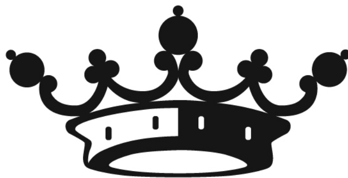
INSIDE THE MINDS

Strategies for Trusts and Estates in New York

Leading Lawyers on Protecting Clients' Assets, Determining the Best Estate Planning Strategy, and Adapting to New Laws and Trends



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First Printing, 2010
10 9 8 7 6 5 4 3 2 1

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New Options and Trends to Consider in New York Estate Planning

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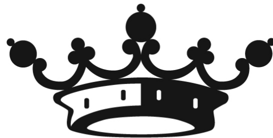

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Introduction: Current Topics and Concerns

Key Concerns of Clients Regarding Surviving Family Members and Beneficiaries

- To maximize the funds available for surviving family members by reducing the amount of taxes paid on an estate
- To continue the lifestyle to which the surviving family members are accustomed
- To ensure that the younger generation is provided for while at the same time not depriving them of a motivation to work
- To provide funds for grandchildren to attend college
- To provide liquidity to pay any estate tax that may be due
- To provide for a minor in case both his or her parents die
- To provide for the continuation of a closely held business
- To ensure that the benefits of a trust outweigh the costs of the trust's administration
- To protect funds from a beneficiary's potential creditors
- To ensure that trust funds do not jeopardize government benefits a beneficiary may be receiving or for which a beneficiary may be eligible in the future

The Most Common/Popular Types of Trusts

- Testamentary trusts, including those for the surviving spouse, such as disclaimer trusts (a trust created through a beneficiary's post-mortem disclaimer of an amount up to the "exemption amount," the amount that can pass free of estate tax), mandated trusts created to hold the exemption amount and/or over which the executor may make a total or partial qualified terminable interest property election (to qualify all or part of the trust for the marital deduction), as well as trusts created for descendants
- Revocable trusts, to benefit the grantor during his or her lifetime, and most often to continue in trust for a surviving spouse and/or descendants
- Irrevocable intentionally defective grantor trusts, which are used for a variety of estate planning techniques, including grantor-

retained annuity trusts, qualified personal residence trusts, life insurance trusts, asset protection trusts, and dynasty trusts
- Supplemental needs trusts, created to benefit a disabled person while not jeopardizing government benefits to which the person may be entitled

Most Frequently Recommended Trusts and the Benefits Offered by Each

- *Disclaimer trusts:* These are established through post-mortem disclaimers by a surviving spouse, and they allow for post-mortem estate planning. They are used to minimize taxes through both spouses' estates, and are used by married couples who trust each other's judgment. These trusts provide great flexibility to an estate plan, but should only be used where creditor concerns are not an issue.
- *Mandated testamentary trusts:* These types of testamentary trusts allow the decedent to provide asset protection and financial management for the surviving spouse and/or other beneficiaries, while also being able to dictate the remainder beneficiaries of such trusts.
- *Revocable trusts:* The use of revocable trusts in lieu of wills is worth the additional up-front costs for many clients, especially those who want to simplify and organize their matters for the surviving spouse and other heirs, those who want a mechanism in place to manage their affairs if they become incapacitated, those who want privacy of their affairs, and those who want to avoid the delay and costs of probate.
- *Dynasty trusts:* These are for those clients with greater wealth (usually above $10 million) who may have closely held business interests with which they wish to benefit future generations, or charitable endeavors, and who wish to generate the least amount of estate taxes in the current and future generations. A sale of a business interest to a dynasty trust established as a grantor trust will allow the grantor to sell an appreciating asset, usually at a discount due to lack of marketability or lack of control, and thereby freeze the value of the asset in his or her estate and transfer the future appreciation out of his or her estate. The fact that the dynasty trust is a grantor trust allows the trust to be treated as the alter ego of the grantor for income tax purposes, and thereby allows the sale

and subsequent payments of interest to the grantor to be non-taxable events. By using a dynasty trust, the assets transferred to the trust, and the future appreciation thereon, will be available for future generations without the concern of estate or generation-skipping transfer taxes (assuming the right planning is in place—that is, if there are any gifts to the trust, as discussed later in this chapter, an allocation of generation-skipping transfer tax exemption will have to be made to the trust). In addition, the grantor may continue to have access to income from the asset in a number of ways, including: (i) interest payments under the note, (ii) discretionary distributions to the grantor (who may be a discretionary beneficiary without causing estate tax inclusion) and/or the grantor's spouse, and (iii) if the grantor continues to work for the business, compensation payments.

- *Medicaid protection trusts:* These allow asset protection trusts to be created for the middle class. These are used most frequently for clients who are unable, for medical or financial reasons, to obtain long-term care insurance, and who are concerned about the cost of long-term care or who wish to protect some portion of their assets to pass on to their children.
- *Supplemental needs trusts:* These trusts are imperative for families with a disabled family member, one who is already receiving or is likely to be eligible to receive government benefits in the future. A third-party supplemental needs trust allows family members to provide funds for the benefit of a disabled person without jeopardizing that person's government benefits. A self-settled supplemental needs trust allows an individual to (i) transfer their own funds (perhaps an inheritance received outright before adequate planning) to a trust for his or her benefit, (ii) remain or become eligible to receive government benefits, and then (iii) "pay back" such benefits after his or her death (before having any remaining assets pass to his or her heirs).

Trends in Estate Planning Practices and the Laws Affecting Them

- *The creation of fewer life insurance trusts:* As the federal estate tax exemption grows, fewer clients are concerned about liquidity to pay estate taxes.

- *Less mandated testamentary trusts to manage funds for the surviving spouse:* With the federal exemption amount having increased to $3.5 million per individual, there is less of a need to shelter assets from the surviving spouse's estate. And with many families having two spouses who work outside the home, and who are more educated regarding financial matters, there is less of a need to have trusts solely for financial management purposes.
- *Increased creation of grantor-retained annuity trusts, sales to intentionally defective grantor trusts, charitable lead trusts, and intra-family loans:* With many assets having depressed values, interest rates at record lows, and Congress reviewing discounting techniques that may decrease clients' ability to take discounts of family-owned businesses and use short-term grantor-retained annuity trusts.
- *Use of Medicaid-qualified trusts:* With health care costs and long-term care costs skyrocketing, and life expectancies continuing to grow, clients continue to be concerned about protecting assets, and Congress recently further limited allowable asset transfers under Medicaid.

Best Practices for Client Strategies

Motives

Motives for clients to establish a trust include:

- Estate tax and generation-skipping transfer tax avoidance
- Asset protection for the client
- Asset protection for the beneficiaries:
    - From creditors of the beneficiaries, including a spouse in a divorce action
    - From profligate beneficiaries who would otherwise be spendthrifts
- For use with estate freezing techniques, such as grantor-retained annuity trusts or sales to intentionally defective grantor trusts (These topics are discussed in greater detail both earlier and later in the chapter.)
- For property management purposes

- To hold insurance on the life of the grantor that is excluded from the grantor's estate, but that provides liquidity to the grantor's heirs
- For disabled beneficiaries, who are receiving or in the future are likely to receive government benefits (This class of beneficiaries is very broad, and spans to include people with mental and emotional disabilities such as autism and manic depression, those with degenerative diseases such as multiple sclerosis, and those with physical disabilities.)

Different motivations result in different types of plans. All my trusts are customized to the client's particular needs. Most of the new trusts I am creating are for the lives of the grantor and the grantor's spouse. Some of the trusts are generation-skipping trusts that do not provide for all trust property to be distributed outright to surviving children. This mechanism allows all the descendants (children, grandchildren, and great-grandchildren) to benefit from the use of trust assets, but when the grandchildren or great-grandchildren eventually receive the remaining funds, it will be without the prior imposition of estate taxes at the deaths of the grantor's children (although there may be generation-skipping transfer taxes on distributions to the grandchildren and great-grandchildren for amounts that are not sheltered by the grantor's generation-skipping transfer tax exemption). Other trusts give withdrawal rights to the children when they reach specified ages, such as when they are twenty-five (one-third of the trust corpus), thirty (half of the remaining trust corpus) and thirty-five (the rest of the trust corpus) years of age, with the option given to the child to leave the property in trust for their lifetime. Some of the generation-skipping trusts are in jurisdictions, such as Alaska and Delaware, that have abolished the Rule Against Perpetuities. Others are New York trusts that will have terms up to, but no longer than, that allowed by the New York Rule Against Perpetuities.

The Rule Against Perpetuities invalidates certain future interests and is intended to prevent property owners from controlling the disposition of property for too long from the grave. The rule evolved in feudal England during the 1600s. It was intended to prevent people from tying up property from generation to generation, and to promote the productive use of property by simplifying ownership and removing unknown impediments to alienability.

New York codified the Rule Against Perpetuities in N.Y. EST. POWERS & TRUSTS LAW § 9-1.1 (West 2009). The rule has two parts. The first part, in N.Y. EST. POWERS & TRUSTS LAW § 9-1.1(a), governs restraints on the ability to convey real property. It provides that no interest in real property is valid if the instrument conveying the interest suspends the absolute power of alienation for longer than lives in being (which includes a child conceived before the creation of the conveyance but born thereafter) plus twenty-one years.

The second part, in N.Y. EST. POWERS & TRUSTS LAW § 9-1.1(b), governs remote vesting, and provides that no estate in property is valid unless it vests no later than twenty-one years after one or more lives in being at the creation of the estate and any period of gestation involved.

Trends and Resulting Changes in Motivations over the Last Five Years

- With the growing federal estate tax exemption, clients are less focused solely on saving taxes, and more focused on what will allow the surviving spouse and other beneficiaries to continue with their lifestyles, or what will allow the next generation to have access to funds in the most beneficial manner, taking into account special circumstances including the need to protect assets from creditors of the beneficiaries.
- Parents more frequently view their adult children as peers, and are less likely to be motivated by controlling the disposition of their assets beyond their children's generation than by ensuring that their planning is tax-efficient and flexible.
- As medical care and long-term care costs grow, more people recognize that disabled family members need to be eligible to receive government benefits, even while recognizing the importance of providing other funds to assist with such individuals' supplemental needs and lifestyles.
- With many marriages ending in divorce, blended family issues are more prevalent, and planning needs to take into account that the beneficiaries may not all have the same interests, and may not work well together after the client's death.

