

Exploring the New Uniform Power of Attorney Act
04/28/05 10:15am – 12:15 am

Non-client beneficiary has right of action against the attorney who drafted the estate plan depending on the facts as weighted in a balancing test.

Watkins Trust v. Lacosta, 321 Mont. 432, 92 P. 3d 620 (2004).

Plaintiffs brought suit against attorney to recover damages caused by the attorney's alleged malpractice in drafting the estate plan of decedent. The decedent, Stanley Watkins, and his stepson had interests in the family business. The decedent's wife, Carolyn Watkins, contacted an attorney to draft their estate plan as well as partnership/shareholders agreements for the business. In January 1992 Stanley and Carolyn Watkins executed and fully funded a Revocable Trust of which they both served as Co-Trustee. Since Stanley suffered from poor health, the attorney neither met with nor consulted with him. In addition, contrary to the attestations in the wills, the documents were signed outside of the presence of the purported witnesses and a notary public.

In April 1992 Stanley died and his will was admitted to probate. The drafting attorney did not disclose to the surviving spouse or to the court that the will was improperly executed. Also, the drafting attorney did not disclose to the surviving spouse, Carolyn, that when Stanley died, the Trust became irrevocable. In January 1995 Carolyn discovered that the trust was a QTIP trust, and the trust provisions which directed her deceased husband's interests in the family business to their son were irrevocable. In August 1995 the drafting attorney met with the surviving members of decedent's family, but she gave no indication of any flaws in the validity of the trust or will. In December 1995 an independent attorney reviewed the documents and disclosed the attestation defects in the will and the irrevocability of the trust provisions. In February 1997 the surviving spouse died and appellants (Trust and decedent's stepson in both his individual capacity and as Personal Representative of the Estate) sued attorney for malpractice.

The issue was whether the Appellants (non-client beneficiaries of the Estate and Trust) had standing to bring suit against the drafting attorney.

Decedent's stepson sought standing as a non-client beneficiary of the estate. The Montana Supreme Court noted that the majority rule in other jurisdictions supports the rule that named beneficiaries have standing against attorneys drafting wills because creating the benefit is the mutual intent of the attorney and client. The court adopted a multi-factor balancing test to determine whether there was a duty owed by attorneys to non-client beneficiaries. The Court held that the Estate does have standing to sue the drafting attorney, and it remanded the factual issue of whether the Trust and decedent's stepson (individually and as Personal Representative of the Estate) had standing to be determined at trial.

Posthumously conceived children are entitled to Social Security death benefits provided they are legitimate children under state law.

Gillett-Netting v. Barnhart, 371 F.3d 593 (9th Cir. 2004).

In December 1994 decedent was diagnosed with cancer and deposited his sperm for storage and future use in in-vitro fertilization procedures. Decedent died in February 1995. In-vitro fertilization was successful in December 1995 and two children were born in August 1996.

Mother applied for Social Security child's insurance benefits based on her deceased husband's earnings. The Social Security Administration denied the benefits claim. An Administrative Law Judge upheld the denial of benefits reasoning that under the Social Security Act a child is entitled to benefits if the child was dependent on the insured wage earner at the time of death. Since the children were not in existence at the time of the insured's death, they are unable to establish actual dependency. The District court affirmed, and the Plaintiff appealed to the Ninth Circuit Court of Appeals.

The Ninth Circuit Court reversed the lower court's findings arguing that neither federal nor Arizona state law had addressed the specific issue of a posthumously conceived child's right to insurance benefits. The Ninth Circuit Court argued that although the children may not be actually dependent on the insured, they may be deemed statutorily dependent if they are determined to be the insured's legitimate children. Even though the children were conceived using in-vitro fertilization after the death of the insured, it was undisputed that the insured was their biological father and married to their mother. Under Arizona law all children—not excluding posthumously conceived children—are considered the legitimate children of their natural parents. Since the children qualify as legitimate children under Arizona law, they are deemed dependent, thus, eligible for survivor benefits.

