

University of Kentucky

UKnowledge

---

Continuing Legal Education Materials

Kentucky Legal History

---

7-2002

## The Essential Toolbox for the Estate & Trust Lawyer

Office of Continuing Legal Education at the University of Kentucky College of Law

Follow this and additional works at: [https://uknowledge.uky.edu/uky\\_cle](https://uknowledge.uky.edu/uky_cle)



Part of the [Estates and Trusts Commons](#)

**Right click to open a feedback form in a new tab to let us know how this document benefits you.**

---

### Repository Citation

Office of Continuing Legal Education at the University of Kentucky College of Law, "The Essential Toolbox for the Estate & Trust Lawyer" (2002). *Continuing Legal Education Materials*. 47.

[https://uknowledge.uky.edu/uky\\_cle/47](https://uknowledge.uky.edu/uky_cle/47)

This Book is brought to you for free and open access by the Kentucky Legal History at UKnowledge. It has been accepted for inclusion in Continuing Legal Education Materials by an authorized administrator of UKnowledge. For more information, please contact [UKnowledge@lsv.uky.edu](mailto:UKnowledge@lsv.uky.edu).

**UK  
CLE**

---

**THE ESSENTIAL  
TOOLBOX  
FOR THE  
ESTATE & TRUST  
LAWYER**

**July 2002**



Written materials and oral presentations offered through the University of Kentucky College of Law Office of Continuing Legal Education (UK/CLE) are designed to assist lawyers in maintaining their professional competence. The Office of Continuing Legal Education and its volunteer speakers and writers are not rendering legal or other professional services by their participation in continuing legal education activities. Attorneys and others using information obtained from UK/CLE publications or seminars must also fully research original and current sources of authority to properly serve their or their client's legal interests. The forms and sample documents contained in our continuing legal education publications are intended for use only in conjunction with the professional services and advice of licensed attorneys. All parties must cautiously consider whether a particular form or document is suited to specific needs. The legal research presented herein is believed to be accurate, but is not warranted to be so. These written materials and the comments of speakers in presentation of these materials may contain expressions of opinion which do not necessarily reflect the views of the Office of Continuing Legal Education, the University of Kentucky, the Commonwealth of Kentucky, or other governmental authorities. UK/CLE strives to make its written materials and speaker presentations gender-neutral; however, gender-specific references may remain where it would otherwise be awkward or unclear. It should be understood that in such references the female includes the male, and vice-versa.

Copyright 2002 by the University of Kentucky College of Law,  
Office of Continuing Legal Education.  
All rights reserved.

Printed in the United States of America





ABOUT...

# UK CLE

---

The University of Kentucky College of Law, Office of Continuing Legal Education (UK/CLE) was organized in 1973 as the first permanently staffed, full-time continuing legal education program in the Commonwealth of Kentucky. It endures with the threefold purpose to: 1) assist lawyers in keeping abreast of changes in the law; 2) develop and sustain practical lawyering skills; and 3) maintain a high degree of professionalism in the practice of law. Revenues from seminar registrations and publication sales allow the Office to operate as a separately budgeted, self-supporting program of the College. No tax dollars, bar dues or public funds are budgeted in the Office's finances.

## **Courses**

UK/CLE provides a variety of workshops, conferences, and institutes to satisfy the continuing education needs of lawyers and other professionals. Courses range from half-day programs in selected areas to in-depth programs extending over several days. While most courses are conducted at the College of Law in Lexington, UK/CLE has a longstanding statewide commitment. Since its first year of operation, beginning with a criminal law program in Madisonville, Kentucky, the Office has continued to bring the highest quality continuing education to attorneys across Kentucky, the Midsouth, the Midwest, and the nation.

## **Publications**

Each course is accompanied by extensive speaker-prepared course materials. These bound materials are offered for sale following courses and are consistently regarded as valuable, affordable references for lawyers. In 1987, UK/CLE began producing a series of publications which now consist of Practice Handbooks, Monographs, and Compendiums. Each Practice Handbook is an extensively referenced, fully indexed practice guide consisting of separately authored chapters, sequenced for the comprehensive coverage of a distinct body of law. Their format allows for updating through supplements and cumulative indexes. Each Monograph is a concisely written practice guide, usually prepared by a single author, designed to cover a topic of narrower scope than Practice Handbooks. Compendiums contain both official forms and sample documents. Designed to assist the lawyer by suggesting specific structures and language to consider in drafting documents, these publications are beneficial in the resolution of legal drafting concerns. The Compendiums are often used most effectively in conjunction with UK/CLE Practice Handbooks and Monographs.

## **Professional Management**

UK/CLE serves the needs of the bar from its offices on the University of Kentucky campus in Lexington. Its staff manages course planning, publication content planning, course registrations, publications sales, course and publication marketing, publication composition and printing, as well as internal budgeting, accounting, and financial reporting. As an "income based" program, UK/CLE's course tuitions and publications sales are designed to generate sufficient revenues for self-support.

## **Commitment to Quality and Creativity**

UK/CLE is a member of the Association for Continuing Legal Education (ACLEA). As such, UK/CLE subscribes to the Standards of Operation for Continuing Legal Education Organizations, and the Standards of Fair Conduct and Voluntary Cooperation administered under the auspices of the American Law Institute-American Bar Association Committee on Continuing Professional Education. Throughout its existence UK/CLE has been actively involved in the activities of and discourse sponsored by ACLEA. UK/CLE's association with national and international CLE professionals has afforded it the opportunity to continually reassess instructional methods, quality in publications, and effective means of delivering CLE services at consistently high levels of quality.

