 75% in 2004, New York will continue to collect taxes substantially in excess of that which is allowed as a credit against the federal estate tax."

The next set of calculations compares the amount of New York estate taxes to be paid where a federal estate tax return is required and where one is not.

2004 Taxable Estate	$2,000,000
Gross Federal Estate Tax	$780,800
Federal Applicable Credit Amount	(555,800)
Federal Credit for State Death Taxes	(24,900)
Net Federal Tax	$200,100
New York Estate Tax ($24,900 ÷ .25)	$99,600
Total Tax	$299,700
2004 Taxable Estate	$1,450,000
Gross Federal Estate Tax	$534,300
Federal Applicable Credit Amount	(555,800)
Federal Credit for State Death Taxes	(0)
Net Federal Tax	$0
New York Estate Tax (from State Death Tax Credit Table for 2001)	$61,200
Total Tax	$61,200

As you can see, where the 2004 taxable estate ($1,450,000) is less than the federal filing threshold, obviously there is no federal tax and no Credit for State Death Taxes.

From 2005 through 2009, when the Credit for State Death Taxes is replaced by a deduction allowable in determining the federal taxable estate, presumably New York State will still collect its tax in the amount of the "credit" as calculated under the 2001 tables. As indicated in Part I of this article, these tables can be found in the current New York State Estate Tax Return, Form ET-706. The following calculation shows the interplay between the New York estate tax and how this tax is deducted for federal estate tax purposes.

2005 Taxable Estate	$2,000,000
Deduction for State Death Taxes[4]	$99,600
Adjusted Federal Taxable Estate	$1,900,400
Gross Federal Estate Tax	735,980
Federal Applicable Credit Amount	(555,800)
Net Federal Tax	$180,180
New York Estate Tax	$99,600
Total Tax	$279,780

New York Estate Tax and Non-Residents

Section 960 of the Tax Law of the state of New York addresses the calculation of a "non-resident's" estate tax. A non-resident of the state of New York who, at the time of death, owns real and/or tangible personal property actually located within New York State is subject to estate tax in the same manner as if the decedent was a resident of New York. However, the amount of the New York tax payable (which, as indicated above, is the amount of the State Death Tax Credit calculated under the 2001, pre-EGTRRA tables) is reduced by *the lesser* of: (1) the amount of the death tax paid to other states that is allowed as a federal Credit For State Death Taxes; or (2) an amount determined by multiplying the maximum federal Credit For State Death Taxes by a fraction, the numerator of which is the decedent's federal gross estate reduced by his New York gross estate and the denominator of which is his federal gross estate.[5] This second calculated reduction is an attempt to allocate the total amount of tax to be paid pro-rata between two jurisdictions (New York and the state of residence of the decedent).

However, for large, non-resident estates that include property taxable in New York, there is a potential for the amount of New York non-resident estate tax to actually exceed the value of the property located in New York. Because of the 25% reduction (in 2002) in the amount of the State Death Tax Credit for federal estate tax purposes discussed above, if the value of the non-resident's property that is subject to tax in New York State is less than the 25% difference between the New York tax and the reduced federal credit, New York will collect an estate tax in an amount greater than the value of New York property. For example, using round numbers, if the New York estate tax is $1 million (before the reduction for the tax paid to the state of domicile), the State Death Tax Credit for federal estate tax purposes is $750,000 ($1 million less the 25% reduction). If the deceased taxpayer resided in a state that is a "true" SOP tax state which collects only the amount of the actual federal Credit For State Death Taxes ($750,000 in this example), that state would collect the $750,000 SOP tax. The New York estate tax would be reduced by this payment, leaving a balance due and payable to New York in the amount of $250,000. If the value of the actual taxable property located in New York is less than $250,000, the New York estate tax payment will be greater than the value of the taxable New York property. This result is due to the fact that section 952 of New York's Tax Law mandates that the New York

estate tax be reduced by the *lesser* of the tax paid to the other jurisdiction or the pro-rated allocation of the tax. Since a true "SOP" tax state will receive a tax, in 2002, that is 25% less than the New York tax, the New York tax will most likely be reduced by this lower number, leaving the difference payable to New York.

This is an issue that will have to be addressed legislatively. As indicated, the source of this problem can be found in section 952 of New York's Tax Law and the reference to the Credit for State Death Taxes. Paragraph (a) of that section imposes a New York estate tax in an amount equal to the credit for state death taxes under IRC § 2011. As indicated above, however, paragraph (b)(1) reduces this tax by the amount of death tax paid to another jurisdiction that is "allowable as the federal credit for state death taxes." Since New York estate tax law does not automatically incorporate legislative changes to the federal estate tax laws, New York continues to calculate its tax under the 2001 Credit for State Death Tax table. However, if the other jurisdiction only collects tax in the amount of the "reduced" credit (which is the amount "allowable" as a credit against the federal estate tax under section 952) there will continue to be a "disconnect" in the calculation of the New York estate tax and the allowable federal Credit for State Death Tax.

Also, as the differential between the New York estate tax and the federal Credit for State Death Taxes increases in 2003 and 2004, it would appear that this problem may actually get worse. In those circumstances, with a 50% difference between the New York estate tax and the federal credit in 2003, and a 75% difference in 2004, the scenario in which the New York estate tax would exceed the value of the New York taxable property of a non-resident becomes even more plausible since the amount of the reduction in the New York estate tax under section 952 will potentially be even less.