Arbitration clause is not binding on trust beneficiaries. Although the inter vivos trusts contained an arbitration clause, an Arizona statute enforcing arbitration provisions was inapplicable because trust was not a written contract.

Schoneberger v. Oelze, 208 Ariz. 591, 93 P.3d 1078 (Ariz. App. Div. 1 2004).

Plaintiffs are the daughters of defendants. In January 1991 the defendants created three irrevocable inter vivos trusts, and each daughter was named as sole beneficiary of one of these trusts and a co-beneficiary of the family trust. Each trust contained an arbitration provision governing any dispute arising between Trustee and Beneficiary. In 2002 the daughters filed suit against the Trustee of their respective trusts and the Co-Trustees of their family trust claiming breach of trust, conversion and fraudulent concealment.

The issue presented before the court was whether the arbitration provision in the trust document could be enforced against the trust beneficiaries. Under Arizona statute (A.R.S. § 12-1501) "a provision in a written contract to submit to arbitration any controversy thereafter arising between the parties is valid, enforceable and irrevocable..." Defendants argued that the arbitration clauses were within the statute, thus requiring the beneficiaries to submit to arbitration. Plaintiffs

countered that the trusts did not qualify as a "written contract," so the trust and its beneficiaries were exempt from statutory enforcement of arbitration.

The Arizona Court of Appeals ruled that the arbitration clause was not enforceable against the trust beneficiaries noting that arbitration is a creature of contract law. Drawing upon the fundamental differences between a trust and a contract, the Court reasoned that a trust relationship does not involve assent to a mutual exchange of promises, and the fiduciary relationship between Grantor and Trustee does not qualify as contractual. Since the trust beneficiaries were not contractually bound to arbitrate their disputes, the arbitration clauses in the trust document were not enforceable under Arizona statute and inapplicable to the trust beneficiaries.

Arbitration agreement between trustees and broker does not bind income beneficiary.

Morgan Stanley DW Inc. v. Halliday, 873 So.2d 400 (Fla. Ct.App. 4 Dist. 2004)

The lifetime beneficiary of a QTIP trust sued both her trustees (who were also the remainder beneficiaries of the trust) and the broker with whom the trustees had a customer account agreement alleging mismanagement of the trust assets. The broker moved to compel the income beneficiary to arbitrate in conformity with the customer account agreement arguing that the income beneficiary was a third-party beneficiary of the customer agreement or that the trustees acted as the income beneficiary's agent in agreeing to the arbitration provision.

The trial court dismissed the motion to compel arbitration rejecting both arguments and the Florida District Court of Appeal for the Fourth District affirmed. The court disposed of the third party beneficiary argument by observing that it was clear that the customer account agreement was not made primarily for the income beneficiary's benefit nor did it express an intent to primarily or directly benefit the income beneficiary. The agency theory fared no better. Trustees cannot avoid responsibility for negligent performance of their duties by delegating those duties. In addition, the agreement was made primarily for the trustees' benefit. Finally, the income beneficiary clearly never agreed to the arbitration clause. The court finally opined that the agreement was entered into primarily for the benefit of the trustees perhaps to allow them to avoid responsibility for mismanagement. The court's hostility to the arbitration provision as applied to the income beneficiary is obvious.

Child support claim against the putative father's estate one year after its closing is untimely being subject to probate statute of limitations.

Fazilat v. Feldstein, 180 N.J. 74, 848 A.2d 761 (2004).

In 1992 the plaintiff, Fazilat, began an intimate relationship with Feldstein, a married man. In 1995 Fazilat became pregnant and informed Feldstein that he was the father. In June 1996 a child, Elisabeth, was born and Feldstein was listed as the father on the birth certificate. Feldstein provided support for Elisabeth prior to his death in December 1996 and informed Fazilat that he would not differentiate between Elisabeth and his other children. Feldstein's will was probated in December 1996 and made no provision for any of his children including Elisabeth. Pursuant to the terms of the will Feldstein's entire estate passed to his wife, and his estate was closed in late 1997. In October 2000 Fazilat filed a complaint against Feldstein's estate for paternity and child support. The trial court dismissed the complaint on the grounds that the claim was untimely since it was filed six months after the probate period of limitations. The Appellate Court affirmed the trial court's findings.