## **An Integral Part of the Legal Profession's Tradition of Service**

An enormous debt is owed to the practitioners, professors, judges and other professionals who generously donate their time and talent to continuing legal education. Their knowledge and experience provide the fundamental components of our seminars and publications. Without their motivation and freely given assistance in dedication to the legal profession, high quality continuing legal education would not exist. As a non-profit organization, UK/CLE relies upon the traditional spirit of service to the profession that attorneys have so long demonstrated. We are constantly striving to increase attorney involvement in the continuing legal education process. If you would like to participate as a volunteer speaker or writer, please contact us and indicate your areas of interest and experience.



UNIVERSITY OF KENTUCKY  
COLLEGE OF LAW

OFFICE OF CONTINUING LEGAL EDUCATION

---

Suite 260 Law Building  
Lexington, Kentucky 40506-0048

Phone  
(859) 257-2921

Facsimile  
(859) 323-9790

Web Address  
[www.uky.edu/Law/CLE](http://www.uky.edu/Law/CLE)

---

PRESIDENT, UNIVERSITY OF KENTUCKY: Lee T. Todd, Jr.

DEAN, COLLEGE OF LAW: Allan W. Vestal

---

DIRECTOR OF CLE: Kevin P. Bucknam

ASSISTANT DIRECTOR OF CLE David L. Kinsella

ADMINISTRATIVE/BUSINESS MANAGER: Melinda E. Rawlings

EDITORIAL/MARKETING ASSISTANT: William G. Nims

### UK/CLE: A Self-Supporting Entity

The University of Kentucky Office of Continuing Legal Education (UK/CLE) is an income-based office of the University of Kentucky College of Law. As such, it is separately budgeted and financially self-supporting. UK/CLE operations are similar to not-for-profit organizations, paying all direct expenses, salaries and overhead solely from revenues.

No public funds or tax dollars are allocated to its budget. Revenues are obtained from registrant enrollment fees, and the sale of publications. Our sole function is to provide professional development services. In the event surplus funds become available, they are utilized to offset deficits or retained in our budget to improve the quality and variety of services we provide.

# **29th Annual Estate Planning Institute Pre-Institute Planning Committee**

**Glen S. Bagby – Co-Chair**  
*Woodward, Hobson & Fulton, LLP  
Lexington, Kentucky*

**Turney P. Berry – Co-Chair**  
*Ogden Newell & Welch  
Louisville, Kentucky*

**Jack R. Cunningham – Chair, Pre-Institute Session**  
*Frost Brown Todd LLC  
Lexington, Kentucky*

**John T. Bondurant**  
*Frost Brown Todd LLC  
Louisville, Kentucky*

**Mark T. MacDonald**  
*Wyatt, Tarrant & Combs LLP  
Lexington, Kentucky*

**Cynthia S. Buttorff**  
*Stites & Harbison PLLC  
Louisville, Kentucky*

**Wade T. Markham, II**  
*English, Lucas, Priest & Owsley  
Bowling Green, Kentucky*

**Tawana L. Edwards**  
*The Glenview Trust Company  
Louisville, Kentucky*

**Edward A. Rothschild**  
*Woodward, Hobson & Fulton, LLP  
Louisville, Kentucky*

**Emily Ledford Lawrence**  
*Goldberg & Simpson, P.S.C.  
Louisville, Kentucky*

**George Thacker**  
*Thacker, Bickel, Hodskins & Thacker, L.L.P.  
Owensboro, Kentucky*

**Richard J. Lyon**  
*National City Bank  
Lexington, Kentucky*

**David D. Wolfe**  
*Bank One, Kentucky  
Lexington, Kentucky*



# **THE ESSENTIAL TOOL-BOX FOR THE ESTATE & TRUST LAWYER**

*Pre-Institute Session To The 29<sup>th</sup> Annual Midwest/Midsouth Estate Planning Institute*

## **TABLE OF CONTENTS**

### **THE TOP 10 THINGS TO REMEMBER WHEN DEVELOPING A BASIC ESTATE PLAN ..... SECTION A**

*James L. Coorssen*

### **THE TOOLS AND TRAPS WHEN DEALING WITH POWERS OF ATTORNEY AND LIVING WILLS ..... SECTION B**

*Melissa H.P. Palmer*

### **THINGS YOU GOTTA KNOW ABOUT MARITAL DEDUCTIONS ..... SECTION C**

*Paul J. Dyar*

### **THE ESSENTIALS OF ETHICS FOR AN ESTATE & TRUST LAWYER .. SECTION D**

*Sheldon G. Gilman*

### **THE TOTAL RETURN TRUST: THE BIG POINTS ..... SECTION E**

*Barton T. Rogers*

### **THOSE FUNNY LITTLE LAWS THAT YOU DIDN'T KNOW EXISTED AND THAT WILL EFFECT YOUR ESTATE & TRUST PRACTICE ..... SECTION F**

*Turney P. Berry*

### **THE BASICS OF FIDUCIARY LIABILITY: CAN YOU RISK PROOF A FIDUCIARY? ..... SECTION G**

*Tawana Edwards*





# **THE TOP 10 THINGS TO REMEMBER WHEN DEVELOPING A BASIC ESTATE PLAN**

*James L. Coorssen  
Ogden Newell & Welch PLLC  
Louisville, Kentucky*

Copyright 2002. James L. Coorssen. All Rights Reserved.