However, in 2005, when the credit is replaced for federal estate tax purposes with a deduction, it is unclear how this issue will pan out. The two obvious factors in determining whether or not this continues to be a problem from 2005 through 2009 is how New York decides to calculate its estate tax at that time (and whether or not any legislative changes have come into play) and how the non-resident's state of residence calculates its tax. Since there will no longer be a federal "State Death Tax Credit," but only a deduction for state death taxes paid, those states that impose a tax equal to the amount of the State Death Tax Credit will have to re-legislate their own tax structure in order to continue to receive tax revenue. In situations where a particular jurisdiction determines not to collect an estate tax (however unlikely that may appear to New Yorkers), there would be no tax paid to the other jurisdiction that would reduce the New York tax, which would result in New York receiving an even larger amount of estate tax from non-resident estates with taxable New York property.

In conclusion, New York residents once again find themselves in the same estate tax situation that was in place prior to February 1, 2000, when the amount of New York estate tax paid exceeded the federal credit for state death taxes (and often exceeded the tax paid by residents of other states). This differential will only get worse in future years when the federal estate tax exemption exceeds the $1 million New York exemption, and when the credit for state death taxes is subject to further reductions and the ultimate conversion to a deduction (instead of a credit) from 2005 through 2009. Also, for non-residents owning estate-taxable property in New York the potential for paying New York estate tax in excess of the value of the New York property should be a tremendous cause for concern and may result in the non-residents severing all ties with New York and disposing of the taxable property. Hopefully, the legislature will address these issues in a timely and appropriate manner.

Endnotes

1. Technical Services Bulletin Memorandum, TSB-M-02(2) M (Mar. 21, 2002).
2. *Id.*
3. The author would like to thank Joshua Rubenstein, of KMZ Rosenman, a former Chair of the Section, for allowing the reprint of this chart which was used by him in, among other things, addressing these concerns with members of the New York State legislature.
4. Calculated from State Death Tax Credit Table for 2001.
5. *See* N.Y. Tax Law §§ 960, 952.

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New York State Bar Association Trusts and Estates Law Section

Fall 2002 Meeting • Boston, MA

Sleepless in Boston: Administering the Problem Estate

Program Summary

For those of you who were unable to attend our Section's Fall Meeting in Boston, you missed a fun time and an informative program, or, for tax deduction purposes, an informative program and an okay time. Our Chair, Arlene Harris, chose an excellent hotel on the waterfront in downtown Boston and we were treated to an informative cocktail reception at the JFK Library and a dinner at the Boston Museum of Fine Arts.

The topic was Administering the Problem Estate and our distinguished panel proposed solutions to many recurring problems that we face in administering the more problematic estates.

On Friday, Jonathan J. Rikoon spoke about "Difficult Decedents," offering suggested approaches to handling an estate where the decedent led a less than conventional life—decedents who failed to file income or gift tax returns or were less than forthright about values on their gift tax returns. Surrogate Kate Doyle discussed the use of will construction proceedings as methods to deal with "Problem Wills"—wills that are ambiguous, contain mistakes, missing bequests, and impractical provisions. Gary Mund discussed "Probate Issues"—such as determining domicile, dual jurisdiction probate, lost wills, missing attesting witnesses, and acquiring jurisdiction over all parties that should be cited. Victoria D'Angelo then discussed "Ethical Traps for the Unwary Practitioner"—issues such as who is the client in an estate matter, conflicts of interest, the attorney-client privilege and the recent legislation abolishing the fiduciary-exception to the privilege, the pitfalls in representing multiple fiduciaries, self-dealing and the potential problem where the attorney is asked to wear multiple hats such as drafter/beneficiary or drafter/fiduciary.

Saturday's program began with Mike Supronowicz's discussion of "Tax Apportionment Traps" and why the tax apportionment clause may be the most important dispositive provision in a will or trust; the various rules of construction used in construing these clauses; and the impact of lifetime gifts and non-probate assets. Linda Wank spoke about "Problematic Assets and Valuation Issues—Practical and Ethical Considerations" that can arise in handling the estate involving collectibles or intellectual property rights, such as the IRS appraisal requirements, blockage discounts, valuation of intellectual property rights, succession rights, and the right of publicity. Nicole Marro discussed the nightmare of the "Insolvent Estate" from both the fiduciary and the creditor's perspective, how to negotiate the numerous claims provisions contained in SCPA article 18, the order of payment of claims when there are insufficient assets and the order of abatement legacies. Steve Hand spoke about "Accounting Issues" that can arise with the problem estate and how to avoid them; the recent amendment of SCPA 711 and SCPA 2205 to provide a beneficiary or creditor with additional relief when a fiduciary fails to comply with an order to account; the importance of Schedule K where you make disclosure of matters such as any questionable transactions, the operation of a business, the ademption of legacies, tax elections, adjustments and apportionments, the need for construction and any open issues remaining in the estate.

The program concluded with a presentation by two Massachusetts attorneys, Hanson Reynolds and Albert Fortier, who discussed "Administering Trusts the Massachusetts Way." We learned that in contrast to the practice in New York, many firms in Massachusetts provide the same services as trust companies in New York—members of the firm are named as trustees and the firms have full-service trust departments to administer the trust; some firms even have created subsidiaries that provide investment advisory services.

In addition to the outstanding presentations by the panelists, attendees also received a two-volume course book, assembled by Ilene Cooper, which contained articles by the panelists, as well as a wealth of relevant cases, statutes and articles relating to the speakers' presentations—a resource that will undoubtedly receive heavy use in the future. This issue and future issues will reprint several of the speakers' articles for the benefit of those who could not attend.

The weather cooperated for the tennis and golf outings; we enjoyed a bright sunny Saturday afternoon. The tennis tournament sponsored by Fiduciary Trust International was held at the Boston Athletic Club. The golf outing was again sponsored by Brown Brothers Harriman Trust Company and held at Brookline Golf Club. Richard Rothberg, Lansing Palmer, Rich Carter and Gerard Joyce took top honors as first-place team. For those who did not participate in either tournament there was the "Duck Tour," numerous self-guided walking tours and Surrogate Czygier's walking tour of the "Big Dig."