The New Jersey Supreme Court considered the question of whether the natural mother and her daughter could pursue an action for paternity and child support against the estate of her putative father. On the one hand, the Court cited the New Jersey Parentage Act under which parentage claims are required to be presented within five years after the claimant reaches the age of majority. However, parentage claims do not expire upon the death of the father and may be presented against the decedent's estate. On the other hand, the Court cited the Probate Code which mandates that claims against an estate must be presented within six months after letters testamentary have been granted or at any time before all estate assets have been distributed. Thus, although a parentage claim can survive the death of a putative father, a parentage claim cannot extend the statute of limitations governing the administration of a decedent's estate. The Supreme Court noted that the limitations period under the Parentage Act and the Probate Code are mutually independent. Even though the paternity claim against the Estate is permitted, the Supreme Court denied the child support claim against the estate since it was filed after the probate limitations period had ended.

Trusts are governed by the law in effect at the time of creation. Since adopted persons were not considered lineal descendants terms at the time of its creation, they do not qualify as "direct lineal descendants."

McGehee v. Edwards, 268 Va. 15, 597 S.E.2d 99 (2004).

Between 1929 and 1931 the children of Dr. and Mrs. Montfort Jones established 11 inter vivos trusts (Jones Family Trusts) benefiting a class of approximately 142 beneficiaries. These beneficiaries were described in the trust terms as the "direct lineal descendants" of Grantor's parents, Grantor's brothers and sisters, or Grantor's named sons. In January 2000 the Trustees of the Jones Family Trusts filed a complaint for a judicial determination of whether children born out-of-wedlock qualified as "direct lineal descendants." A defendant-beneficiary filed an answer which included a request that the court also determine whether the class description included the adopted children of "direct lineal descendants." The trial court ruled that persons adopted by "direct lineal descendants" were considered issue or descendants, so they were included in the

class descriptions of the Jones Family Trusts. Six defendant-beneficiaries appealed, and the Virginia Supreme Court granted the appeal.

Although current Virginia statute presumptively includes adopted persons as "issue" or "descendants", the Supreme Court ruled that the grantor's intent must be construed at the time at which the instrument was executed circa 1930. At common law adopted children were not included in the class of "direct lineal descendants" unless the trust instrument specifically expressed such intent. Current statute which defines adopted persons as "issue" or "descendants" may apply to wills but it does not apply to trusts executed prior to 1978.

Trustee held liable for failing to inform beneficiary of drafting error in trust document.

Hatleberg v. Norwest Bank Wisconsin, 271 Wis.2d 225, 678 N.W.2d 302 (Wis.Ct.App. 2004), review granted, 275 Wis.2d 295, 687 N.W.2d 522 (2004)

A bank trust officer contacted a potential client and offered estate and investment planning services. The offer was accepted as was the bank officer's suggestion that the client create an irrevocable trust through which the client could take advantage of the present interest exclusion to reduce her taxable estate while providing for her grandchildren's education. The trust was drafted by a lawyer selected by the client. The trust officer knew that the lawyer was not an expert on trusts.

The trust as drafted did not contain a Crummey power and therefore the grantor's contributions to the trust did not qualify for the present interest exclusion. Three years after the trust was created the trust officer contacted the lawyer suggesting that the trust be modified to add a Crummey power, but the trust officer did not contact the grantor or the beneficiaries and nothing was done. Because the gifts totaling \$440,000 did not qualify for the present interest exclusion they were adjusted taxable gifts and caused an additional \$173,644 in estate taxes.

The intermediate Wisconsin appellate court affirmed a judgment for the personal representative of the decedent's estate. The court held that the bank breached a duty to the grantor because of the "peculiar facts" of the case. The bank solicited the client's business, represented that it had expertise in estate planning, and continued to tell the client that gifts to the trust would reduce the client's estate tax even after the bank was aware of the omission of the Crummey power and the failure to remedy the omission. In addition, notice to the attorney who drafted the trust was unavailing since the attorney did not represent the grantor when the notice was given.