## **SECTION A**



## **THE TOP 10 THINGS TO REMEMBER WHEN DEVELOPING A BASIC ESTATE PLAN**

I.	YOU CONTROL THE MEETING .....	A-1
II.	THE FIRST MEETING .....	A-3
III.	THE FIRST MEETING (Continued) .....	A-4
IV.	THE FIRST MEETING (Continued) .....	A-5
V.	THE FIRST MEETING (Continued) .....	A-6
VI.	THE FIRST MEETING (Continued) .....	A-7
VII.	THE FIRST MEETING (Continued ) Select The Plan .....	A-9
VIII.	THE ENGAGEMENT LETTER .....	A-11
IX.	PREPARE THE DOCUMENTS AND OUTLINES AND MAIL .....	A-12
X.	THE MEETING TO SIGN THE DOCUMENTS AND COMPLETE THE ESTATE PLAN .....	A-13

---

EXHIBIT V.A.1	Federal Estate Tax Analyses .....	A-14
EXHIBIT V.A.2	Federal Estate Tax Analyses .....	A-15
EXHIBIT VIII	Firm Information Documents .....	A-18
EXHIBIT IX.B	Revocable Trust Agreement .....	A-23
EXHIBIT IX.C	Sample Correspondence .....	A-27
EXHIBIT X.D	Notice For Tax Deduction Purposes .....	A-30



## I. YOU CONTROL THE MEETING

- A. This begins when the time for your meeting is set.

### Tell the client what you want to know:

1. The names and ages of the players in the ball game
2. What you (the client) own in your single name - because those are the only assets covered by a Will
3. What you and spouse own in joint name - automatically passes to survivor
4. Life insurance you own on your life - passes by beneficiary designation and no one pays income taxes on these proceeds. Note: We now list Roth IRAs here because, like life insurance, they pass by beneficiary designation and with no income tax consequences
5. Employee benefits - 401(k) plans, SEPs, IRAs, etc., because they pass by beneficiary designation but eventually someone will pay income taxes on these proceeds
6. What spouse owns in single name
7. Spouse joint name = 1/2 of 3, above
8. Spouse life insurance and Roth IRAs
9. Spouse employee benefits

### Tell the client what you do not want to know.

1. The value of automobiles, unless collectibles
2. The value of stuff in the house if it is the type of stuff that I would expect to see in a home of your value; i.e., no Rembrandts. Why? Because you will do no tax planning with these items, and they will let you know if grandma's sugar chest should go to David.

- B. Tell client what the meeting is supposed to accomplish. We want to meet your estate planning objectives and, at the same time, reduce taxes.

Why? So the client can agree or disagree.

- C. Strong general rule: Meet with husband and wife - who both become your clients.  
Why? No decisions will be made if you meet with only one.

Exception: Second marriage when you will not be preparing documents for both spouses.

- D. Place and length of meeting: Your office if at all possible and it should last 1 1/2 hours.

## II. THE FIRST MEETING

It is not difficult, and you not need be Merlin, to identify the goals of the husband and wife who are parents and this is their first marriage (or there are no children by any prior marriages):

- A. You want to provide for both of you while both of you are living;
- B. You want to provide for the survivor knowing that the survivor will provide for the children;
- C. You eventually want to pass assets to, or for the benefit of, your children after both of you die; and
- D. You want to save taxes whenever doing such does not screw up your non-tax goals.

In most cases you have hit the nail on the head. Sometimes you will have variations: the family farm or closely held business should pass to one or more, but not all, children; the disabled or chemically dependent child; provide for parents or sibling; charitable gifts; etc.

Why? You don't want to waste time telling them how you plan to provide for children and grandchildren after their deaths only to find out they have not seen the kids in 10 years....



### III. THE FIRST MEETING (CONTINUED)

#### A. Assemble the family data discussed in I, plus

1. Social security numbers of clients
2. Home and office phone numbers, e-mail, fax
3. Other advisors - CPA, stockbroker, banker, trust officer, life insurance agents
4. Are they U.S. citizens
5. Any expected inheritances

#### IV. FIRST MEETING (CONTINUED)

A. Assemble the assets as discussed in I, plus

1. Deal in round thousands - it does you no good to have exact figures today (which they are not) because they will be approximate tomorrow. Besides, using round thousands makes your addition much easier.

B. Until you become facile with this process, create your own form. Use lined paper - one page for each category:

\_\_\_\_\_ Single Name  
\_\_\_\_\_ and \_\_\_\_\_ Joint Name  
\_\_\_\_\_ Life Insurance and Roth IRAs  
\_\_\_\_\_ Employee Benefits

Prepare a similar sheet for obtaining the family and advisor data.

C. Should you send the form to the client for completion before the first meeting? I rarely find doing such to be helpful - they do not do it correctly; you will want to review each item with them so no appreciable time is saved; you have a chance to think while you are listing these assets; and you are in control.

V. THE FIRST MEETING (CONTINUED)

A. Illustrate taxes

1. H and W, first marriage, adult children whom they all like (an Ozzie and Harriet family) and total assets of \$1,000,000, or less. Show them why there are no taxes (see EXHIBIT V.A.1) and go to VI.
2. Ozzie and Harriet again, but their total estates exceed \$1,000,000 (\$1,500,000 in 2004, \$2,000,000 in 2006, \$3,500,000 in 2009). You now need to illustrate taxes - see EXHIBIT V.A.2.

VI. THE FIRST MEETING (CONTINUED)

A. Describe the plan

1. Ozzie and Harriet with no need for tax planning.

(i) Will

Exor \_\_\_\_\_ C. E. \_\_\_\_\_ 2nd C. E. \_\_\_\_\_

Pay debts and taxes

tangible personal property by memo; balance to spouse; if deceased  
to surviving children or descendants, per stirpes

Any cash bequests?

Residue to spouse and if deceased to descendants, per stirpes

Guardian for minors

Executor's powers

(ii) Power of Attorney

(iii) Living Will/Health Care Surrogate Designation

2. Ozzie and Harriet with tax planning.

(i) Same Will provisions as in VI.A.1., but residue is bequeathed to a  
Trust under Agreement

(ii) Why a trust under agreement, and not a testamentary trust?