- Married couples today are more likely than in previous generations to not require trustees to manage the financial affairs of the surviving spouse, and are likely to appoint the surviving spouse as a sole trustee or a co-trustee of a trust created for his or her benefit, and as the agent to manage the client's financial affairs if he or she becomes incapacitated.
- Clients are looking for trusts and trustees to multi-task, which is to say that they want trusts to provide the basic protections outlined here, but also perhaps do more—for example, to put in place planning, such as business succession planning, and to convey philosophies and moral lessons, such as being philanthropic and not living extravagantly, that the client may not have accomplished or completed during their lifetime.

Preparation

When taking on a new trust and estate client, the most important aspect of the initial client interview is to secure the confidence of the client so that the client will feel comfortable discussing personal information, and will be comfortable relying on the lawyer's experience, advice, and counsel to develop his or her own personalized estate plan. While actual plan implementation for the client will often follow established patterns, each family is unique—and as important, each client *believes* his or her own situation is unique. The attorney's listening skills are very important at this stage. In addition, the attorney must be prepared to ask the right questions to elicit information vital to the design of the client's plan.

The questions that are asked help the lawyer determine whether the client is an appropriate candidate for use of a particular estate planning technique (e.g., a revocable trust), what assets will be involved in the technique (e.g., what needs to be transferred into the trust), and what beneficiary designations need to be changed.

It is important for the lawyer to review and consider the entire estate plan, and how each document relates to and depends upon other documents to carry out the client's plan. For example, every person who has a revocable trust also must have a will, to administer and distribute to the trust at death any assets that come into the probate estate (a so-called "pour-over will").

The will may never have to be probated. However, one must be mindful of the possibility that there will be probate assets, either due to the client's own acts or otherwise. Social Security payments, final paychecks and bonuses, deferred compensation payments, distributions from partnerships, and inheritances and lottery winnings received near the time of death are examples of assets that, even with proper planning, may likely become part of a decedent's probate estate.

When representing couples—whether they are married or unmarried (same-sex or opposite sex)—an initial step is to obtain the consent of the clients to represent them jointly. This involves disclosing to them the ethical considerations the attorney must follow, and that the attorney will be representing both of them as one client, collectively, and not individually.

The clients must be advised that matters one of them might discuss with the attorney may be disclosed to the other, and that the attorney is prohibited from agreeing with either of them to withhold information from the other. The lawyer should unequivocally state that the lawyer would not give legal advice to either of them or make any changes in any of their estate planning documents without their mutual knowledge and consent.

If a conflict of interest arises between the couple during the course of their planning, or if they have a difference of opinion, the lawyer may point out the pros and cons of their respective positions or differing opinions. However, ethical considerations prohibit the lawyer, as the attorney for both of them, from advocating one of their positions over the other. Furthermore, the lawyer cannot advocate one of their positions versus the other if there is a dispute at any time as to their respective property rights or interests, or as to other legal issues between them. If actual conflicts of interest do arise between them of such a nature that, in the lawyer's judgment, it is impossible to perform the lawyer's ethical obligations to both of them, the lawyer will need to withdraw as their joint lawyer, and may not represent either of them separately.

In New York, a written engagement letter consented to by the client is required for all engagements where the fee is expected to be more than $3,000. As a matter of good practice, engagement letters should be the norm, not the exception. The engagement letter should disclose the scope

of the lawyer's work; all ethical considerations, including those specific to joint representation (where appropriate); the fee arrangement, including how fees are determined, what disbursements will be billed, and the frequency of billing; each party's right to terminate the engagement; and the client's right to arbitrate any fee dispute pursuant to Part 137 of the Rules issued by Administrative Order of the Chief Administrative Judge, *available at* http://www.courts.state.ny.us/rules/chiefadmin/137.shtml.

The attorney should send an estate planning questionnaire to the client to review and hopefully complete prior to the first meeting. However, scheduling the first meeting should not be delayed if the client procrastinates in completing and returning the form.

I use several forms of questionnaire. There are two forms that elicit information on the client's assets, one that is used for clients with significant and diverse assets, and the other used for clients with simpler and more "typical" assets, such as one or two homes, cars, boats, investment accounts, bank accounts, and retirement accounts. The forms are periodically updated. The forms ask the clients to list the assets by ownership—individual ownership in the name of each spouse/partner, joint ownership, and ownership through revocable or irrevocable trusts.

In addition, there is a separate form that elicits personal and family information. I have found that the following information is extremely important for the client to have in a centralized, known location and for me to obtain where relevant to current planning:

- Names, phone numbers, physical addresses, e-mail addresses, birth dates, and Social Security numbers of spouses, children, grandchildren, siblings, and parents
- Employment history
- Contact information for the client's medical care providers, financial advisers, accountants, insurance agents, bankers, clergy, health insurance providers, and others
- Copies of current wills, trusts, living wills, health care proxies, and powers of attorney—or if copies are unavailable, the current physical location of the originals and the names of the executors, trustees, proxies, and agents named in the current documents

- Copies of beneficiary designations to insurance policies and retirement plans
- Copies of transfer on death designations to brokerage and other accounts
- Safe deposit box information, including the location of the keys and the names, addresses, and phone numbers of any deputies on the account
- Funeral or cremation arrangements and the existence of burial plots or mausoleum crypts
- Security information, including login names and passwords to computers and online accounts, and credit and debit card numbers and PINs
- Copies of prior filed gift tax returns
- Financial statements for the individual client and for the client's closely held businesses, and income tax returns when appropriate

Before the initial meeting, clients also should be asked to think about and provide information on the people they would like to act as their executors, trustees, health care agents, and agents under their powers of attorney, and guardians of their minor children, and who should be the successors to these named people.

I have found that obtaining information and client preferences on the following subjects is critical to a proper analysis of all issues in a client's estate plan:

- Prior marriages, together with copies of separation agreements and divorce decrees. This information is necessary for me to review beneficiary designations to the client's insurance policies and retirement plans, title to real estate and other property, and provisions of trusts created during the prior marriages, to ascertain if all transfers have been made and beneficiary designations updated to comply with the provisions of any such agreements and decrees, and to take into account changed circumstances since the separation or divorce. Since a divorce decree does not nullify a designation of a former spouse as a

beneficiary of a retirement account or an insurance policy, it is important to ensure that a client updates their beneficiary designations to match their current estate plan, while at the same time complying with any legal obligations under the divorce decree.

- Adopted children and grandchildren, and step-children and step-grandchildren, to determine how the client would like to treat these people in the estate plan
- Spouses of children and spouses of grandchildren, to determine how the client would like to treat these people in the estate plan
- Pre-nuptial and post-nuptial agreements with the current spouse, together with copies of the signed documents, to make sure the estate plan conforms with the provisions of these agreements
- Jurisdictions in which a married couple has previously resided, to determine the effect of community property law or foreign law on the ownership and disposition of their assets
- Citizenship of the clients and their heirs, to properly plan for tax law consequences and dispositive provisions impacted by citizenship
- Location of property in states other than New York or in foreign countries, to properly plan for estate, inheritance, and other tax ramifications, state and foreign law rules of inheritance and distribution, and to plan for, or to avoid, ancillary probate
- Agreements related to the ownership of interests in closely held businesses, including partnership agreements, operating agreements, shareholder agreements, and buy-sell agreements, to ascertain the rights and obligations of the client with respect to the transfer of closely held business interests upon the client's death
- Compensation agreements, such as employment agreements, deferred compensation agreements, split dollar agreements, salary continuation agreements, and covenants not to compete, to ascertain the client's interest in compensation arrangements during retirement and after death
- Copies of qualified plan and IRA plan documents, to determine whether each plan itself will permit the type of beneficiary designation I recommend for the client

- Prior planning, including documentation, regarding disabled beneficiaries or beneficiaries with special needs, and a description of the disability or the special needs accompanied by contact information for caregivers, medical providers, and others on whom the beneficiary depends

If I am given the financial information prior to the first client meeting, for clients with potentially taxable estates, I often prepare a software-generated estate tax analysis, which shows the tax results of passing property at death under the client's current plan, and the tax savings that could result from changes in ownership and the use of different planning techniques. This analysis may be performed after the initial meeting, and may be used to show clients the pros and cons of different planning ideas.

Use of Revocable Trusts as Will Substitutes

Generally, New York is not a jurisdiction in which the cost of probate is prohibitive. The state is large, and different areas may or may not experience delays in obtaining letters testamentary from the surrogate's courts. However, I have started to see more delay from certain of the surrogate's courts, and this, coupled with the desire for privacy, ease of administration, and cost reduction, has led me to recommend to more clients the use of revocable trusts as a substitute for wills in the transfer of their assets at death.

I always advise the client that the establishment of a revocable trust, together with the transfer of the client's assets to that trust, will have more significant up-front costs than merely having a will. The client also must be diligent, from when the trust is created and throughout the remainder of the client's lifetime, in making sure that newly acquired assets are titled in the name of the trust, if one of the client's goals is to avoid probate. Otherwise, there may have to be a probate of the will, even though most of the client's assets are owned by the trust, to effectuate the transfer of assets that never made their way into the trust.

My experience indicates that clients often underestimate the time, effort, paperwork, phone calls, letters, e-mails, and document preparation that go into transferring assets to their revocable trusts, and to ensure that

beneficiary designations to insurance and retirement plans are changed so that their revocable trusts are named as the beneficiaries. Clients often ask the attorney and the law firm staff to assist in the transfers, and it is important for the attorney to advise the clients of the significant costs the client may incur for the professional time involved. In fact, it would not be unusual to have the costs associated with completing all transfers to the trust equal or exceed the initial cost incurred in establishing the trust.