The bank argued that the statute of limitations started to run when the trust officer notified the drafter of the error, but as already noted, the drafter no longer represented the grantor and was not the grantor's agent. The statute of limitations therefore began to run at the grantor's death and the suit was timely. Finally, public policy is not contravened by holding the bank liable given its solicitation of business and its representation of expert knowledge.

Once trust income tax eliminated; situs may not be changed.

In re Application of Chase Manhattan Bank, 2 Misc.3d 554, 773 N.Y.S.2d 529 (Sur. Ct. New York County, 2003); *In re Bush*, 2 Misc. 3d 744, 774 N.Y.S.2d 298 (Sur. Ct. New York County, 2003)

Under New York Tax Law 605(b)(3)(D) a New York resident trust consisting of intangible property will not be subject to taxation if all of the trustees are domiciled outside of New York. In two cases the New York County Surrogates have approved the resignation of a New York trust company as trustee and its replacement by the Delaware affiliate of the same bank, thus preventing the trusts from being subject to New York State fiduciary income tax. In both cases, however, the Surrogates refused to allow a change of situs to Delaware. In neither case were there any benefits to be gained by a change of situs, the elimination of the fiduciary income tax having been accomplished by the appointment of an out-of-state trustee.

Equitable distribution reward takes precedence over creditors' claims.

Painter-Jamieson v. Painter, 163 N.C.App. 527, 594 S.E.2d 217 (2004)

At decedent's death the equitable distribution award made to his ex-wife as part of their divorce proceedings had not been paid. The decedent's personal representative refused to pay the award maintaining that the ex-spouse was a creditor of the estate to the extent of the award and therefore could only be paid after payment was made to creditors with a higher priority. Were that the case, the ex-spouse would receive nothing, the decedent's estate having been consumed by federal taxes. The trial court ruled for the ex-spouse and the personal representative appealed.

Because the North Carolina statutes were silent on the relationship between an equitable distribution award and creditor claims, the North Carolina Court of Appeals resolved the appeal by examining the two statutory schemes and the policy issues involved. The statutory scheme for administering estates applies only to the decedent's property. The policy behind equitable distribution is the idea of marriage as an economic partnership. Equitable distribution recognizes that marital property is a form of common ownership. To allow property awarded to a former spouse under equitable distribution to be subject to the debts and expenses of the estate of the deceased former spouse would be to pay claims against the decedent's estate with property belonging to someone else. Given this analysis, the court easily affirmed the trial court's order that the personal representative pay the equitable distribution award to the ex-spouse.

The Court noted, however, that recent amendments to the relevant statutes made the statutory scheme for paying estate creditors applicable to claims for equitable distribution against a deceased spouse. (N.C. Gen.Stat. § 50-20(I)(2)). The amendments do not apply to the instant case, however, because they are not expressly applicable to actions pending at the time the amendments became law and in any event the ex-spouse's rights had vested and were immune from change by subsequent legislation.

Consent of principal to transaction by attorney-in-fact under durable power of attorney not vitiated by subsequent incapacity.

In re Estate of Cummin, 258 Mich.App. 402, 671 N.W.2d 165 (2004)

Decedent executed a durable power of attorney giving her daughter as attorney-in-fact authority to lease, sell, assign, and convey interests in real property owned by the decedent on whatever terms the attorney-in-fact might decide. Sixteen months after executing the power of attorney decedent moved into a residential care facility where she remained until her death five years later. Within two years of the move the decedent's mental condition had deteriorated to the point where she occasionally would fail to recognize family members.