(a) Privacy - the trust agreement is not in the Probate file as is the  
Will

- (b) May be funded during grantor's life, thus making estate administration a bit simpler, and providing additional privacy since trust assets are not listed on the estate inventory
- (c) May be funded during grantor's life with out-of-state realty (a two-week time share at Myrtle Beach or a winter home in Palm Beach), possibly eliminating the need for ancillary administration
- (d) There are no state law restrictions on who may be Trustee

## VII. THE FIRST MEETING (CONTINUED) Select the Plan

The family and asset data is collected, taxes are illustrated, and the plan is decided upon (though it may be “tweaked” after documents are mailed).

It does not matter how sophisticated (Bill Gates) or unsophisticated (Ozzie and Harriet) is the client - neither knows much, if anything, about trusts, federal estate taxes and all the other stuff you have been discussing. Thus, if you merely verbalize the provisions of the Wills and trust agreements you will lose them and they can't say, “Go back to what you said two minutes and 22 seconds ago and say that again.” If the clients do not understand, they will do nothing. And in the almost rare cases where the clients say, “Yes, that's great,” you'll forget in a couple of days (when you begin to draft) what it was that was so great.

Thus, on your legal pad, talk through and write out the options, eventually “pointing arrows” to what the clients have selected and/or striking what they do not want.

Ozzie's  
Will

Exor =  
debts, taxes  
tpp  
Gdn  
Residue

CE =

2d CE =

Ozzie's Revocable Trust  
Ozzie dies/  
Harriet survives

Fund A  
\$100,000

Tee =

ST =

Fund B  
\$1,000,000

Outright to Spouse  
or  
In trust for Spouse  
Required: income to  
Spouse for life  
Option: encroach for Spouse

In trust for Spouse  
Option: income to Spouse  
or Tee's discretion to pay  
income to Spouse,  
descendants, or reinvest  
Option: encroach for Spouse  
and descendants

At death of Spouse  
etc.

## VIII. THE ENGAGEMENT LETTER

See EXHIBIT VIII. We do not use an engagement letter but give a copy of EXHIBIT VIII to the clients when they leave the first meeting

The data typed *in italics* on Exhibit 8 is handwritten in actual cases.



**IX. PREPARE THE DOCUMENTS AND OUTLINES AND MAIL**

- A. Forms are an absolute necessity if you want to have an efficient and profitable estate planning practice and, at the same time, delivering the product for a competitive price.

But the forms must be good, must be regularly updated and improved upon, and may never be a substitute for your brain power.

- B. Document outlines - see EXHIBIT IX.B.
- C. Cover letter - see EXHIBIT IX.C.

X. THE MEETING TO SIGN THE DOCUMENTS AND COMPLETE THE ESTATE PLAN

A. Sign the original Will only and then make machine copies

Sign as many copies of the trust agreement as you wish - we would usually sign two in this case and keep one original in our files

We sign the original of the Power of Attorney only (though some people prefer to sign several copies) and make machine copies

We sign the original of the Living Will and make machine copies

B. And the original Wills are kept . . . ? Not in our safe! But some feel differently.

C. Signing the documents may, or may not, bring an end to the estate plan. No end has yet been reached if a substantial amount of the clients' wealth is represented by insurance policies, 401(k) plans, IRAs, etc.; where beneficiaries need to be changed; or if jointly owned assets need to be retitled.

D. Your invoice. In tax planning situations your clients may be able to deduct a portion of your fee. It constitutes a Miscellaneous Itemized Deduction and all such items in excess of 2 percent of adjusted gross income are deductible. We use a simple stamp on the invoice. See EXHIBIT X.A.

FEDERAL ESTATE TAX ANALYSES

Plan 1. First spouse to die leaves his/her total estate to the survivor. Assume Ozzie dies first but the order of deaths is immaterial.

<u>At death of:</u>	<u>Ozzie</u>	<u>Harriet</u>
1. Personal Estate	\$500,000	\$400,000
2. + Assets from Ozzie's line 4	<u>N/A</u>	<u>500,000</u>
3. Gross Estate	\$500,000	\$900,000
4. - Marital Deduction	<u>500,000</u>	<u>-0-</u>
5. Taxable Estate	\$ -0-	\$900,000
6. Tentative Federal Estate Tax	\$ -0-	\$307,000
7. - Credit	<u>N/A</u>	<u>346,000</u>
8. - Federal Estate Tax Payable	\$ -0-	\$-0-

**FEDERAL ESTATE TAX ANALYSES**

Plan 1. First spouse to die leaves his/her total estate to the survivor. Ozzie has \$1,100,000 and Harriet has \$1,200,000. Assume Ozzie dies first but the order of deaths is immaterial.

<u>At death of:</u>	<u>Ozzie</u>	<u>Harriet</u>
1. Personal Estate	\$1,100,000	\$1,200,000
2. + Assets from Ozzie's line 4	<u>N/A</u>	<u>1,100,000</u>
3. Gross Estate	\$1,100,000	\$2,300,000
4. - Marital Deduction	<u>1,100,000</u>	<u>-0-</u>
5. Taxable Estate	\$ -0-	\$2,300,000
6. Tentative Federal Estate Tax	\$ -0-	\$ 928,000
7. - Credit	<u>N/A</u>	<u>346,000</u>
8. - Federal Estate Tax Payable	\$ -0-	\$ 582,000

David and Ricky each inherit \$859,000  $[(\$1,100,000 + 1,200,000 - 582,000) \div 2]$ .

Comment. Taxes are totally unacceptable.