Revocable trusts are not for everyone, and the client must be asked the following questions to ascertain if a revocable trust is right for them:

- Is avoiding probate your primary concern, and if so, why? In connection with the costs associated with probate, will the executor take commissions (family members usually do not, or the will may prohibit them from taking commissions)? Will the successor trustee of a revocable trust be entitled to take trustee commissions (assuming the client will act as the initial trustee)?
- If a client is married, will the assets they are leaving to the surviving spouse be held in trust, will they pass outright to the spouse, or will it be a combination of both? If the decedent's assets will not be held in trust for the surviving spouse, one reason for using a revocable trust—the avoidance of probate—will be lost in the surviving spouse's subsequent estate.
- What type of assets does the client own? Assets held jointly with a spouse or other heirs, or that pass by beneficiary designation or by transfer on death designation to the surviving spouse or other heirs, are not probate assets in the decedent's estate, and do not have to be transferred to a revocable trust to avoid probate.
- Is the client willing to pay the up-front costs associated with forming and transferring assets to a revocable trust? Will the client be diligent about titling newly acquired assets in the name of the revocable trust?
- Does the client own out-of-state real property? If the client does own out-of-state real property, some kind of planning, including owning the real property in a revocable trust, is required to avoid ancillary probate in the other state.

I have found that couples who desire for the survivor's assets to be held in trust, and who each plan during their lifetime to hold their assets in revocable trusts, incur significantly less in legal costs at the death of the first to die than couples who do not. If planned correctly, for those clients who use revocable trusts, the only significant legal work that needs to be done at the death of the first to die is to assist in submitting claims for property that passes by beneficiary designation, preparing fiduciary income tax returns for the trust, and preparing any necessary federal and state estate tax returns for the decedent.

When both members of a couple desire to use revocable trusts, I have found that use of one joint revocable trust accomplishes the same result as having two separate revocable trusts, and is something that clients find appealing (assuming, of course, that neither individual has creditor issues). However, I have found that the financial institutions in which client funds are held have a difficult time understanding joint revocable trusts and the requirement that, for proper tax planning, property held separately outside the trust not be commingled upon transfer to the trust.

Single clients who are leaving property outright to children, grandchildren, and others may have less of a need for a revocable trust than couples do. The cost and effort involved in making sure assets will be titled in the name of the trust will be for naught upon the grantor's death, as the trust assets will then have to be transferred and re-titled in the names of the beneficiaries. Therefore, in this situation the cost-effectiveness of using a revocable trust over the probate of a will needs to be closely analyzed. However, some clients' desire for privacy will be reason enough to justify the use of a revocable trust, regardless of the costs of creating and administering the trust.

Same-sex domestic partners may find that use of revocable trusts, or a joint revocable trust, is the desired form of at-death transfer. The probate process requires notification be given to the decedent's distributees. The distributees, who would inherit from the decedent but for the provisions of the decedent's will, have the right to contest the will and other aspects of the probate proceeding, including who may be appointed as executor. Further, the distributees, as well as the general public, will have access to the will and therefore the dispositive provisions of the will. Use of a

revocable trust does not require that any notice be given to the decedent's distributees, eliminates the possibility of a will contest, and shields the contents of the decedent's estate plan from public disclosure.

As mentioned above, clients who own real property in states other than New York also should consider use of a revocable trust to own and dispose of such property, even if the trust owns no other asset, to avoid ancillary probate in the other state.

Process

During the initial client meeting, I review the client questionnaire and estate tax analysis with the client, discuss the client's objectives, and obtain information that is not already in the questionnaire.[1] By the end of the meeting, I have developed a plan of action. I have handwritten notes from the meeting but, often equally as important, I have acquired knowledge that is not in the notes. Soon after the meeting, I prepare a memorandum of the meeting that includes all of the information necessary to draft the estate planning documents. This includes background information on the client, which is of value to the drafting attorney in understanding the facts that gave rise to the plan, and which, being in written form, will be accessible if someone else needs it in the future.

If I did not perform an estate tax analysis before the client meeting, and if the client has a potentially taxable estate, I generally prepare a tax analysis at this time. I also e-mail the estate plan memorandum to the appropriate drafting attorney to prepare the first drafts of the documents. Using a separate drafting attorney, who bills at lower rates, is cost-effective for the client, and is a way to involve at least two attorneys in a review of the client's documents. Once the documents are in a form to send to the client, I draft an explanatory letter that explains in a few pages the overall plan and directs the client to look at specific provisions in the documents to understand how the plan is being implemented. The letter and drafts of the documents are mailed to the client, who is asked to call for an appointment, or to call to discuss any questions, after the client has reviewed the letter

[1] For ease of reading, I will refer to clients in the singular, whether talking about an individual client or a couple.

and the documents. I use a tickler system in Microsoft Outlook Tasks to follow up with the client to make sure I schedule an appointment to sign the documents.

At that appointment, I review the plan with the client, and the documents are signed and witnessed. Original wills and duplicate originals of the living wills, trusts, health care proxies, and powers of attorney are kept in our office fireproof safes. Copies of the wills and duplicate originals of the other documents are mailed to the clients the day after the meeting.

Planning with Trusts

Trusts are devices for estate planners to use to assist a client in achieving goals that could not be achieved through the "outright" disposition of assets to the client's heirs. These goals include:

1. Privacy
2. Professional management of assets
3. Protection of assets from the client's creditors
4. Avoidance of probate and its costs
5. Management of assets in multiple jurisdictions
6. Minimizing estate taxes
7. Minimizing generation-skipping transfer taxes
8. Preserving assets for later distribution to future generations
9. For "second marriage" couples, ensuring that both the current spouse and the children of the "first marriage" are provided for and protected
10. Protection of assets from the creditors of children and further descendants
11. Income tax planning through use of the grantor's, the trust's, and/or the beneficiaries' tax brackets and through selection of the trust's jurisdiction for state income tax purposes
12. Forum shopping, in the initial establishment of the trust and through use of change of situs provisions, to select the best state as trust domicile for income and estate tax, asset protection, and principal and income purposes

Trusts can be established during lifetime or at death. Lifetime trusts (living trusts) are either revocable or irrevocable. Testamentary trusts are always irrevocable.

Transfers to revocable trusts do not have any immediate income, estate, or generation-skipping transfer tax benefits. The revocable trust is considered an alter ego of the grantor. The grantor is treated as the taxpayer for income tax purposes.

Transfers to irrevocable trusts often do have an immediate gift, estate, and generation-skipping transfer tax consequence. A transfer without consideration will be considered a gift for gift tax purposes and, depending on the type of trust, may qualify as a gift of a present interest and the annual $13,000 per donee exclusion from gift taxes. Gifts in excess of the donor's annual exclusions will qualify for the $1 million (cumulative) exemption from federal gift taxes.

Lifetime transfers to irrevocable trusts are warranted when the donor has an estate that would generate federal or state estate tax and the donor can part with the use of the property transferred. The current federal estate tax exemption is $3.5 million per individual. Cumulative lifetime taxable gifts count as part of the $3.5 million total.

The best assets to transfer during lifetime to an irrevocable trust are assets that have the greatest potential for appreciation. The future appreciation in the assets transferred will pass to heirs without taxation in the donor's estate.

If the trust instrument provides for the transferred assets to stay in trust for the lifetimes of the grantor's children (or bypass the grantor's children entirely) and pass eventually to the grantor's grandchildren or further descendants, the transfer to the trust will be a generation-skipping transfer, and the assets in the trust will be subject to the generation-skipping transfer tax, unless the transfer has been sheltered by use of the generation-skipping transfer tax exemption, which currently is $3.5 million. Cumulative lifetime taxable gifts to grandchildren count as part of the $3.5 million total.

Lifetime transfers to irrevocable trusts can be structured so that the grantor *is not treated as the owner* of the trust property for estate and

generation-skipping transfer tax purposes (an estate tax "effective" trust) but *is treated as the owner* of the trust for income tax purposes (an income tax "defective" trust). Such a trust, commonly known as an intentionally defective grantor trust, described earlier in the chapter, opens the door for planning that leverages upon, and saves for future use, the $1 million gift tax and the $3.5 million estate and generation-skipping transfer tax exemption amounts.

Creating a Grantor Trust

A trust becomes a grantor trust by intentionally subjecting itself to provisions under the grantor trust rules set out in I.R.C. §§ 671–679 (West 2009).[2] It is important to select grantor trust powers that can be released by the power-holder, so that the trust may at some point in the future terminate its grantor trust status.

If the grantor (for our purposes, I will assume the grantor is also the person who transferred all the property to the trust) retains the right to enjoy, or to control the enjoyment of, the income or principal of the trust, or if someone who is related or subordinate to the grantor, whose exercise or non-exercise of a power will not impact his or her interest in the trust, has a right to control the enjoyment of the income and principal of the trust, the grantor will be treated as the owner of trust assets for income tax purposes.[3]

Below is a list of grantor trust rules commonly used to create a grantor trust.

Right to Substitute Assets

Under I.R.C. § 675(4), a grantor is treated as the owner of any portion of the trust over which the grantor has retained the right, exercisable in a non-

[2] All section references hereinafter are to the Internal Revenue Code of 1986, as amended, unless otherwise indicated.

[3] A "related or subordinate party" is any non-adverse party who is (i) the grantor's spouse if living with the grantor, or (ii) any one of the following: the grantor's father, mother, issue, brother, or sister; an employee of the grantor; a corporation or any employee of a corporation in which the stock holdings of the grantor and the trust are significant from the viewpoint of voting control; a subordinate employee of a corporation in which the grantor is an executive.

fiduciary capacity, to reacquire trust assets by substituting assets of equivalent value.

Premium Payment Power

Under I.R.C. § 677(a)(3), the grantor is taxable as the owner of any trust or trust portion as to which the grantor or a non-adverse person (or both) may apply trust income to pay premiums on life insurance policies on the life of the grantor or the grantor's spouse.[4]

Power of Appointment

Under I.R.C. § 674(a), a grantor is treated as the owner of the entire trust if a non-adverse party has the power, without the approval or consent of an adverse party, to appoint trust income and principal, exercisable during the grantor's lifetime.