The program was chaired by Gary B. Freidman and Barbara Levitan.

Scenes from the

Fall Meeting

October 3-6, 2002 • Boston, MA



















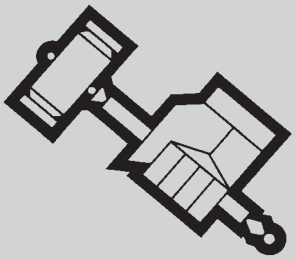

RECENT NEW YORK STATE DECISIONS

John C. Welsh

WILLS

PROBATE—UNDUE INFLUENCE

An elderly wealthy testator died in 1992 leaving a 1988 will which divided his residuary estate into seven equal shares. Four of these shares were to be taken by his sister, M, and her three children. Objections were filed by H, a distributee-brother, who took one share of the 1992 residuary estate and by R and S, children of testator's deceased brother, N, who were included as residuary beneficiaries in the 1986 will of decedent and were also distributees. R and S had been omitted from the 1988 will. The Appellate Division affirmed the finding of the Surrogate that the will was the product of undue influence exerted by M. At the time of the 1988 will execution, M was in control of the testator's finances and he had begun showing signs of physical and mental deterioration after living an independent life. M had prepared checks which testator signed that transferred hundreds of thousands of dollars to an account for which M had authority to sign checks. Although testator had not established a pattern of family giving, when M took over the finances, he transferred approximately $1.5 million to new accounts jointly with M's children. The issue of testamentary capacity, found to be lacking by the Surrogate, was not addressed. *In re Estate of Rosen*, __ A.D.2d__ , 747 N.Y.S.2d 99 (2d Dep't 2002).

OBJECTIONS TO PROBATE

Testator's will devised his real estate and bequeathed his 51% interest in his auto body business to his daughter, A, with a life interest in one-half thereof to his wife. His other daughter, B, was bequeathed $5,000. A worked with her father in the business and owned the remaining 49% interest. B unsuccessfully objected that (1) the will was improperly executed; (2) testator lacked testamentary capacity and (3) A exerted fraud and undue influence over testator. The attorney-drafter, who was also an attesting witness, and the other attesting witness testified as to a voluntary, proper execution. Negative comments made by A to testator about B were irrelevant because there was no showing that they had any impact on him. The fact that the will offered for probate made substantial changes in the previously existing estate plan was also irrelevant. *In re Estate of Minervini*, __ A.D.2d__ , 745 N.Y.S.2d 625 (3d Dep't 2002).

OBJECTIONS TO PROBATE

Objectants were unsuccessful in their claims that decedent's will was executed when she lacked testamentary capacity and that proponent exercised undue influence over her. Although she was sometimes confused, at the will execution, testatrix knew the natural objects of her bounty and the nature and extent of her property. Speculation and motive were insufficient to prove the moral coercion required for undue influence. *In re Estate of Chiurazzi*, __ A.D.2d __, 744 N.Y.S.2d 507 (2d Dep't 2002).

STANDING TO CONTEST

Two years before his death, testator executed a will leaving 70% of his estate to his home health aide and her husband, with the remaining 30% to the granddaughter of the attorney-draftsman. In the prior will executed seven years earlier, the estate was left to several charitable beneficiaries with B, his then attorney, named as executor. About five months after the second will was admitted to probate, B sought to reopen probate and contest the admitted will. The motion was granted and separate objections based upon lack of testamentary capacity, fraud and undue influence were filed by B, one charitable beneficiary and the attorney general. Thereafter, the charity and the attorney general entered into a settlement agreement with the existing personal representative from which B was excluded. Since the attorney general and the charity had appeared in the matter, the court concluded that the need for B's participation had ended. The Appellate Division agreed that the parties had adequate representation and that the negotiated settlement was proper despite B's opposition. However, the award of counsel fees to B from the estate was not error. The court found that B had unselfishly and effectively pursued his duty to carry

out decedent's intent as expressed in the will naming him as executor. *In re Estate of Baldwin*, __A.D.2d__, 745 N.Y.S.2d 265 (3d Dep't 2002).

JURISDICTION—CONTRACT NOT TO REVOKE WILL

Where beneficiaries brought action in Supreme Court against decedent's spouse alleging the violation of a reciprocal will agreement, the case was properly removed to Surrogate's Court. Although Supreme Court is the appropriate court in which to seek enforcement of a contract, this agreement is so intertwined with a pending will contest that the result would affect administration of the estate. The matter is within the general jurisdiction of the Surrogate and there is a preference for the resolution of estate matters in that court. Apparently, the contract provided that neither spouse would revoke or amend reciprocal wills without the consent of the other. *Hoffman v. Sitkoff*, __ A.D.2d__ , 745 N.Y.S.2d 539 (1st Dep't 2002).

DESCENT AND DISTRIBUTION

PROOF OF PATERNITY

An alleged non-marital child was not successful in his claim for an intestate share of decedent's estate. Letters of administration issued to decedent's sister were not revoked. The sister had failed in her opposition to claimant's request to have DNA testing done on blood samples retained by the medical examiner after conducting an autopsy. When the testing showed a 0% probability of paternity, the opposing parties switched their positions. The court found that posthumous DNA testing was admissible as "clear and convincing evidence" on the issue of paternity. The statutory subdivision relating to genetic marker tests administered to the father was not applicable. Since the blood samples had been retained, no issue of exhumation was present. Since there was no issue of fact, there was no need for a hearing. *In re Estate of Bonanno*, 192 Misc. 2d 86, 745 N.Y.S.2d 813 (Sur. Ct., N.Y. Co. 2002).