**EXHIBIT V.A.2 (continued)**

Plan 2. Ozzie dies first and leaves \$1,000,000 (this amount increases to \$1,500,000 in 2004; \$2,000,000 in 2006; \$3,500,000 in 2009; and the federal estate tax is scheduled to be repealed in 2010, but with reinstatement in 2011 at rates similar to those in 2001) to a trust for the benefit of Harriet - the value of this trust will not be subject to estate taxes at Harriet's death. The balance of the assets owned by Ozzie will pass to, or for the benefit of, Harriet in a manner that will qualify for the marital deduction - the value of these assets will not be taxed at Ozzie's death, but will be taxed at Harriet's death.

<u>At death of:</u>	<u>Ozzie</u>	<u>Harriet</u>
1. Personal Estate	\$1,100,000	\$1,200,000
2. + Assets from Ozzie's line 4	<u>N/A</u>	<u>100,000</u>
3. Gross Estate	\$1,100,000	\$1,300,000
4. - Marital Deduction	<u>100,000</u>	<u>-0-</u>
5. Taxable Estate	\$1,000,000	\$1,300,000
6. Tentative Federal Estate Tax	\$ 346,000	\$ 470,000
7. - Credit	<u>346,000</u>	<u>346,000</u>
8. - Federal Estate Tax Payable	\$ -0-	\$ 124,000

David and Ricky each inherit \$1,088,000  $[(\$1,100,000 + 1,200,000 - 124,000) \div 2]$ .

Comment. Taxes are less than in Plan 1, and will be \$0 if the death of the second to die occurs in 2004, or later.

Comment. If one spouse cannot dispose of \$1,000,000 (for instance, if the \$2,300,000 of assets were all owned by Ozzie) illustrate how the plan will not work as illustrated above if Harriet dies first.

Solution: Transfer assets to Harriet.

**OGDEN NEWELL & WELCH PLLC**

**ESTATE PLANNING**

**OGDEN NEWELL & WELCH PLLC**  
1700 PNC Plaza  
500 W. Jefferson Street  
Louisville, Kentucky 40202  
(502) 582-1601  
(502) 581-9564 - FAX



1700 PNC PLAZA  
500 WEST JEFFERSON STREET  
LOUISVILLE, KENTUCKY 40202-2874  
(502) 582-1601  
FAX: (502) 581-9564  
WWW.OGDENLAW.COM

RICHARD F. NEWELL  
JOHN T. BALLANTINE  
SPENCER E. HARPER, JR.  
JOSEPH C. OLDHAM  
WILLIAM W. DAVIS  
JAMES L. COORSSEN\*  
STEPHEN F. SCHUSTER  
JOHN G. TREITZ, JR.  
WALTER LAPP SALES  
ERNEST W. WILLIAMS  
JAMES S. GOLDBERG  
SCOTT W. BRINKMAN  
BRUCE K. DUDLEY

JEFFEREY M. YUSSMAN  
W. GREGORY KING  
KENDRICK R. RIGGS†  
JAMES B. MARTIN, JR.  
LISA ANN VOGT  
TURNERY P. BERRY  
JOHN WADE HENDRICKS  
LYNN H. WANGERIN  
DOUGLAS C. BALLANTINE  
THOMAS E. RUTLEDGE††  
THOMAS M. WILLIAMS\*\*‡  
SHARON A. MATTINGLY  
ANTHONY L. SCHNELL

STEPHEN C. HALL  
ALLYSON K. STURGEON  
TIMOTHY J. EIFLER  
KELLY S. HENRY  
CRAIG C. DILGER  
J. GREGORY CORNETT  
JOSEPH A. KIRWAN  
LAURA H. PULLIAM\*\*  
CONNIE L. VERRILL  
JOSEPH A. BICKETT  
MARK S. FRANKLIN  
MATTHEW G. MERCER

OF COUNSEL  
JAMES S. WELCH  
JOHN S. GREENEBAUM PSC  
MAUREEN M. CARR††  
  
SQUIRE R. OGDEN  
1899-1984  
ALSO ADMITTED:  
\*FLORIDA  
\*\*INDIANA  
†VIRGINIA  
††DISTRICT OF COLUMBIA  
‡ TENNESSEE

## Our People

### Attorneys:

Turney P. Berry  
James L. Coorsen  
Bruce K. Dudley  
Kelly S. Henry  
Joseph C. Oldham  
Jefferey M. Yussman

### Phone Numbers:

(502) 560-4276  
(502) 560-4229  
(502) 560-4255  
(502) 560-4214  
(502) 560-4230  
(502) 560-4272

### E-Mail Address:

tpberry@ogdenlaw.com  
jcoorsen@ogdenlaw.com  
bkdudley@ogdenlaw.com  
khenry@ogdenlaw.com  
jcoldham@ogdenlaw.com  
jyussman@ogdenlaw.com

### Paralegals:

Connie S. Bueter  
Amela K. Cemerlic

(502) 560-4239  
(502) 560-4207

cbueter@ogdenlaw.com  
acemerlic@ogdenlaw.com

### Assistants:

Aynn C. Dillard  
Nancy J. Johnston  
Paulette R. Milliner  
Debbie A. Webb

(502) 582-1601 X-4325  
(502) 582-1601 X-4238  
(502) 582-1601 X-4327  
(502) 582-1601 X-4331

adillard@ogdenlaw.com  
njohnston@ogdenlaw.com  
pmilliner@ogdenlaw.com  
dwebb@ogdenlaw.com



## Our Process

### **Estate Planning Work for *Ozzie and Harriet Nelson*.**

1. **Our Goal.** Our goal is to provide you with an estate plan that accomplishes your non-tax objectives with the lowest tax cost that reasonably can be achieved. We write and speak nationally about estate planning ideas and developments and fully intend to provide you with the best advice available anywhere.