Power to Borrow

Under I.R.C. § 675(2), the power of a grantor or a non-adverse party or both that allows the grantor to borrow from the trust without adequate interest or without adequate security, will cause the portion of the trust subject to the power to be treated as owned by the grantor.

Benefits of Using a Grantor Trust as an Estate Planning Vehicle

Freezing Value of Appreciating Property

Using a grantor trust as an estate freezing technique is a way the grantor can freeze the value of an asset for purposes of determining the grantor's total adjusted taxable gifts during lifetime and the total value of the grantor's taxable estate at death.

[4] An "adverse party" is a person with a substantial interest in the trust that would be adversely affected by the exercise or non-exercise of the power such party possesses in respect of the trust. A person holding a general power of appointment over the trust will be deemed to have a beneficial interest in the trust.

Grantor Taxable on Income

As the grantor is taxable on the income of the trust, the income tax paid by the grantor is in effect a tax-free gift to the trust beneficiaries.

Grantor Trust Can Accumulate or Distribute Income Tax-Free

As the trust pays no taxes on its income, the trust is essentially tax-exempt. Distributions to the beneficiaries may be made tax-free, and accumulations of income are tax-free as well. This “tax-free” status allows more to accumulate for the benefit of the beneficiaries.

Transferring Discounted Income-Producing Assets

A grantor may transfer an already discounted asset, such as an interest in a family limited partnership or family limited liability company, which produces an income stream. The income from the transferred asset is taxable to the grantor and may be used to fund the loan payments on the note to the grantor.

Grantor Trust Qualifies as an S Corporation Shareholder

As a general rule, a trust is not a permissible shareholder of S corporation stock. Among other exceptions to this rule, a trust treated as owned by an individual U.S. citizen is a permissible S corporation shareholder. Although there are other trusts that can qualify as S corporation shareholders, a grantor trust is the simplest permissible trust.

Grantor Trust Enables Grantor to Take Deductions and Qualify for Exclusions on Transferred Property

Because the trust is ignored for income tax purposes, the grantor is entitled to the I.R.C. § 121 (2008) exclusion of gain from the sale of a principal residence owned by the trust. Likewise, a grantor is allowed to take the I.R.C. § 163(h)(3) (2009) mortgage interest deduction with respect to real property owned by the trust.

Income Tax Consequences of Certain Transactions between the Grantor and the Trust

For income tax purposes, a grantor trust is ignored as a taxable entity. As a result, most transactions between the grantor and a grantor trust will not be taxable.

Sale to Grantor Trust

No gain is recognized by the grantor on the sale of assets to a grantor trust. The Internal Revenue Service's position is that there is no gain or loss recognized in transactions between the grantor and the trust when the grantor is treated as the owner of the trust.[5]

Interest Payments from Grantor to Trust

Interest payments on a note to the grantor from a grantor trust will not be includable in income by the grantor, nor be deductible by the trust.

Rent Payments

Rent payments from the grantor to the trust are not taxable rental income to the trust. Rather, much like income tax payments, they are in effect tax-free gifts to the beneficiaries.

Structuring a Sale to a Grantor Trust

1. The client creates a grantor trust with at least one of the grantor trust powers listed in I.R.C. §§ 671–679. The trust contains provisions for the trustees and/or the power-holder to release the powers to terminate the grantor trust status.
2. The trust agreement will name the beneficiaries. Keeping in mind the fact that the grantor will be paying taxes on trust income, including the grantor's spouse as a beneficiary is a safe way to ensure that the grantor will have sufficient assets to pay the income taxes.

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[5] Rev. Rul. 85-13, 1985-7 I.R.B. 28 (1985); but compare *Rothenstein v. United States*, 735 F.2d 704 (2d Cir. 1984).

3. The grantor must determine the term of the trust. Given the benefits conferred by the trust (and the allocation of generation-skipping transfer tax exemption to the trust), it is better to not have the trust terminate at designated hallmarks, such as a specific age of a beneficiary, but rather to provide that the property remain in trust for a beneficiary's lifetime.
4. The trust should have flexibility by giving a beneficiary a limited power of appointment over trust property during the grantor's life.

2. Selecting the assets to sell:
    a. The best assets to transfer to a grantor trust are assets with a current low valuation that have great appreciation potential.
    b. A fair market value appraisal must be obtained for the assets that are transferred.
3. Structuring the sale

Rather than using the annual gift tax exclusion (currently $13,000 per donee) or the lifetime exemption (currently $1 million) to shelter a gift of an asset to a grantor trust, the grantor instead chooses to sell an asset to the trust in exchange for an installment note. With a sale, the grantor is able to transfer the future appreciation of the asset without any income or gift tax consequences, and preserve their $1 million exemption for later use during life or at death.

It is important to follow certain formalities so that the sale is respected as a sale, and not treated as a transfer with a retained life estate, which would cause estate tax inclusion under I.R.C. § 2036(a)(1) (West 2009), or a transfer with a retained interest under I.R.C. § 2702 (1996). The most important factor to qualify the transaction as a sale is that the debt be bona fide debt. The following criteria are important in establishing that the debt is bona fide:

A. *Promissory note:* There should be a promissory note or other evidence of indebtedness.
B. *Bona fide debt:* The promissory note should qualify as bona fide debt:
    1. The amount of the payments should not be based on the amount of income produced by the trust.

    2. The obligation should not be chargeable to the transferred property.
    3. The promise must be a personal obligation of the transferee.[6]

C. *Interest rate:* The interest rate should be equal to or greater than the applicable federal rate, and not tied to the potential or expected earnings from the property.
D. *Payments under the note:* The payments should be made on time, without regard to the trust's income. If not made, the seller should make demand for payment.
E. *Repayment schedule:* The note should have a fixed repayment schedule. Balloon notes appear to satisfy this requirement.
F. *Security:* The obligation of the trust should be secured or guaranteed.
G. *Seed money:* The trust should have assets, other than the purchased property, equal to at least 10 percent of the value of the property sold to the trust.
H. *Beneficiary guarantees:* If the trust does not have seed money, or sufficient seed money, beneficiary guarantees of the note may be used to establish that the transaction is bona fide and arm's length.

Dynasty Trust and Asset Protection Planning

Multiple jurisdictions, including Alaska and Delaware, allow a grantor to create a self-settled perpetual trust, safe from creditors of the grantor and not subject to the Rule Against Perpetuities that would otherwise be applicable to a trust created under the law of the grantor's state of domicile. By using a grantor trust as a dynasty trust, a grantor may transfer appreciating assets for the benefit of future generations, and protect such assets from the creditors of the grantor and the beneficiaries of the trust.

Key Elements of Strategy Development

Each client is unique, but similar strategies may be applicable to a wide variety of planning situations. It is important to listen to the client to

[6] *Fidelity-Philadelphia Trust Co. v. Smith*, 356 U.S. 274 (1958).

determine the client's needs, to assess with the client the risks associated with a particular strategy, and to formulate with the client the best path to take. In selecting strategy, the attorney needs to take into account federal and state gift, estate, generation-skipping, and income tax laws, the trust laws of different states, and the Estates, Powers, and Trusts Law and the Surrogate's Court Procedure Act, for New York clients.

The most important elements of the estate planning process include:

- Clarity of communication between lawyer and client
- Obtaining correct and up-to-date information about the client
- Listening to the client and the client's expressed needs and desires
- Knowledge of the applicable laws
- Knowledge of the many different estate planning techniques and solutions
- Creativity in applying the appropriate techniques to the client's unique set of facts
- Excellent drafting skills
- Excellent implementation of the overall plan

These are the traits of a good estate planning lawyer. An off-the-shelf plan not tailored to a client's specific circumstances and goals ultimately does not provide much value to the client.

I generally work with the client and the client's other advisers to develop a coherent strategy for the client. Often a meeting with the client and the client's investment adviser, insurance agent, financial planner, and accountant yields new ideas and approaches based on a review and understanding of the client's existing plan, and through sharing observations and insights informed through the vantage points of our different professions.

Often the insurance agent or financial planner has met with the client one or more times prior to the first meeting with the attorney. The gathering of financial and personal information, an estate tax analysis, and recommendations for specific actions may have been developed by these professionals and communicated to the client. The attorney's role in this context is to review what has been previously prepared, but not to slavishly

follow any recommendations unless the attorney also believes the recommended actions to be appropriate for the client. The attorney must exercise his or her own judgment and bring to bear his or her own expertise in advising the client as to an appropriate course of action. It is always best for the attorney to obtain consensus from the other advisers, if possible, before communicating a plan of action to the client. The client's accountant is usually the adviser most familiar with the client's financial picture and that of the client's business, and usually has the best feel for the client's personal predilections and capacity for taking risk.

Sometimes time is a mitigating factor, as when a client is ill or about to have surgery, or is about to take a trip. In these cases, it may be necessary to prepare "stop-gap" documents that put into place a plan that, while not perfect, is better than the plan (or lack of a plan) the client currently has. In addition, if a client does not have a strong relationship with one or more of the other advisers, or does not have an adviser in one of those other professions, planning will proceed without such an adviser's participation.

Understanding Developing Issues in Estate Planning

New issues have been added recently to my estate planning checklist. I have advised our clients of these matters by personal letter and in postings to our Web site. In the letters, I have provided clients with a short synopsis of their current wills and suggested recommendations for changes to their wills. I have also conducted client seminars regarding the effective use of grantor-retained annuity trusts in this low interest rate, low market value environment. These issues are as follows.