ADMINISTRATION OF ESTATES

STANDING OF PUBLIC ADMINISTRATION

An elderly, childless widow died testate leaving a substantial estate. Since her distributees included unknown first cousins, the Public Administrator was appointed to act on their behalf. Objections to probate of her last will were filed by the Public Administrator and by beneficiaries under earlier wills whose legacies were allegedly superseded. M, the principal beneficiary under the latest will, sought to have objections by the Public Administrator stricken on the ground that the class of first cousins had been fully identified so that the Public Administrator lacked standing. The Appellate Division found that SCPA 1123 made the Public Administrator a necessary party to a probate proceeding when decedent was survived by no one less remote than first cousins even when all distributees are identified. If the challenges of fraud and undue influence are successful as to M, the residuary beneficiary, and the will is admitted to probate, a large portion of the estate will pass through intestacy. *In re Estate of von Knapitsch*, ___A.D.2d__, 746 N.Y.S.2d 694 (1st Dep't 2002).

LEGAL FEES AND DISBURSEMENTS

In an accounting proceeding relating to requests for fees and disbursements by six of seventeen law firms claiming to have rendered services on behalf of the estate, the Appellate Division increased the fees awarded by the Surrogate by amounts as follows: firm A, $500,000; firm B, $100,000; firm C, $600,000; firm D, $150,000; and firm E, $20,000. The court indicated that it had familiarity with the services performed by the firms and that application of the usual criteria by the Surrogate produced some inadequacy. A settlement agreement made by firm A, the attorney general and the sole residuary charitable beneficiary was not binding on the Surrogate. A review of the reasonableness of the components was appropriate. Criminal defense services provided to an attesting witness to the probated will resulted in no benefit to the estate and no obligation to make payment. The Surrogate correctly awarded interest on the overpayments made to the firms and refunded to the residuary beneficiary. The firms had received and enjoyed the use of the money with the understanding that all or a portion of the fees were subject to the possibility of return. *In re Lafferty*, __ A.D.2d__ , 746 N.Y.S.2d 709 (1st Dep't 2002).

VALIDITY OF INDEMNIFICATION AGREEMENT

Decedent's estate claimed that A abused his personal relationship with decedent by taking advantage of decedent's diminished mental capacity to cause a sale of certain business interests by decedent to A for a small fraction of market value. Thereafter, A brought a declaratory judgment action against the preliminary executor of decedent's estate, in her individual capacity, seeking indemnification for expenses incurred in defending suit by the estate against A. The Appellate Division found that the indemnification agreement was not enforceable. The personal representative was not a party to it. Her actions of enforcement against A were properly undertaken in the performance of her duties as an officer of the court. Personal liability for misconduct does not occur when the personal representative is legitimate-

ly attempting to recover estate assets. *Skolnick v. Goldberg*, __A.D.2d__, 746 N.Y.S.2d 296 (1st Dep't 2002).

STANDING TO BRING HOLDOVER PROCEEDING

The personal representatives of the estate of a Florida domiciliary, appointed in Florida, began a holdover proceeding in New York to recover possession of a New York cooperative apartment. Since no ancillary letters had been issued to the petitioners by a New York court, they were not duly authorized to act in New York and the estate itself was not a legal entity. *Estate of Hershkowitz v. Walker*, __A.D.2d__, 746 N.Y.S.2d 228 (2d Dep't 2002).

TRUSTS

INVESTMENT RESPONSIBILITY

A remainderman of an *inter vivos* trust brought suit against a New York trustee for breach of fiduciary obligation and an accounting because of a failure to diversify the trust portfolio over a period in excess of 30 years. Twelve years after the trust was created to pay the income to a citizen of Brazil for her life, the trustee liquidated the stock holdings of the trust and invested the proceeds in cash and tax-exempt bonds. This action was taken to avoid adverse tax consequences that would arise as a result of a possible ratification of a bilateral income tax treaty by Brazil and the United States. The income beneficiary agreed to the sale but the two remaindermen, descendants of the income beneficiary, were not consulted. The treaty was never ratified and after several years it became apparent that ratification was not expected. The trust corpus was continued in cash and tax-exempt bonds. In the trustee's motion for summary judgment, it asserted that damages should be calculated on lost-capital only, $3,114 measured over a period of 27 years. The remainderman alleged damages of $20 million based on a hypothetical reinvestment and use of the S&P 500 Index over 26 years. The federal district court found that loss of income or appreciation damages were not available to the remainderman because the alleged misconduct did not consist of deliberate self-dealing and faithless transfers. Such damages are not applicable for breach of the prudent investor standard of care according to state law precedent. Although Restatement (Third) of Trusts § 211 may be to the contrary, it has not been adopted as the law of New York. *Williams v. J. P. Morgan & Co.*, 199 F. Supp. 2d 189 (S.D.N.Y. 2002).

OBJECTIONS TO TRUST ACCOUNTING

Prior to their divorce, H and W created various trusts which were thereafter consolidated. When the trustees sued W to recover the amount of an unpaid debt, the issues were settled by stipulation which required the trustees to provide a complete accounting. In the various objections to this accounting that were presented by W, she asserted that the details of a $200,000 loan from the trust to H were incomplete and inaccurate. The trustees had treated the payment as a distribution of principal and no repayment was sought. Objections with respect to an insurance holding trust and a title holding trust were also properly interposed. The lower court improperly dismissed the objections and the issues were remitted for a hearing. *Silkwood v. Butler*, __ A.D.2d __, 747 N.Y.S.2d 109 (2d Dep't 2002).