2. **Joint Representation of Spouses.** We represent both spouses only so long as your estate planning objectives are consistent. If your objectives cease to be consistent, then we may continue to represent one of you if we believe we can do so fairly. So long as we represent both of you, we will not deliberately keep anything that one of you tells us from the other. We will assume that both of you receive and read mail that is addressed to both of you. You should know that the one of you who survives may disrupt your estate plan by "electing against the Will" which is a right given under state law. The election gives the survivor outright ownership of about half the deceased spouse's assets, regardless of the estate plan.

If you are concerned about the possibility of election against the Will, or if you have any concerns about our joint representation of you, please let me know.

3. **The Information We Need.** We will rely on the information you give us about your family situation and the nature and value of your assets in giving you advice and developing your estate plan. Our advice may be inappropriate if that information is incorrect or incomplete.

4. **Responsiveness.** We are committed to providing you with extraordinary service at all times. In particular, we commit to returning your telephone call within 24 hours (or, if we are unavailable, having someone else in our office return your call) and providing the documents required to implement the ideas we discuss within two weeks (or more rapidly if you need us to do so). We welcome your comments on our responsiveness.

5. **Fees.** Our fees compensate us for the time and expertise your plan requires, and are commensurate with the value you receive and the costs of comparable advice elsewhere. We will tell you what we expect our fee to be before we begin working for you. Generally we will bill you monthly although in some instances we may wait until a project is finished. If you have preferences on billing frequency please let us know. And, of course, please let us know anytime you have a question about our fees.

6. **Other Advisors.** If you want us to, we will discuss your plan with your other financial advisors. In particular, we recommend a discussion with your accountant. Other advisors could include trust officers, brokers, appraisers, and insurance agents.

7. **Follow-Up.** You should have your estate plan reviewed every two or three years and more often if your family or asset situation changes. To initiate a review you should call us. Of course, from time to time we may send you a note about developments that may interest you, or you may read about those in our newsletter, but that is no substitute for a complete periodic review.

## Your Estate Planning Documents

- ☐ Will -- Individual  
☒ Wills -- Spouses
- ☒ Power(s) of Attorney  
☒ Health Care Surrogate Designation/Living Will(s) -- Kentucky  
☐ Health Care Surrogate Designation/Living Will(s) -- \_\_\_\_\_
- ☐ Revocable Trust -- GST Planning only  
☐ Revocable Trusts -- A/B Planning, outright to children  
☒ Revocable Trusts -- A/B and GST Planning
- ☐ Irrevocable Trust -- Crummey Trust without life insurance  
☐ Irrevocable Trust -- Crummey Trust with life insurance
- ☐ ON&W helps with ownership and beneficiary change forms  
☐ ON&W responsible for ownership and beneficiary change forms
- ☐ Irrevocable Trust -- Grandchild Only  
☐ Asset Protection Crummey Trust (Delaware)  
☐ Irrevocable Trust -- Lifetime QTIP
- ☐ Limited Partnership -- Securities  
☐ Limited Partnership -- Real Estate  
☐ Limited Partnership -- Charitable Gift  
☐ Limited Liability Company -- Real Estate
- ☐ Grantor Retained Annuity Trust -- Start-Up company  
☐ Grantor Retained Annuity Trust -- S corp stock  
☐ Grantor Retained Annuity Trust -- Rental real estate
- ☐ Qualified Personal Residence Trust -- Ky residence  
☐ Qualified Personal Residence Trust -- Non-Ky residence  
☐ Qualified Personal Residence Trust -- Vacation home
- ☐ Charitable Remainder Trust  
☐ Charitable Lead Trust  
☐ Creation of Family Foundation or Supporting Organization
- ☐ Deed transferring residence to \_\_\_\_\_  
☐ Deed transferring residence to \_\_\_\_\_'s Revocable Trust  
☐ Deed transferring vacation home to \_\_\_\_\_'s Revocable Trust  
☐ Deed transferring residence to \_\_\_\_\_'s QPRT  
☐ Deed transferring vacation home to \_\_\_\_\_'s QPRT  
☐ Deed(s) transferring real estate to LP or LLC
- ☐ Documents recapitalizing company (voting and nonvoting shares)  
☐ Stock Certificates for funding GRAT or LP
- ☐ Other Specialized Documents: \_\_\_\_\_
- ☐ TINs needed for: \_\_\_\_\_
- ☐ Copies of documents to: Trust Officer; CPA; Broker; CLU  
☐ Other: \_\_\_\_\_

**ESTIMATED FEE: \$**           XXX          .

## Your Tasks

\_\_\_ Deeds.

For each piece of real estate to be transferred we will need:

- \_\_\_ Deed
- \_\_\_ Current tax assessed value
- \_\_\_ If there is a mortgage, the name and address of mortgagee, contact person and account number

You will send us information for us to transfer:

Residence at: \_\_\_\_\_  
Vacation Property at: \_\_\_\_\_  
Investment Property at: \_\_\_\_\_  
Other Property at: \_\_\_\_\_

If we receive the information in advance of the next meeting we can have the new deeds ready to be signed when you sign your other estate planning documents.

XX Life Insurance.

If we are going to help you change the beneficiary and ownership of your policies it would be best for you to bring to the next meeting:

- XX Each insurance policy
- XX Change of Beneficiary Forms
- \_\_\_ Change of Ownership and Beneficiary Forms

XX Employee Benefits (IRAs, 401(k) plans, retirement plans).

If we are going to help you change the beneficiary of your retirement plans it would be best for you to bring to the next meeting:

- XX Copy of each IRA agreement
- XX Copy of each Plan document or Summary Plan Description
- XX Change of Beneficiary Form for each IRA and Plan

\_\_\_ Corporate Documents.