Obtaining Information Regarding Transfer on Death Designations, Due to Changes in New York Law

Since January 1, 2006, Article 13, Part 4 of the Estates, Powers, and Trusts Law (N.Y. EST. POWERS & TRUSTS LAW §§ 13-4.1 et seq. (West 2009)) has provided for registration of securities in beneficiary form, so that, upon the death of the owner of the securities, title to the securities passes to the named beneficiary, who may then re-register the securities in the beneficiary's own name, and name their own beneficiaries. The transfer of securities on death to named beneficiaries bypasses probate, and is an

alternative to using a revocable trust. A transfer on death is especially useful, and is superior to the use of a revocable trust, when the beneficiary is to own the securities outright, and not in further trust, after the death of the original owner. In advising a client regarding transfer on death designations, the attorney must be careful to make sure there are enough assets passing through probate, or through a revocable trust, and not directly to beneficiaries, to ensure that sufficient resources are available to pay the decedent's debts, taxes, and administration expenses, and to fund all of the decedent's other specific bequests. If a client is married, it is important to ensure that the appropriate amounts and types of assets are available to maximize the benefits of the estate plan. If nothing is available to pass pursuant to the terms of a will or trust that has been drafted, the attorney may not have helped the client achieve their estate planning objectives. As a result, careful drafting for renunciations or disclaimers should include references not only to probate and trust-owned assets, but also to assets passing outside of the will or trust.

Topics of Disability and End-of-Life Care, Which Lead to Discussions Regarding Long-Term Care Insurance, Asset Protection Planning, Living Wills, Health care Proxies, and Durable Powers of Attorney

Many clients will suffer disabilities or need end-of-life care that will consume valuable resources. Planning for this possibility, and analyzing the pros and cons of long-term care insurance as part of the funding solution, has become an important part of estate planning advice. Medicaid planning has become more difficult, and the possibility is real that clients will run out of money, or have significantly less to leave to their surviving spouses and children, due to the costs of medical, custodial, and long-term care. This issue has been exacerbated by the steep decline in individual net worth resulting from the recent recession.

Changes and Uncertainty in the Federal Tax Law, the Decoupling of the Federal and New York Estate Tax Regimes, and the Decline in Asset Values Due to the Recession, Which Lead to Discussions Regarding the Use of Formula Provisions in Wills and Trusts and the Importance of Flexible Post-Mortem Planning

Recent changes in the federal estate tax law, the decoupling of the federal and New York estate tax exemptions, uncertainty regarding the federal estate tax

beyond 2009, and the economically volatile times in which we live, means it is more important than ever for clients to review and update their estate plans. A significant consideration in estate planning is the impact of estate taxes. The federal estate tax exemption (the amount that can pass free of estate tax) has increased significantly over the past ten years and continues to be in a state of flux. The federal exemption amount is currently $3.5 million per person, but it is scheduled to return to $1 million in 2011 (after a year of no estate tax in 2010). However, several bills have been introduced in Congress, one of which would extend the $3.5 million exemption beyond 2009, and another of which would provide for a reduced exemption of $2 million in place of the planned $1 million exemption in 2011. To complicate matters, the New York exemption amount is only $1 million, and there is no indication that it will change any time in the near future. The gap of $2.5 million between the New York exemption amount and the current federal exemption amount means the difference between the two may be subject to New York state estate tax.

Many clients have wills with a formula provision that divides the property the predeceased spouse leaves to the surviving spouse into two shares—the "marital share" and the "exemption amount." The marital share is the minimum amount necessary to reduce the predeceased spouse's taxable estate to the exemption amount (the largest sum that can pass free of federal estate tax). The marital share often passes outright to the surviving spouse, and it thereby qualifies for a deduction (the "marital deduction") in calculating the taxes in the predeceased spouse's estate. Anything passing in this manner to the surviving spouse becomes an asset of his or her estate. The exemption amount usually passes into a trust (the "residuary trust" or "credit shelter trust"), the assets of which will escape taxation in the surviving spouse's estate. Some clients pass the exemption amount to the next generation, outright.

The increase of the federal exemption amount at the beginning of this year to $3.5 million created the $2.5 million gap between the New York exemption amount (which remains at $1 million) and the federal exemption amount. Most of the old formula provisions require the maximum federal exemption amount be placed in the credit shelter trust, without the ability to qualify part of it for the marital deduction. Thus,

while the property held in the credit shelter trust will escape federal taxation in both estates, it will be subject to New York state estate tax on the first death because of this gap. For example, if the predeceased spouse has sufficient assets to fully fund the residuary trust with the $3.5 million federal exemption amount, the New York state estate taxes at the predeceased spouse's death will be $229,200.

Incurring the New York state estate tax at the first death may minimize estate taxes through both spouses' estates, but it may not. It is important to incorporate flexibility into clients' wills (or revocable trusts) to provide the executor, the trustee, the surviving spouse, and the client's tax advisers the ability to do post-mortem tax planning at the time of the first spouse's death, and if appropriate, to make decisions that reduce or eliminate the New York state estate tax in the first spouse's estate.

The current federal estate tax law dictates that, to be effective, an estate plan must now take into consideration at least three (and possibly more) potential transfer tax regimes, any one of which may be in existence at the time of a decedent's death. Wills and trusts will need to accommodate the possibility that a decedent will die under any one of the following scenarios:

- Death during 2009 when the estate and generation-skipping transfer tax exemptions are $3.5 million and the lifetime gift tax exemption is $1 million
- Death in 2010 when the estate and generation-skipping transfer taxes will be repealed (and when modified carry-over basis will be implemented)
- Death in 2011 (and thereafter) when the estate and generation-skipping transfer tax exemptions return to $1 million, according to the provisions of the law in effect prior to enactment of the Economic Growth and Tax Relief Reconciliation Act of 2001

Wills and trusts with tax-driven formulas should be reviewed to be certain that the formulas are appropriate based on the size of each spouse's estate and the nature of a person's assets, and to take into account all three of the possible estate tax scenarios described above, while keeping in mind that all of the above are subject to change at any time by an act of Congress. Consideration should be given to the following:

- The will and any trusts must be drafted to properly dispose of assets regardless of when death occurs. Most existing wills with formula clauses do not adequately address how property will pass in the event that the federal estate tax is repealed.
- If the credit shelter share and the marital share will ultimately pass to different beneficiaries, such as in a second marriage situation, a plan with a substantial charitable bequest at the death of the second spouse, or a plan with specified business assets passing to only some of the heirs, the formula provisions for dividing assets into the credit shelter and marital shares should be reviewed to determine whether there should be a cap on the dollar value of assets passing into either of the two shares.
- As the exemptions have increased pursuant to the phase-ins under the Economic Growth and Tax Relief Reconciliation Act of 2001, typical formula provisions will cause more assets to pass into the credit shelter trust, and less into the marital share. This may cause more assets than are necessary for elimination of tax at the surviving spouse's death to pass into the credit shelter trust.
- Consideration should be given to establishing a cap on what passes into the credit shelter trust. Capping the amount at $1 million will eliminate any New York estate tax. Alternatively, you could provide for a flexible cap by establishing an initial funding cap of a specified dollar amount, which amount may be increased through a renunciation by the surviving spouse.
- The entire estate could be made to pass into a trust that is qualified terminable interest property. Such a trust must be for the sole benefit of the surviving spouse, and must provide the spouse with all of its income annually. The executor would determine whether to make a partial or complete post-mortem qualified terminable interest property election. The portion of the trust for which the election is made will qualify for the marital deduction. The portion of the trust for which no election is made will bypass the surviving spouse's estate. The election will determine the size of the two shares and the corresponding tax effect in the surviving spouse's estate. The portion for which no election is made can be severed and placed into a separate trust of which the children and further descendants are also beneficiaries ("Clayton qualified terminable interest property"). This

option requires careful planning and drafting to ensure that tax elections by the fiduciaries do not result in unintended gifting.

- The entire estate could be made to pass outright to the surviving spouse, who would utilize post-mortem disclaimers to establish the funding of a credit shelter trust. Note that disclaimers depend upon the good intentions and legal capacity of the surviving spouse, and there is a risk that they will not be made. Disclaimed assets are not free from the creditors of the disclaiming spouse, as are assets in a credit shelter trust and qualified terminable interest property trust.

If less than one-third of the estate (including testamentary substitutes) passes to the surviving spouse, the survivor will have the right under New York law to elect to receive a survivor's share under the N.Y. EST. POWERS & TRUSTS LAW § 5-1.1-A (2006) in lieu of what is given under the will or trust. As the exemption amount has increased from $1 million in 2002 to $3.5 million in 2009, the credit shelter share now encompasses a greater portion of a decedent's estate, and the marital share is smaller. If the marital share (when added to non-probate assets received by the spouse) would be less than one-third of the augmented estate, it will give rise to a right of election. If this is a concern, the estate planning documents should be drafted to ensure that the surviving spouse receives outright at least one-third of the augmented estate.

Use of Estate Freezing Techniques That Benefit from Current Low Interest Rates and Current Low Asset Values

Currently, three favorable factors have made the use of a grantor-retained annuity trust as an estate-freezing device very attractive:

- Interest rates are low.
  - Applicable federal rates, the rates published by the Internal Revenue Service and applicable for many estate freezing techniques, reached historic lows this spring and are still very low.
  - The I.R.C. § 7520 (West 2009) rate, used to value the annuity and remainder interests in a grantor-retained annuity trust, was 3.4 percent in September 2009 (as we are

going to press, the Internal Revenue Service published the October rate, which decreased to 3.2 percent), was 4.2 percent a year ago, and was at or close to 6 percent two and three years ago.
    - Low interest rates allow for greater transfers of wealth at low or no gift tax cost.
- Equities, real estate. and other investments are at depressed values.
    - The possibility of substantial short-term (four years or less) increases in value is significant as markets rebound.
- Congress is considering adverse tax law changes, so now is the time to act when current laws favor freezing techniques.
    - The amount of the federal estate tax exemption is uncertain.
    - Pending legislation would require grantor-retained annuity trusts to have a minimum ten-year term.
    - Pending legislation would eliminate discounts in transactions between family members.