UNITRUST CONVERSION

Testator's widow, who was the income beneficiary of a testamentary trust created by him, sought to have the trust converted to a unitrust pursuant to the optional provisions of EPTL 11-2.4(e)(2) which took effect in 2002. Although no opposition to the conversion was put forth and a presumption existed as to the applicability of the option, the final decision was in the discretion of the court. Affidavits in support of the petition stated that the widow was the principal object of testator's bounty and that none of the 14 remainderman were in need. Through the conversion, the future payout to the life income beneficiary would be raised to 4% of the trust principal from the existing 2%-3% return. Since the trust principal consisted entirely of marketable securities, no problems of sale would exist. The petition was granted retroactive to January 1, 2002, the effective date of the statute. The adjustment of the base using the values currently and of the two prior business years should begin in 2004. Although the trust preceded the enactment of this valuation "smoothing rule," it would be unfair to apply new payout rules to investments made on standards that were not in effect when the investment was made. *In re Estate of Ives*, __ Misc. 2d __, 745 N.Y.S.2d 904 (Sur. Ct., Broome Co. 2002).

CONSTRUCTION

At decedent's death in 1944, his will created two trusts, one with his son, L, as life income beneficiary, and the other with his daughter, M, as life income beneficiary. M was named as the secondary income beneficiary of the trust for the benefit of L and upon M's death, principal was to go to her issue per stirpes. When M died in 1998 having survived both of her children, her grandson, Rex, became entitled to the entire fund set aside for L. Roy, the brother of Rex, who would have shared with him if living, died in 1990 and was survived by one infant adopted daughter who was again adopted in 1995 by the new husband of Roy's widow. The court found that the 1995 adoption completely removed the child to the

new family so as to bar her from taking as issue of M.

Upon the death of M, the principal of her trust was to be divided into two shares, with each of M's two named children, A and D, to receive the income from one share until he or she reached age 30, when principal was to be paid to the child attaining that age. The court found that A and D had vested interests that passed to their estates since the will had no language conditioning their taking upon survivorship of M. Both A and D attained age 30 prior to death. Since A and D were residents of California at the times of their deaths, disposition of the trusts' principal was to be determined by California courts. *In re Cruikshank*, __ Misc. 2d__, 746 N.Y.S.2d 769 (Sur. Ct., Kings Co. 2002).

JURISDICTION—VALIDITY—CONSTRUCTION

The successor trustee of several *inter vivos* trusts questioned the validity of the exercises of powers of appointment over the corpus of the trusts. The MG2 trust had been in existence for 30 years and the successor trustee who had served for the past 14 years had no right to deny the validity of the trust. The trust instrument created a limited power of appointment in the beneficiary-child of the grantor exercisable upon attaining age 25. The court found that there was no ambiguity in naming the donee of the power even though age 25 had been reached when the trust was created. An argument that parol evidence should be admitted to show that the grantor intended her granddaughter to hold the power necessarily failed. A possible violation of the rule against perpetuities remained unresolved. A challenge to the right of the court to exercise jurisdiction over the RSX Trust also failed. Although the trust agreement recited that it was established to be construed and administered under the laws of the Bahama Islands, the trust had been administered in New York since 1985. The trustee and all but one interested party resided in New York and the corpus was physically located in New York. Additionally, the court found substantial compliance with a provision allowing removal of the trust from the jurisdiction of the Bahama Islands. A possible violation of the rule against perpetuities in this trust was also unresolved. All of the parties had conducted themselves as though the RSX Trust was valid. *In re Marcus Trust*, 191 Misc. 2d 497, 742 N.Y.S.2d 777 (Sur. Ct., Nassau Co. 2002).

VALIDITY OF POUROVER TRUST

As part of his estate plan, decedent had created a revocable *inter vivos* trust which was to pay him the income for life with principal to be paid upon his death to his niece, N, except for $200 to be paid to his other niece, O. On the same day, decedent executed a will which gave his estate to the trust or, if the trust were not valid, to the beneficiaries named in the trust. After decedent's death, O filed the usual objections to probate together with numerous objections to the validity of the trust. At the execution ceremony for both instruments, decedent was given $10 by his attorney to initially fund the trust. No other assets were ever transferred to the trust. The ceremony occurred in 1997 shortly before the effective date of the imposition of formal requirements to create a trust. The court found that retaining the trust provisions in a looseleaf binder did not affect its validity. It appeared to be complete and accurate in a version that matched a stapled duplicate original. Arguments that the trust was invalidated by the merger doctrine or was illusory or that the trustee was passive had no merit. The trust agreement provided for a second trustee with significant duties who would serve with the settlor. Despite a provision that the trust terminated upon the death of the settlor, it continued in existence to collect estate assets passing under the will to the trust. Issues concerning the validity of the acknowledgment in the trust instrument were not reached since the sufficiency of the defects raised questions of fact. O's motion for summary judgment to declare the trust invalid was denied. *In re Estate of Klosinski*, __ Misc. 2d__, 746 N.Y.S.2d 350 (Sur. Ct., Kings Co. 2002).

MISCELLANEOUS

INVALID GIFT—NO DELIVERY

Plaintiff brought action, individually and as executrix of her mother's estate, against her brother to recover the proceeds of two certificates of deposit transferred by the brother from decedent's name to his own name, pursuant to a power of attorney, three days before her death. One month later, the brother transferred the funds to his daughters, allegedly in keeping with decedent's desire to make gifts to them. The court found that no gifts had been made because no valid delivery occurred during decedent's lifetime. Such a delivery could have been made easily. *Bentley v. Dox*, 295 A.D.2d 952, 744 N.Y.S.2d 598 (4th Dep't 2002).