We are going to recapitalize your company so send us a copy of your Minute Book. We can then have the recap documents completed for you to sign when you sign your other estate planning documents.

\_\_\_ Partnership Documents.

We are forming a partnership for you. Stocks will be transferred into the partnership so you will establish a brokerage account. Let us know when you have spoken with your broker about that.

\_\_\_ Decisions to be Made.

We left several items undecided at today's meeting. You were going to think about:

Remote - Where do assets go if Ozzie, Harriet, David and Ricky die and no other descendants survive?  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

**EXHIBIT IX.B.**

Ozzie Nelson Revocable Trust Agreement  
dated \_\_\_\_\_, 2002

You are named Trustee, Harriet is named Successor Trustee, and David is named second Successor Trustee.

Article 1 contains definitions.

- 1.2           A Qualified Trustee is defined as a Trustee named as such herein, a trust company or bank, or one or more of your descendants age 30 or older when appointed.

Article 2 discusses the administration of the trust during your life. You may choose to fund the trust during your lifetime -- such a funded, revocable trust is often called a Living Trust.

- 2.1           You may withdraw trust assets, revoke or amend the trust, or change the Trustee at any time.
- 2.3           Income producing assets added to the trust during your life will be administered for your benefit and the benefit of Harriet and your descendants.

Article 3 provides that administration expenses, taxes, and bequests will be paid from the trust if the residue of your estate is insufficient to pay these items, and debts may be paid.

Article 4 provides that the trust assets will be divided between Fund A and Fund B if Harriet survives you.

- 4.2           If the federal estate tax is in effect, Fund B will contain the largest amount of assets possible without causing your estate to incur any federal estate taxes. This amount may be as much as \$1,000,000 in 2002, \$1,500,000 in 2004, \$2,000,000 in 2006, and \$3,500,000 in 2009. The remaining assets will be added to Fund A which qualifies for the marital deduction. Changes in asset values occurring during estate administration will cause the value of Fund B to increase or decrease.

4.2A This paragraph divides trust property between Fund A and Fund B if the estate tax is repealed. It will have no effect until then (currently slated for January 1, 2010).

4.7 If Harriet predeceases you, the trust assets will be administered as provided in Article 6.

Article 5A provides that any assets added to Fund A will be distributed to Harriet.

Article 5B discusses the administration of Fund B during Harriet's life.

Trustee is to consider a beneficiary's income, assets and tax consequences when making distributions under this trust, but Harriet is the primary beneficiary.

5B.1 The Trustee may pay the income of Fund B to Harriet and your descendants and may reinvest undistributed income.

5B.2 The Trustee may encroach on the principal of Fund B for the benefit of Harriet and your descendants.

5B.3 Harriet may designate by Will the amount, time, and manner your descendants will receive Fund B assets. Amounts not designated will be referred to as the remaining assets of Fund B.

5B.4 Upon Harriet's death, the remaining assets of Fund B will be administered as provided in Article 6.

Article 6 discusses the administration of trust assets after you and Harriet have died.

6.1 The trust assets will be divided in equal shares -- one for each then living child and one for the then living descendants of any deceased child -- and held or distributed as provided herein.

6.2 Notwithstanding the above, if one of your descendants dies within 90 days after your death, such descendant will be deemed to have predeceased you.

6.3 When the Trustee is given discretion to make distributions among your beneficiaries, preference will be given to those in the oldest generation.

Article 7 discusses the administration of the trusts for the primary benefit of your children after you and Harriet have died.

- 7.1           A share set aside for your child will be administered as follows.
- 7.2           A trust that is not exempt from the generation skipping tax will be distributed to your child and a trust that is exempt will continue in trust.
- 7.3           The Trustee may pay income to or for the benefit of your child until age 25. Undistributed income will be added to principal. Thereafter, the net income will be paid to your child. The Trustee may encroach on principal for the benefit of your child and your child's descendants. A child's trust will terminate 1/3 at 30, 1/2 at 35 and the balance at 40.
- 7.4           Your child may designate by Will the amount, time, and manner your descendants (or if none, any person or entity) will receive the trust assets that are exempt from the generation skipping tax. Amounts not designated will be referred to as the remaining trust assets.
- 7.5           If your child dies prior to the termination of the trust, the remaining trust assets will be distributed to the child's descendants; but if none, to your descendants. The share for any then current trust beneficiary will be added to his or her trust.
- 7.6           A share set aside for the descendants of your deceased child will be divided and distributed to them.
- 7.7           If the Trustee is directed to distribute a share of the trust to a beneficiary (your grandchild) under age 21, the Trustee may withhold distribution of this amount, manage it for the benefit of the beneficiary, and distribute the remaining assets to the beneficiary at age 21 or to his or her estate if the beneficiary dies prior thereto.

Article 8 provides that if no beneficiary survives to inherit the trust assets, the assets will be distributed to \_\_\_\_\_.

Article 9 sets forth the powers of the Trustee.

Article 10 discusses the removal of the Trustee.

- 10.1 Harriet, and after her death a majority of the current income beneficiaries in the oldest generation of each trust, may replace the acting Trustee or any successor Trustee of such trust with a Qualified Trustee.

Article 11 contains administrative provisions designed to minimize (or eliminate) a generation skipping tax.

Article 12 contains miscellaneous provisions.

- 12.1 To the extent possible, a beneficiary's creditors cannot attach trust assets.