A grantor-retained annuity trust is created by a grantor transferring one or more high-yield assets into an irrevocable trust and retaining the right to an annuity interest for a fixed term of years or for the shorter of a fixed term or life. When the retention period ends, assets in the trust (including all appreciation) go to the named "remainder" beneficiaries. In some cases, other interests, such as the right to have assets revert back to the transferor's estate in the event of the transferor's premature death, may be included. The annuity is calculated by using the I.R.C. § 7520 rate published monthly. The gift tax value of the transferred assets is determined at the time the trust is created and funded, using the "subtraction method," by subtracting the value of the annuity interest (and, in some cases, other retained interests, such as the right to have the assets revert back to the transferor's estate if he or she does not live the entire term of the trust) from the fair market value of the assets transferred in trust. It is advantageous to try to nearly "zero out" the value of the remainder interest, so that for gift tax purposes there is only a nominal gift to the remainder beneficiaries. This is done by increasing the amount of the annuity until the present value of the remainder interest is almost zero. In essence, the amount of the annuity is computed so that over the trust term, the value of the original trust property, plus a yield equal to the I.R.C. § 7520 rate, will

be returned to the grantor. If the trust earns a greater rate, something will pass to the remainder beneficiaries without the grantor making any additional taxable gift.

As an example of what can be achieved in today's low interest rate environment, if a two-year "zeroed out" grantor-retained annuity trust had been funded with $1 million of marketable securities in September 2009, when the I.R.C. § 7520 rate was 3.4 percent, and if the actual return on investment for each of the two years ends up being 12 percent per year, the remainder beneficiaries, instead of receiving $0 as calculated for gift tax purposes, will receive $140,018 gift tax-free at the end of the two-year term. The grantor will have received $1,051,304 in two equal annual installments of $525,652, representing a 3.4 percent return on the grantor's initial $1 million investment.

The Updated New York Power of Attorney Statute and Forms

On September 1, 2009, the form for a statutory power of attorney changed in New York. The new law establishes the form of the statutory power of attorney and the rules that govern the use of a power of attorney. The changes are significant and offer critical protections to the grantor of a power of attorney. These protections, however, introduce increased complexity in the form and the decisions a client must make in executing a New York power of attorney.

It is not necessary to execute a new power of attorney if a client has a validly executed power of attorney currently in place.

The power of attorney is an important and effective tool in managing a client's financial and contractual affairs, especially if the client becomes disabled or incapacitated, temporarily or permanently. The power of attorney grants to another individual (the "agent") the authority to act on the principal's behalf without consultation with the principal. Because this document is a significant grant of authority, careful consideration of its terms is recommended.

The new law is primarily an attempt to remedy the potential for financial exploitation and abuse that existed under the old law.

Chapter 644 of the laws of 2008 (2008 N.Y. Sess. Laws ch. 644) amends the provisions of the General Obligations Law relating to the use of powers of attorney in New York, and creates a new statutory form that incorporates the changes listed below:

- All powers of attorney must be executed by both the principal and the agent. Although the principal and the agent do not have to sign at the same time, the power of attorney is not effective until signed by the principal and the agent.
- If the principal wishes to grant the agent the authority to make transfers and gifts, the principal may do so only by executing a "major gifts rider" that must be executed in the presence of two witnesses. This rider is necessary if the agent is to be authorized to make annual exclusion gifts or other transfers in connection with financial and estate planning.
- The new form will allow an agent access to health care billing and payment matters, so that the agent may review, question, and pay medical bills without concern that the Health Insurance Portability and Accountability Act privacy rule will prevent the agent's access. The new law continues to prohibit an agent from making health care decisions for the principal (which authority may be granted only under a health care proxy).
- The new statutory form includes an explanation of the agent's role, the legal limits on the agent's authority, and the fiduciary obligations of the agent, including recordkeeping. An agent had these fiduciary obligations under the old law, but the new law attempts to ensure that agents are aware of their responsibilities.
- The new form allows the principal to appoint a "monitor" to request and receive records of the agent's transactions.
- An attorney may certify a copy of the power of attorney instead of having to record the power of attorney to obtain certified copies.
- The new law requires financial institutions to accept a validly executed power of attorney form even though the form may not be

the financial institution's own form, unless the institution has a reasonable basis to not accept the form. Under the old law, brokerage houses and other non-bank financial institutions did not have to accept the statutory power of attorney, and most of them required a customer to complete and execute the institution's own power of attorney forms. This will no longer be the case, not only with respect to powers of attorney executed under the new law, but also with respect to statutory powers of attorney validly executed under the old law. If the client has significant assets invested in institutions other than in banks, the new law eliminates the need for multiple brokerage powers of attorney.

Impact of Laws on Strategy and Administration

The estate and trust laws that have had the most impact on my client strategies and the administration of their trusts include:

- The Internal Revenue Code, especially as it relates to gift, estate, and generation-skipping transfer taxes and to the income taxation of grantor trusts and trusts in general
- The New York estate tax laws
- N.Y. EST. POWERS & TRUSTS LAW § 11-2.1 (2002), the Principal and Income Act
- N.Y. EST. POWERS & TRUSTS LAW § 11-2.3 (2008), the Prudent Investor Act
- N.Y. EST. POWERS & TRUSTS LAW § 11-2.4 (2008), the Optional Unitrust Provision
- N.Y. EST. POWERS & TRUSTS LAW §§ 13-4.1 et seq., regarding transfer-on-death security registration
- N.Y. EST. POWERS & TRUSTS LAW § 10-6.6(b) (2001), regarding decanting irrevocable trusts
- N.Y. EST. POWERS & TRUSTS LAW § 10-10.1 (2004), regarding the power of a trustee to make certain distributions to himself or herself
- The New York General Obligations Law, as it relates to the new power of attorney statute
- The Alaska and Delaware laws dealing with self-settled asset protection trusts

These laws provide the framework for developing sophisticated estate planning strategies.

Examples of How New Laws Impact Client Strategies

By way of example, a wife is an income beneficiary of a testamentary trust established by her husband. The trust's major asset is stock in an S corporation that does not pay dividends. The trustees consider the S corporation stock to be a sound investment. By investing for total return, the trustees are able to maximize the value of the trust. However, their duty of impartiality requires that they endeavor to make distributions to the income beneficiary. The trustees have three options: (1) diversify the trust's portfolio to invest in "income"-producing assets, (2) exercise their power to adjust and pay out some "principal" to the income beneficiary, or (3) speak to the board of the corporation to see if the corporation is able to pay a dividend. In this scenario, the best alternative would be the third option. The trust would continue to invest in what the trustees believe to be a growth-oriented asset, yet an income stream is created from that asset to satisfy the wife's income needs. If that option were not available, it would be important for the trustees to consider other factors in making their decision. For example, if the life income beneficiary is the second wife of the decedent, and the remainder beneficiaries are the decedent's children from his first marriage, electing unitrust treatment (see below) may be the most attractive, and least controversial, course of action.

Having different amounts that can pass free of estate tax under the New York and federal estate tax laws requires an analysis of the estate tax that might be paid through both estates (assuming the clients are a married couple) under several possible scenarios, in an effort to determine which option allows for the least amount of tax to be generated through both estates. As discussed earlier, it is important to look at whether funding a credit shelter trust up to the $1 million New York exemption amount will help reduce the overall taxes paid by both estates, or whether increasing the amount passing into the credit shelter trust and thereby generating a New York estate tax at the first death would be more tax-efficient. This analysis will differ depending upon the size of the estates, whether the clients have children from former marriages, whether there will be charitable beneficiaries, and how the clients want their assets to be divided among these potential classes of beneficiaries.

The decanting statute is a beneficial tool to make an irrevocable trust more flexible in meeting the needs of its beneficiaries. For example, a trust is established for a decedent's brother, his spouse, and their descendants. The trust has a substantial corpus. The decedent's brother is now deceased, and the decedent's spouse is currently the life income beneficiary, entitled to all the income earned by the trust. The trustee has complete discretion to invade the trust principal for the life income beneficiary. The trust will terminate at the death of the life income beneficiary, and it must then distribute its assets outright to her son, who is the only child and an adult. Her son would prefer that the trust not terminate on her death, but continue to benefit him and his children during his lifetime, and to pass into trusts for his children upon his death. The trustee, who is independent, may appoint ("decant") the trust property to a new trust, the terms of which provide for all income to be paid to the decedent's surviving spouse but which continues in trust for the life of her son and further descendants until the Rule Against Perpetuities requires termination of the trust.

Dynasty trusts are often best utilized for families with closely held businesses that, if successful and sustained, may be able to provide benefits free of estate and generation-skipping transfer taxes for multiple future generations. A dynasty trust is so appealing in this scenario because of the ability to protect the business interests (and anything else transferred to and remaining in the trust) from estate tax and/or generation-skipping transfer tax in multiple generations. Of course, the transfer to the trust must be structured correctly, so that if a gift is made to the trust, generation-skipping transfer tax exemption is allocated to the trust to protect the full amount of the gift.

See the discussions of "Planning with Trusts" and "Understanding Developing Issues in Estate Planning" earlier in this chapter for a further discussion of the impact of the Internal Revenue Code and the New York estate tax laws on client planning strategies.

The Prudent Investor Act establishes fiduciary standards concerning risk and return objectives, diversification, total return (income and principal), inflation, deflation, and tax consequences that must be considered by a trustee when making investment decisions for a trust, unless exceptions are specifically dealt with through language in the trust document. Often

owners of closely held business interests and real estate, and wealthy individuals with alternative investment strategies, own assets that would not be proper for a trustee to hold under the Prudent Investor Act. A trust that will receive assets from such an individual should therefore contain provisions that permit the trustee to invest outside the bounds of the Prudent Investor Act. In addition, the Prudent Investor Act gives the trustee authority to delegate investment and management functions to third parties, and to exercise a power to adjust between trust principal and income if it would be fair and reasonable to all of the beneficiaries, so that current beneficiaries may be given such use of trust property as may be consistent with preservation of its value. These are important powers that make the use of trusts and their administration more flexible, and that give trustees more authority to make adjustments based on changes in the economy, in the tax laws, and in the lives of the trust beneficiaries.

The Optional Unitrust Provisions give a trustee, and the appropriate court, the power to substitute, for a mandatory income beneficiary of the trust, payment of a 4 percent unitrust amount for the payment of trust accounting income to such a beneficiary. This provision provides needed flexibility in situations where there may exist a conflict of interest between the current income beneficiary, who will normally want to maximize the production of income, and the remainder beneficiaries, who will normally want to maximize growth in the portfolio. By providing for a 4 percent unitrust payment in lieu of an income distribution, the trustee may invest the underlying portfolio primarily for growth without adversely affecting the cash flow of the income beneficiary (assuming that income would average approximately 4 percent of portfolio value over the term of the income beneficiary's interest in the trust, and assuming no substantial decline in the value of the underlying portfolio when invested for "growth"). A unitrust election works particularly well when a second spouse is the income beneficiary of a trust and children of a prior marriage are the remainder beneficiaries.