DECLARATION OF DEATH OF ABSENTEE

Under EPTL 2-1.7, a person who has been absent for less than three years may be declared dead when facts show the person was exposed to a specific peril of death even though the body has not been recovered. On September 11, 2001, a commuter took the train from Dutchess County, New York, en route to

his job in lower Manhattan and was never heard from again. Proof showed a stable family life, including a marriage of 37 years, with no reason to disappear intentionally. His subway card was used 42 minutes before the highjacked airliner crashed into World Trade Center, Tower No. 1. His lifetime employment involved working with computers. In his existing job, he had no precise arrival obligation and was merely charged with completing the required work in such time as was needed. A trade show was being held that day on floor 106 of Tower No. 1 by a company with which the absentee had conducted business. The absentee never arrived at work again. Except for the clothing worn that day, none of his personal items was missing. His car was found parked at the train station. His credit card was not used thereafter. Neither of the absentee's two medical advisers had heard from the absentee. The Surrogate found sufficient proof to declare the absentee dead on the date of the disappearance and to allow his executrix to offer his will for probate. *In re Lafuente*, 191 Misc. 2d 577, 743 N.Y.S.2d 678 (Sur. Ct., Dutchess Co. 2002).

JOINT BANK ACCOUNT

An elderly woman died leaving a bank account with a balance of $151,486 held in the names of decedent and N, her great nephew, who was not a beneficiary of her very substantial estate. The beginning deposit to the account, $240,000, was entirely supplied by decedent. All of the withdrawals from the account were made and used by N. Decedent reported all of the interest paid on her income tax return. The bank treated the account as one held jointly with the right of survivorship. The original signature card including the joint account agreement could not be found by the bank. The court found that, although survivorship language on the signature card is the most effective way to trigger the statutory presumption of joint tenancy, it is not the exclusive way. It arises in any case where the deposit is made to two parties or to the survivor. In addition, a common law joint tenancy may be created upon sufficient proof without benefit of the statutory presumption. N was entitled to the balance on deposit and was not prejudiced because the bank had lost the signature card. *In re Estate of Butta*, __Misc. 2d__, 746 N.Y.S.2d 586 (Sur. Ct., Bronx Co. 2002).

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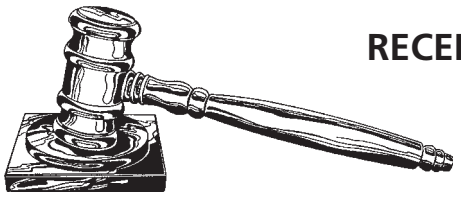

CASE NOTES— RECENT NEW YORK STATE SURROGATE'S AND SUPREME COURT DECISIONS

Ilene Sherwyn Cooper and Donald S. Klein

Constructive Trusts

In a contested proceeding to determine the validity of a claim, the executrix of the estate moved for summary judgment seeking a dismissal of the claimant's objections. In opposition to the motion, the claimant asserted a defense based upon the theory of constructive trust.

The genesis of the claim at issue—title to the decedent's home in Islip Terrace—was a payment in the sum of $50,000 made by the respondent toward purchase of the premises with the decedent. Respondent maintained that she and the decedent lived together for approximately 19 years prior to his death, and that she gave this money to him in reliance upon his promise to transfer title to the residence into both of their names. At the time of the decedent's death, title remained in the decedent's name alone.

The executor of the estate, supported by the guardian ad litem appointed to represent the grandchildren of the decedent, sought dismissal of the claim on the grounds that it was unsupported by documentary evidence or the testimony of independent witnesses. Significantly, the respondent acknowledged at her deposition that there was no writing of any kind documenting the alleged promise to transfer the deed and that no one was present when the promise was allegedly made. Moreover, none of the closing documents in connection with the purchase of the premises made any reference to the respondent nor was respondent able to produce any evidence of the transfer of funds from her to the decedent.

After examining the criteria for imposition of a constructive trust, the court found that the major obstacle to respondent's claim was the fact that she was the primary witness to the event in support of her contentions. Although this testimony could be considered for purposes of defeating a motion for summary judgment, at trial it could be excluded pursuant to the provisions of CPLR 4519. This being the case, the court concluded that a trial of the issues raised by the motion would be unnecessary and dismissed the respondent's claim. *In re Estate of Chester Kacprzyk, a/k/a Chester Thomas Kacpryzk*, N.Y.L.J., July 19, 2002, p. 23 (Sur. Court, Suffolk Co., Surr. Czygier)

Gift

In a contested discovery proceeding, the executor of the decedent's estate sought recovery of a two-door sedan from the respondent, the decedent's nephew. The sedan was owned by the decedent at death. The respondent claimed that the automobile was a gift. Further, respondent claimed that in the event a gift was not found, the court reimburse him for sums expended to improve the vehicle.

Based upon the testimony adduced at trial, the court found that respondent failed to prove a gift of the auto in issue. The court concluded that any intention articulated by the decedent to effectuate a transfer was ambiguous at best. Conversations offered to substantiate the decedent's intent were instead consistent with a conditional gift, particularly when coupled with the fact that the decedent retained ownership in his name. Indeed, the decedent retained the registration of the car amongst her personal papers, and the respondent made no attempt to re-register the vehicle until after the decedent's death.

Nevertheless, despite its determination that a gift of the auto had not been made, the court awarded respondent the sum of $6,466.05 for sums expended on repairs and improvements to the car while in respondent's possession. *In re Estate of Madeline Smith, a/k/a Madeline L. Smith*, N.Y.L.J., July 30, 2002, p. 21 (Sur. Court, Suffolk Co., Surr. Czygier)

Jurisdiction

At issue was whether the court had subject matter jurisdiction over a proceeding brought pursuant to Article 10 of the Debtor and Creditor Law. Subsequent to the decedent's death, it was determined that a survivorship account between the decedent and his daughter was a testamentary substitute subject to the elective share of his surviving spouse. Thereafter, incident to an accounting proceeding in the estate, it was stipulated that the surviving spouse would be

able to enforce her claim against the decedent's daughter as a judgment creditor upon docketing the accounting decree with the county clerk. When the decedent's spouse went to enforce the decree, she learned that several years prior to its entry, the decedent's daughter transferred a portion of the proceeds to which she was entitled to her brother and sister-in-law. The decedent's spouse sought to set aside these transfers as a fraudulent conveyance.