Approximately two years after decedent moved into the care facility, daughter conveyed the decedent's real property to herself, retaining a life estate for decedent. Daughter rented the property and collected the rents and finally sold the property after decedent's death. Decedent's son who along with daughter was a beneficiary of decedent's estate, sued his sister alleging conversion of the estate's assets, demanding an accounting, and requesting the imposition of a constructive trust on the decedent's property including the proceeds of the sale or rental of the real property. The Probate Court imposed a constructive trust on daughter in favor of decedent's estate.

The Michigan statute in effect at the time the case was brought, the Estates and Protected Individuals Code (M.C.L. § 700.1101 *et seq.* and specifically § 700.1214), prohibits a fiduciary from engaging in a transaction with an estate the fiduciary represents unless the governing instrument expressly authorizes such a transaction. The court, over a dissent, held that the statute did not apply because the daughter's "accrued rights" as owner of the property would be impaired by invalidating the transaction under the statute enacted after the transaction. The statute in effect at the time of the transaction also prohibited self-dealing by fiduciaries but did not include attorneys-in-fact in the statutory definition of fiduciary.

Under the common law, the agent owes the principal a common-law fiduciary duty which prohibits the attorney-in-fact as an agent from engaging in a transaction with the principal unless the principal consents after full disclosure of the details of the transaction. Daughter and her husband testified that the decedent repeatedly instructed daughter to transfer the decedent's real estate to daughter, retaining a life estate for decedent. So long as consent to the transaction was given while the decedent was competent it is irrelevant that the transaction might have occurred after the decedent became incompetent. In addition, the daughter's authority to convey real estate was sufficient to authorize a gift of the real estate. Because it was not evident from the record that the probate court determined whether or not the decedent had freely consented to the conveyance of the real property the case was remanded.

Scott W. Lamb, Asheville, North Carolina

B.A. - University of North Carolina-Chapel Hill, M.A. - Wake Forest University,

J.D. - American University

Memberships: North Carolina Bar Association, American Bar Association, Land-of-Sky Estate Planning Council, Chartered Financial Analyst Institute

Honors: 2004-2006 Fellow for Real Property, Probate and Trust Section of the ABA.

Publications: "Applicable Exclusion + Unlimited Marital Deduction = Basic Estate Planning for Spouses," *The Will and The Way* published by the North Carolina Bar Association (Vol. 23, No. 3, June 2004); *Lawyers Weekly*, June 7, 2004.

William P. LaPiana is the Rita and Joseph Solomon Professor of Wills, Trusts and Estates at New York Law School and Director of Estate Planning for the Graduate Tax Program at NYLS. He is a graduate of The Nichols School, Buffalo, New York, and holds the A.B., summa cum laude (1973), the A.M. in history (1975), the J.D. cum laude (1978), and the Ph.D. in history (1987) from Harvard University. From 1979 to 1983 he was associated with Davis Polk and Wardwell where he worked primarily in the estates group. He began teaching in 1983 at the University of Pittsburgh School of Law and joined the New York Law School faculty in 1987. His teaching responsibilities include wills and trusts, property, federal estate and gift tax, estate planning, and American legal history. Prof. LaPiana is the author of several articles on estate planning and a co-author of *Disclaimers in Estate Planning: A Guide to their Effective Use* and of the third edition of *New York Wills and Trusts* and its annual supplements and has contributed to Klipstein and Bloom, *Drafting New York Wills*. In 1992 he was elected an Academic Fellow of the American College of Trust and Estate Counsel and in 1998 was elected to membership in the American Law Institute. He was the Reporter for the revised Uniform Disclaimer of Property Interests Act, which was promulgated by the National Conference of Commissioners on Uniform State Laws in July 1999. He is currently a member of the Supervisory Council of the Real Property Probate and Trust Section of the American Bar Association and is the American Bar Association advisor to the Drafting Committee for the Revised Uniform Durable Power of Attorney Act, another NCCUSL project. In 2003 he lectured at the 37th annual Heckerling Institute on Estate Planning. He has also written numerous articles in American legal history, and is the author of *Logic and Experience: The Origin of Modern American Legal Education* (Oxford Univ. Press, 1994). He currently serves on the Board of Directors of the American Society for Legal History.