The ability to decant an irrevocable trust allows trustees the option to consider whether a trust needs revising and, if so, whether the use of the decanting statute is the best method to do so. Where "irrevocable" used to be thought of as inflexible, this statute allows a trustee with absolute discretionary distribution authority over an irrevocable trust to modify the

terms and conditions upon which the trust property is administered. The exercise of the power must not reduce a fixed income right of any beneficiary, and may be exercised only in favor of the "proper objects of the exercise of the power." Although this phrase is not defined in the statute, the trustee's decanting power under the statute is akin to a special power of appointment, and so the power of appointment rules provide insight to the meaning of "proper objects." The donee of a power of appointment may exercise the power only within the permitted class of beneficiaries. The trustees do not need to obtain consent from the settlor or the beneficiaries, and do not need court approval (although court approval may be desired if the trustee is concerned about whether the statutory prerequisites are met, or about potential claims by the beneficiaries).

A beneficiary may act as a sole trustee of his or her trust as a result of the amendments to the N.Y. EST. POWERS & TRUSTS LAW § 10-10.1, which allow a trustee to distribute principal or allocate income to himself or herself as a beneficiary of the trust, but only for his or her own health, education, maintenance, or support within the meaning of I.R.C. §§ 2041 and 2514 (West 2009). This provision allows a grantor to make a beneficiary the sole trustee of a trust, thereby reducing costs of administration of the trust while providing the beneficiary creditor protection and estate tax savings. This technique is gaining popularity as more spouses trust each other, and parents trusts their children, to each manage his or her own financial affairs.
See the discussion of the New York Power of Attorney Statute earlier in this chapter for a discussion of the impact of the new New York power of attorney rules on client planning strategies.

Alaska and Delaware trust laws provide asset protection to trust settlors, and the ability for trusts to hold assets "in perpetuity," neither of which are available to trusts established under New York law. Use of these trusts for estate freezing strategies that utilize the grantor trust rules, as discussed earlier, is especially effective.

Traditionally, trusts would often be drafted to provide the life beneficiary with a stream of income, and usually no principal, except as and when necessary, so as to preserve the principal for those who would inherit the trust property at the death of the life beneficiary (the "remaindermen"). While the wording remains the same, the concept of income has changed

over time, as has the basic investment philosophy on which the concept was based. It used to be the view of fiduciaries that maintaining the value of the initial trust principal was enough. But a trust invested to achieve such a goal will not protect the real value of the trust, taking into account the effect of taxes, expenses, and inflation. Acknowledging a newer approach to financial theory, the Prudent Investor Act endorses the use of "modern portfolio theory." This approach analyzes the appropriateness of an investment within the context of the trust investment portfolio as a whole, rather than from one beneficiary's perspective, and it allows the trustee to take into account the effect of taxes, expenses, and inflation on the trust's portfolio. However, a trustee has a duty of impartiality, so if the investment approach has changed to no longer favor the income beneficiary, other tools may be necessary to provide adequate options for distributions to the income beneficiary. One such tool is the power to reallocate or adjust trust receipts and expenses between principal and income. The power to adjust allows a trustee to invest for "total return" without worrying about generating what was traditionally categorized as income for the life income beneficiary. Another such tool is the power to convert to a unitrust, which allows the trustee to distribute to the income beneficiary a percentage of the fair market value of the trust principal. These tools provide the trustee with significant powers that did not exist under prior law. It is very important to include language in a trust agreement that protects the trustee if the trustee does exercise any of these powers, so long as the exercise is not in bad faith, grossly negligent, or in derogation of specific provisions of law or of the trust instrument.

Notwithstanding all the changes in the laws and in the tools available to clients and their fiduciaries, the basics still must be covered—who is to receive assets of the estate, what is the most efficient means to transfer the property, how can taxes be minimized, and are there unique circumstances, such as creditor protection for beneficiaries, or heirs with special needs, that should be considered? Each tool is not appropriate for every client. Fiduciaries have to actively manage trust assets to keep up with inflation, taxes, and expenses, and they need to be aware of the needs of the trust beneficiaries, to ensure that they are meeting their fiduciary obligations by making the right choices and allocations. It used to be that an individual who worked for a large corporation would have his or her retirement account fully invested in the corporation's stock, and would want his or her trustee to

maintain such investment in a trust for the children. Today, individual investors understand the importance of diversification, and the pitfalls often associated with being invested in only one stock. Similarly, fiduciaries know that prudent investing usually requires diversification. These factors all require an estate planning lawyer to understand clearly a client's goals, and to ensure that the client's trust agreement provides the right directions and flexibility to allow the client's trustees to meet these goals.

Maintenance of the Trust

Monitoring a trust is accomplished by using appropriate checklists and tickler systems, providing trust administration services to clients, notifying the trustees of their responsibilities, and scheduling meetings to review these responsibilities. Often the best fiduciary monitoring systems are simple tickler systems developed in-house or the appropriate use of a program such as Microsoft Outlook. Any such system requires that the relevant calendar information be entered at the start of trust administration, and that the appropriate staff, who are often paralegals, follow the ticklers. At the time a trust is established, and once a year thereafter, meetings with trustees are often helpful to make sure a trustee understands his or her responsibilities and is aware of them on an ongoing basis. Annual meetings also provide a trustee the opportunity to check in with beneficiaries, and to review trust investments to ensure they continue to be appropriate (assuming the type of trust investment does not require more frequent monitoring or that the trustee is not meeting more frequently with trust advisers to whom such function has been delegated). Even investments in life insurance need to be reviewed, by ordering inforce ledgers, as some insurance policies may "blow up" or may become too expensive if not analyzed, remedied, or replaced in a timely fashion.

The following items, among others, must be monitored during the existence of a trust:

- Implementation of, and periodic adjustments to, an investment policy statement
- Compliance with provisions of the Prudent Investor Act, as applicable
- Premium payments if the trust holds insurance policies

- Crummey notices if contributions are being made to the trust on an ongoing basis
- Investment results and investment strategies
- Periodic reallocation within investment classes in accordance with the investment policy statement
- Mandatory periodic distributions of income and principal
- Consideration of discretionary distributions of income and principal
- Quarterly estimated tax payments
- Filing of fiduciary income tax returns and the payment of taxes
- Preparation of an annual accounting, if required or appropriate
- Annual review of insurance policies owned by the trust
- Consideration of exercising the power to adjust
- Consideration of electing unitrust treatment

I meet with clients to update the plan every five to seven years, unless there is a major change in the tax laws or in the laws that affect other aspects of planning, such as the new statute governing powers of attorney. I will meet with clients earlier if there is a change in circumstances, such as a death in the family, a serious or debilitating illness, the birth of a child or grandchild, a change in employment, retirement, a marriage, a divorce, or a change in economic status through inheritance, market conditions, or otherwise.

Each of these factors is an indicator that the estate plan should be reviewed and possibly changed. If appropriate changes are not made, the plan may fail to properly carry out the client's wishes, may result in lapsed legacies (to deceased beneficiaries), improper beneficiaries (former spouses), outright distributions that should have been in trust (distributions to minors), election against the will (failure to provide the current spouse with an amount at least equal to the elective share), increased taxes (failure to properly utilize tax credits and exemptions), and will contests.

Challenges, Pitfalls, and Common Mistakes

Challenges

The most challenging elements of trust and estate practice in New York are the fact that there is a state estate tax, that the rate of tax is high, and that

the state estate tax is decoupled from the federal estate tax. Under the Tax Relief Reconciliation Act of 2001, the credit for state death taxes available to offset the federal estate tax under I.R.C. § 2011 (West 2009) (the "federal credit") was phased out. Effective beginning in 2005, the federal credit was replaced with a deduction for state death taxes paid. Under the old law, it made sense for states to "couple" with the federal law, and to make the amount of the state estate tax equal (and in some cases, such as in New York, exceed) the federal credit for state death taxes. For the decedent, this meant that part of the tax that would have been paid anyway as a federal estate tax was instead paid to the state or states imposing a state tax equal to the federal credit. Under the new law, there are a number of states, including New York, that are "decoupled," that is, their state estate tax laws do not conform to the federal estate tax law. While some states initially did away with their state estate tax altogether, other decoupled states froze the applicable exclusion amount at the level in effect under the Code for the year to which the state law is tied. The New York state estate tax is determined by taking into account the federal exemption amount that was in effect in 2001, that is, $1 million. As discussed earlier, the difference in the federal and state exemption amounts requires careful planning to ensure tax minimization.

In addition to the fact that the estate tax burden is high on New Yorkers, the decoupled estate tax and the high rate of tax requires married taxpayers to make a choice when funding a credit shelter trust. Should the full $3.5 million federal exemption be funded, resulting in a $229,200 New York estate tax, or should a smaller amount be funded, so that the New York estate tax on the first death can be reduced or eliminated? The reduction in the amount in the credit shelter trust will dollar for dollar increase the size of the surviving spouse's estate. Will this increase be enough to cause the surviving spouse to incur significant additional federal and state estate taxes? What if the surviving spouse moves to a state, such as Florida, that has no state estate tax?

Avoiding Pitfalls

A poorly drafted trust will result in litigation, unnecessary and unplanned-for income, estate and generation-skipping transfer taxes, distributions to the wrong beneficiaries, litigation among fiduciaries and beneficiaries

regarding trust terminology or a fiduciary's elections, legal and accounting fees, court supervision, removal of trustees, and possible claims for attorney malpractice. Those most impacted are the settlor, if alive, and the settlor's intended beneficiaries.

While court proceedings, renunciations, or use of a decanting statute may allow trustees and beneficiaries the opportunity to fix certain mistakes in trusts, it is obviously better to avoid the mistakes when drafting.