The court denied respondents' motion to dismiss the proceeding holding that it had jurisdiction to set aside as fraudulent a transfer allegedly made to defeat a spouse's right of election. *See Matter of Vivien King*, 243 A.D.2d 478. *In re Estate of Benjamin Abramson*, N.Y.L.J., July 8, 2002, p. 23 (Sur. Court, Kings Co., Surr. Feinberg)

Preliminary Letters Testamentary

In a contested probate proceeding, the court granted the petitioner's application for preliminary letters testamentary, over the objections of the contestants, finding that the assertions were nothing more than conclusory allegations. Further, the court held that the need for a preliminary executrix was apparent and outweighed the concerns of the contestants, since the power and authority of the preliminary fiduciary would not extend beyond that which was necessary to preserve and protect the estate assets. Accordingly, preliminary letters were issued to the petitioner, upon her posting of a bond in the sum of $215,000, and subject to the restriction that she not reimburse herself or her husband for any monies allegedly due them from the estate. *In re Estate of Ellen Piterniak*, N.Y.L.J., September 20, 2002, p. 23, (Sur. Court, Suffolk Co., Surr. Czygier)

Probate—Due Execution

In a contested probate proceeding, the petitioner moved for summary judgment dismissing the objections to probate. The court granted petitioner's motion with respect to the issues of lack of testamentary capacity, fraud and undue influence, but denied the motion with respect to the issue of due execution. The court found that despite an attestation clause, an issue of fact regarding due execution was created when witnesses could not recall whether the decedent published the will. The court rejected prior cases, which held that an attestation clause created a presumption of undue influence, to find that an attestation clause was merely evidence of due execution. *In re Estate of Joseph Krugman*, N.Y.L.J., August 19, 2002, p. 30 (Sur. Court, Kings Co., Surr. Feinberg)

Probate—Issues for Trial

In a contested probate proceeding, the court held that the issue of intent was not an issue to be separately tried and determined, but instead could be raised in a separate proceeding for the construction of the decedent's will subsequent to its probate. The court based the decision upon an opinion rendered by the court in *In re Strausman*, N.Y.L.J., Sept. 25, 1996, p. 26 (Sur. Court, Suffolk Co.), wherein it was held that "[t]he question of the decedent's intent was clearly subsumed within the issue of testamentary capacity. . . ." *In re Estate of Robert S. Houston, a/k/a/Robert Houston*, N.Y.L.J., September 23, 2002, p.29 (Sur. Court, Suffolk Co., Surr. Czygier)

Right of Election

In a contested proceeding to determine the validity of a right of election, the respondent moved for partial summary judgment dismissing so much of the petition which alleged waiver of the right of election, equitable estoppel and breach of contract. The executor cross-moved for an order striking certain affirmative defenses based upon the issue of whether the right of election was waived. Both motions were denied, and a hearing was directed.

In support of her motion to dismiss, the respondent argued that the Separation Agreement executed by herself and the decedent in November 1999, which contained the purported waiver of her elective share, was invalid as a matter of law, due to defective acknowledgments at the foot of the Agreement. The court found that while the certificate of acknowledgment contained all the requisite language that was required prior to the effective change in the law as of September, 1, 1999, it did not contain all the pertinent information required in the revised standard certificate of acknowledgment, namely, (i) whether the parties produced "satisfactory evidence" concerning their identities, and (ii) in what capacity each party executed the Agreement.

Assuming that an acknowledgment which is defective on its face can be cured after the fact, the court found summary judgment as to the Agreement's validity was inappropriate, and directed that a hearing be conducted to determine whether the parties, in executing their respective acknowledgments to the Agreement, conformed substantially with the formal requirements pertaining to the revised form certificate of acknowledgment. *In re Estate of Wolf B. Fleiss*, N.Y.L.J., July 24, 2002, p. 23 (Sur. Court, Westchester Co., Surr. Scarpino)

Renunciation

Application was made by the decedent's surviving spouse and son to file late renunciations of their respective interests in the proceeds of a wrongful death suit. In support of the application, petitioners stated that they wanted to preserve their eligibility for public assistance benefits.

The court denied the application, finding that aside from being delayed, the renunciations would be ineffective to preserve the petitioners' entitlement to public assistance benefits. Recipients of public assistance may not maintain eligibility for benefits while failing to avail themselves of all available resources. *See* Social Services Law § 366; 18 N.Y.C.R.R. § 360-2.3[c]. *In re Estate of Ramon Machado*, N.Y.L.J., July 15, 2002, p. 28 (Sur. Court, Westchester Co., Surr. Scarpino)

Sanctions

In a proceeding seeking a distribution of the estate pursuant to an agreement among the parties, an award of attorney's fees, or alternatively, removal, the court granted petitioners' request for fees, finding the respondent fiduciary's conduct to be frivolous within the meaning of 22 N.Y.C.R.R. § 130-1.1(c)(2). The court found that the fiduciary's actions in advance of the proceeding were designed to cause frustration and expense to the beneficiaries, and that such actions were sufficient to impose sanctions. *In re Estate of Mary C. Tupper,* N.Y.L.J., September 3, 2002, p. 25 (Sur. Court, Suffolk Co., Surr. Czygier).

Summary Judgment—Probate Proceeding

In a contested probate proceeding, the petitioner moved for summary judgment dismissing the objections filed by the decedent's sole distributee, who was disinherited under the propounded instrument. The objections raised issues respecting due execution, testamentary capacity, fraud, undue influence, and mistake.

With respect to the issue of mistake, the court found that no triable issue of fact existed and granted petitioner's motion. In order to support a claim of mistake, the objectant must establish either that decedent did not understand the provisions of the will, or that the attorney-draftsman erred in interpreting decedent's instructions. *See Christian v. Roesch*, 132 A.D. 22, *aff'd,* 198 N.Y. 538 (1910). The record indicated that on the date of execution, the attorney/draftsman read the entire instrument aloud to decedent in the presence of the two other attesting witnesses, whereupon the decedent either affirmatively confirmed the content of each provision or questioned the attorney/draftsman with respect to the import and received answers to her satisfaction before executing the document. The objectant failed to present any evidence to the contrary, and the objection on the grounds of mistake was dismissed.

As to the remaining objections, however, the court found that triable issues of fact existed and denied petitioner's motion. *In re Estate of Mildred Lipsig*, N.Y.L.J., August 13, 2002, p. 27 (Sur. Court, Westchester Co., Surr. Scarpino)

Summary Judgment—Validity of Trust

Before the court was an application brought by the decedent's spouse and his daughter to declare the insurance trust, of which the daughter was a named trustee, void *ab initio*.

The trust agreement was apparently signed by the decedent and his daughter as trustee, before a notary, on November 1, 1996. On the same day, the decedent executed a Request of Change of Beneficiary Form, naming the 1996 trust as beneficiary and his daughter as trustee of a life insurance policy. On December 19, 2000, the decedent's daughter resigned as trustee. Subsequently, the successor trustee named in the trust agreed to serve.

In support of the application to declare the trust invalid, the decedent's daughter claimed that she never agreed to act as trustee, and that her signature and that of the notary were forgeries. The notary submitted an affidavit stating that she never notarized the document. As such, movants claimed that the trust was void because there was never a trustee when it was created.

The successor trustee opposed the application and moved for summary judgment declaring the trust valid, and her, as trustee.

The court granted the motion, holding that a devise in trust, which is valid in other respects, will not fail for want of a trustee. A valid trust is created notwithstanding the failure of the trustee to accept the designation or even know of it. Hence, inasmuch as the life insurance trust was executed in conformity with law, a valid trust was created, despite the alleged lack of consent by the named trustee to serve. *In re Estate of Laurence J. Gold*, N.Y.L.J., August 16, 2002, p. 20 (Sur. Court, Kings Co., Surr. Feinberg)

Totten Trust Accounts

In a discovery proceeding, the question presented was whether a trust account could be created without a document signed by the depositor which designates the beneficiary.

The record revealed that the decedent established an account in his own name at a banking institution. The respondent claimed that her name was added to the account. A printout of the bank's computer records listed the respondent as beneficiary on the account; however, there was no signature card or other document signed by the decedent to this effect on file. The testimony of a bank employee at her deposition was that it was not the bank's policy to require a signature card when an individual account was converted to a trust account.

The court referred to the provisions of EPTL 7-5.1 for the law governing trust accounts, finding that it required that these accounts were established "by a depositor describing himself as trustee for another." Nevertheless, the court determined that the statute left the common law standard for establishing a trust account intact. This standard authorized a trust account of personal property to be established by an oral declaration, so long as the expression of intent was unequivocal.

This being the case, the court determined that a question of fact existed as to whether the decedent's directions to the bank satisfied the requirements for the creation of a totten trust. The court found that none of the bank's records were conclusive on the issue and that the estate was entitled to test the credibility and accuracy of the bank employee who generated the computer record listing the respondent as a beneficiary of the account. *In re Estate of William R. Posch*, N.Y.L.J., August 12, 2002, p. 26 (Sur. Court, Nassau Co., Surr. Riordan)

Totten Trust Accounts—Revocation

In a contested accounting proceeding, the respondent moved for summary judgment regarding the revocation of a certain totten trust account established at Chase Manhattan.

In April 1991, the decedent opened a savings account in her own name at Chase Manhattan Bank. The account opening document stated that it belonged to the decedent "subject to a tentative trust in favor of the named beneficiaries," Michael and Peter. Several years later, after being diagnosed with cancer, the decedent returned to Chase, and she and Michael executed a title change and signature card, which read "individual to joint." At the top of the card were the words: "add ITF back on." The form and the signature card were signed by the decedent and Michael, and for the type of account arrangement, the joint box was checked.

On the death of the decedent, Michael withdrew the balance of the account.

Within the context of the accounting, Peter moved for summary judgment, arguing that the totten trust established by the decedent was not revoked or modified in accordance with Article 7 of the EPTL. In response, Michael argued that the EPTL should not be applied to frustrate the decedent's intent to gift him the money; that the new account created was a joint account with the right of survivorship; and that the "in trust for" language was added by the Chase bank officer solely for the purpose of increasing the FDIC coverage on the account.

The court held that the purpose of EPTL 7-5.2(1) was to establish exclusive standards in the law of totten trusts, and to remove the subjective issue of the depositor's intent in determining a revocation or modification. The provisions of the statute are strictly construed. Therefore, attempts to revoke bank accounts in trust without literal compliance with the statutory provisions have been deemed ineffective. In the absence of a valid revocation, the original beneficiaries retain their status.

In view of the foregoing, the court held that the decedent had failed to revoke her totten trust account at Chase in compliance with the provisions of EPTL 7-5.2(1), and granted Peter's motion for summary judgment. *In re Estate of Dorothy Fyler, a/k/a Dorothy C. Fyler*, N.Y.L.J., August 20, 2002, p. 22 (Sur. Court, Westchester Co., Surr. Scarpino)

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Unless stated to the contrary, all published articles represent the viewpoint of the author and should not be regarded as representing the views of the Editor or the Trusts and Estates Law Section or substantive approval of the contents therein.

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