The first step to take when drafting a trust is to ensure that you capture the settlor's intentions in the trust agreement. Does the settlor want the trustee to have unlimited discretion to make distributions, or does the settlor want distributions to be made only after the trustee evaluates the beneficiary's other resources? Does the settlor want to provide for luxuries, or does the settlor think that providing funds for a lavish lifestyle will deprive a beneficiary of an important part of life's journey? Having these discussions with a client at the drafting stage will inform the provisions of the trust.

Next, it is important for the drafter to understand the law, including recent developments in the law, so that the trust contains the administrative and tax provisions necessary and desirable for the client's wishes to be carried out, and so proper consideration is given to all potential income, estate, and generation-skipping transfer tax issues. For example, if the trust is to continue for multiple generations, does the trust agreement have a flexible provision that allows the trustee to select whether property should be included in a beneficiary's estate, thereby utilizing the beneficiary's own exemption amount and possibly increasing the beneficiary's own estate tax, or instead bypass the beneficiary's estate, thereby causing there to be a possible later-assessed generation-skipping transfer tax?

Keeping current on changes in the law allows the drafter to ensure that his or her documents adjust to the current law in a way that clearly reflects the client's intentions. For example, an instrument that creates a pre-residuary credit shelter bequest funded to the maximum federal exemption, and which is for the benefit of the decedent's children, without expressing any direction regarding the funding of the marital share, may result in a decedent passing all of his or her property to the children, and leaving nothing for the surviving spouse. Given the increase in the credit shelter

amount over the last decade, it is possible that clients who intended to pass $650,000 to their children at the first death are allowing $3.5 million to bypass the surviving spouse and go directly to the next generation.

Similarly, the standard provisions may be fine for most beneficiaries and trustees, but will not work in all situations. As an example, assume that the attorney usually provides for a trustee of a child's trust to have full discretion to make principal distributions without reference to a standard. This is fine for most clients, as someone other than the beneficiary is usually appointed trustee. But what happens if a client appoints a child to act as co-trustee of his or her own trust, and the trust does not have a provision for appointment of a successor trustee? The client dies, and the independent co-trustee becomes incapacitated. If the trust does not include ascertainable standards or appoint a trust protector to consent to principal distributions, the entire trust will be included in the child's estate and will be available to the child's creditors, unless the child goes to court to have a successor co-trustee appointed.

Common Mistakes

It is imperative for the drafter to pay close attention to the terminology and phrasing in the trust document, to make sure that appropriate language is used. If the client wishes to allow a fiduciary to act without bond, the client probably intends for all fiduciaries acting under the trust agreement to be exempted from such requirement. If the drafter uses the phrase "appointed hereunder" rather than "acting hereunder" when referring to the trustees who are so exempted, any successor trustees who are not appointed by the settlor will be required to obtain a bond, an additional unintended trust expense. Or if a drafter copies a trustee resignation provision from a will to a revocable trust, and forgets to delete a requirement that a trustee resignation be filed with a court, the drafter may have subjected the trust to unintended court supervision, and the additional costs related thereto.

Perhaps the most serious and damaging results that may result from poor drafting are when the beneficiaries are incorrectly identified, or the property is not divided as the client intended. The incorrect use of common terms such as *per stirpes* and *per capita* may lead to unnecessary litigation. So what happens if a drafter provides for a disposition "to my then living children, in equal shares, per stirpes" rather than "to my then living issue, in equal shares, per

stirpes"? It is difficult to understand the intent of the first phrase, in particular if a child has died and leaves living issue. The N.Y. EST. POWERS & TRUSTS LAW § 1-2.14 (West 2009) provides that a *per stirpes* disposition of property is made by dividing such property into as many equal shares as there are (i) surviving issue in the generation nearest to the deceased ancestor that contains one or more surviving issue, and (ii) deceased issue in the same generation who left surviving issue, if any. Alternatively, individuals may take *per capita*, which is defined under the N.Y. EST. POWERS & TRUSTS LAW § 1-2.11 (West 2009) to mean that each individual is to take in his or her own right an equal portion of property. Does the unfortunate reference to "living children" mean that the issue of the deceased child are not included in the intended class of beneficiaries, and that only living children are to inherit? The issue of the deceased child would have taken such deceased child's share had the disposition been correctly stated as being "to my then living issue, in equal shares, per stirpes."

Another example of a simple but dangerous drafting error is when reference is made to the date on which property may be divided among living issue. This error may occur if the drafter is transferring language from a single person's will to that of a married client. In a typical situation, married clients might leave everything to each other in trust, and at the death of the survivor intend to divide their property among their then living children. However, what happens if the dispositive provision refers to a child who is living at "my" death, instead of correctly referring to a child who is living at the "survivor's" death? Does this mean a share should be set apart for a child who was living at the first death but who predeceases the second death? Such a drafting error may result in expensive and harmful litigation, which could easily be avoided by more careful review of the documents before they are signed.

Wills and trusts also need to provide adequate direction to the fiduciaries. What may be a harmless oversight in most situations may cause litigation and strife in others. For example, if the credit shelter and marital trust are created to benefit the surviving spouse, does the document direct that the assets in the marital trust be depleted first before use of the assets of the credit shelter trust? What if the spouses each have children from former marriages. Should the surviving spouse be given a limited power of appointment over the marital trust or credit shelter trust, giving the spouse the ability to alter who will be the remainder beneficiaries of such

trust? Does the predeceased spouse want the surviving spouse to have the power to alter how the predeceased spouse's property will be disposed of at the survivor's death?

Lastly, especially if property may be held in trust for multiple generations, it is necessary for a trust to contain flexible provisions that will allow the trustees to adapt the trust to changing circumstances of the beneficiaries and to changing tax and estate laws.

Avoiding Future Mistakes

It is vital for attorneys involved in estate planning to take steps to avoid the common pitfalls and serious mistakes of estate planning, many of which have been described in this section. Understanding a client's intentions, and setting up a good interview process to do so, is an important first step. Using an estate planning questionnaire, and sending draft documents to the client along with a clear and precise written explanation of the documents, help ensure that the client will understand them. In addition, it is important for an attorney to have good forms that have been vetted by the attorney's peers, whether in or outside of the firm; to read journals, cases, rulings, and articles and attend continuing legal education programs designed to provide current updates and developments; to discuss the design of the estate plan with others in the firm; and always to have at least two lawyers review all documents.

If an attorney's practice is in a firm, there will always be daily dialogue among the estate planning attorneys, paralegals, and staff. Monthly or other periodic meetings should be scheduled for the entire trusts and estates group. At these meetings, tasks should be assigned relating to updating forms, reviewing changes in the law, and assessing procedures. Finally, docket lists and spreadsheets should be maintained of all trusts and estates administered by the firm. Following these steps will help create, maintain, and grow a vibrant estate planning, trust administration, and estate administration practice.

Conclusion

There will always be work for estate planners in New York. I believe there will always be a New York estate tax to plan for. In addition, New York will likely

be in the forefront of changes in rules that are proposed by national groups dealing with developments in trust and estate practice. For example, same-sex clients may use the estate tax marital deduction as an avenue to advance the agenda for legalizing same-sex marriage. If this were to occur, I would have more planning tools available for same-sex couples.

Current proposed changes in the federal estate tax include the possibility of establishing "portability" of the estate tax exemption. Portability of the estate tax exemption means that when the first spouse dies, his or her unused exemption would simply transfer to the surviving spouse, and the surviving spouse would be able to use it along with his or her own federal exemption amount. Portability would effectively create (extrapolating from the 2009 federal exemption of $3.5 million) a $7 million federal estate tax exemption for married couples. While such a law would reduce or eliminate the necessity of transferring assets to avoid federal estate tax, there still would be much to plan for, as there is no indication that New York will adopt portability, and other issues, including creditor protection, would remain as important planning objectives. In addition, no changes appear to be on the horizon for the lifetime gift tax exemption of $1 million, so lifetime planning will remain important and necessary for many clients.

The economy will have some impact on this practice area. Some individuals may put off planning in weak economic times, because of the costs. If the federal exemption amount remains at $3.5 million, a weak economy and low market values will allow more individuals to pass property to their heirs free of federal estate tax, and this will impact the sophistication of the planning I do, the fees that are derived from that planning, and the fees for estate administration that come from preparing and filing the federal estate tax return.

My advice to trust and estate lawyers in New York is to stay current with changes in the law, recent cases and rulings, and articles related to your specific areas of expertise. Make sure the forms for your estate planning documents are continually updated, to take into account changes in the law and best practices. Communicate law changes to your clients. I do this by personalized letters, e-mail blasts, seminars, and Web site updates. Remember that each client is unique and a cookie-cutter approach to implementing a plan will usually miss something of importance to the client. Listen to what your clients are telling you and what they may not be telling you. If at the beginning of a client

interview the client says she trusts her children implicitly, but by the end of the meeting, she does not want any of her children acting as her trustees, a child may not be an appropriate agent under the client's power of attorney. If you send a client draft estate planning documents, and he does not come in to execute them, it may be because he has not told you what he really wants to do with his property. Often the information clients need to provide you is extremely personal, and it is our job to make clients feel comfortable doing so. For some clients, this is something that may need to be developed over time. Eliminate potential mistakes by having someone else proofread your documents for errors, and to make sure the documents carry out the plan you designed for the client. Keep detailed notes or memoranda of your client interviews and of the plan you have designed.

Following this advice cannot fail to improve skills and outcomes. It will ensure that you are current with developments in the law, that you have incorporated these developments into your estate planning strategies and documents, and that you have done your utmost to design and implement a plan that achieves your client's goals.

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Acknowledgment: *I would like to acknowledge the invaluable contributions of Kim V. Heyman, an associate attorney at Green & Seifter, Attorneys, PLLC, to the research, writing, and development of this chapter.*

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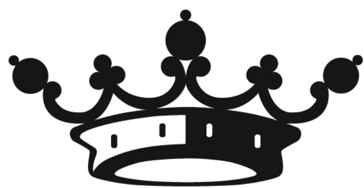

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