**EXHIBIT IX.C.**

Dear

Enclosed are the following estate planning documents we discussed recently:

- Your Wills
- Your Revocable Trust Agreements
- Your Irrevocable (Crummey) Trust
- Outlines of the Wills and Trust Agreements - these are summaries which are designed to help you with your review, but please remember that the documents themselves are controlling
- Owner's Manuals for the Revocable Trust Agreements
- Owner's Manual for the Irrevocable Trust Agreement
- Your Powers of Attorney
- Your Living Wills and Health Care Surrogate Designations
- A list showing your family, some of its advisors, its assets, and several federal estate tax analyses. Please feel free to edit and return your marked-up copy to me and I will have a corrected version prepared. Also, please remember that our computers have stored all of this data. Thus, you may add and delete in the future, return your revised copy to me, and we will prepare an updated edition
- Your Qualified Personal Residence Trust
- Your Grantor Retained Annuity Trust
- Limited Partnership documents for the \_\_\_\_\_ Partnership

Please review all of the enclosures very carefully and feel free to note your questions and comments on your copies of the documents. Call me when you are ready and we can discuss your questions, make any necessary changes, and arrange for a time for us to get together.

We discussed transferring assets between the two of you when we last met. Let me know what changes have been made when we next meet so that I can revise your asset list. We can discuss this again if you have not yet made any changes.



The Owner's Manuals discuss changing the (ownership and) beneficiary of your life insurance policies. Please review the Manual thoroughly and we can discuss any questions you have.

**DRAFTER NOTE:** delete previous ¶ and substitute the next 1, 2 or 3 ¶s if you want to be more specific.

\_\_\_\_\_, you should begin acquiring change of beneficiary forms for your:

\_\_\_\_\_  
\_\_\_\_\_.

\_\_\_\_\_, you should begin acquiring change of beneficiary forms for your:

\_\_\_\_\_  
\_\_\_\_\_.

\_\_\_\_\_, you should begin acquiring change of ownership and change of beneficiary forms for the following policies insuring your life:

\_\_\_\_\_  
\_\_\_\_\_.

We discussed transferring your real estate located in \_\_\_\_\_ to \_\_\_\_\_'s Revocable Trust. I can get started on that once I have the following: the deed; the identity of the mortgagee and your mortgage account number; and the amount of the last property tax assessment. Once the home is transferred to the trust, you will want to contact your homeowners insurance agent and tell the agent about this transfer. You should be notified in writing that your coverage will continue. As a rule, the Trustee of the Trust Agreement is added as an additional insured.

As you probably already know, I represent both of you because your estate planning objectives are consistent. Because I represent both of you, I will not deliberately keep anything that one of you tells me from the other. I will assume that both of you receive and read mail that is addressed to both of you.

Finally you should know that the one of you who survives may disrupt your estate plan by "electing against the Will" which is a right given under Kentucky law. The election

gives the survivor outright ownership of about half the deceased spouse's assets, regardless of the estate plan.

If either of you are concerned about the possibility of election against the Will, or if you have any concerns about my joint representation of you, please let me know.

Thank you very much for asking us to help you with your estate planning.

Enclosures

*Ozzie and Harriet*

75% of the time shown on this invoice was spent on tax planning matters. Thus, 75% of the amount of this invoice is potentially deductible as a miscellaneous deduction-tax planning, on your income tax returns.

*Jim*

# **THE TOOLS AND TRAPS WHEN DEALING WITH POWERS OF ATTORNEY AND LIVING WILLS**

*Melissa H.P. Palmer  
The Rigsby Law Group  
Lexington, Kentucky*

Copyright 2002. Melissa H.P. Palmer. All Rights Reserved.

## **SECTION B**



## **THE TOOLS AND TRAPS WHEN DEALING WITH POWERS OF ATTORNEY AND LIVING WILLS**

<b>I.</b>	<b>The Basics .....</b>	<b>B-1</b>
<b>II.</b>	<b>The Big Questions .....</b>	<b>B-1</b>
<b>III.</b>	<b>Specific Powers .....</b>	<b>B-3</b>
<b>IV.</b>	<b>Recording The Power Of Attorney .....</b>	<b>B-5</b>
<b>V.</b>	<b>Designation Of Health Care Surrogate And Living Will .....</b>	<b>B-6</b>

### **Appendix:**

General Power Of Attorney .....	B-9
Springing General Power Of Attorney .....	B-15
Living Will Directive .....	B-21
Designation Of Health Care Surrogate .....	B-27



**The Tools and Traps  
When Dealing With  
Powers of Attorney and Living Wills**

**by Melissa H.P. Palmer, J.D., LL.M  
The Rigsby Law Group**

**I. The Basics**

A. A power of attorney is a written document in which a person (known as the principal) authorizes another person (known as the attorney-in-fact) to perform certain acts on the principal's behalf. A power of attorney creates a principal and agent relationship which is controlled by the general principles agency law.

B. Ordinarily, a principal and agent relationship terminates upon the death or incapacity of the principal.

C. A durable power of attorney specifies that it remains in effect even if the principal becomes disabled.

KRS 386.093 authorizes the creation of a durable power of attorney:

(1) As used in this section, "durable power of attorney" means a power of attorney by which a principal designates another as the principal's attorney in fact in writing and the writing contains the words, "**This power of attorney shall not be affected by subsequent disability or incapacity of the principal, or lapse of time**", or "**This power of attorney shall become effective upon the disability or incapacity of the principal**", or similar words showing the intent of the principal that the authority conferred shall be exercisable notwithstanding the principal's subsequent disability or incapacity, and, unless it states a time of termination, notwithstanding the lapse of time since the execution of the instrument.

**II. The Big Questions**

A. Who to name as Attorney-in-Fact?

Obviously, the principal will wish to designate an agent in whom the principal has a great deal of trust and confidence. This is often a spouse and/or children of the principal. This can create conflict, especially if there are children by a prior marriage or conflicts within the family. It is important to note that in Kentucky the attorney-in-fact is not included in the definition of a fiduciary.

**KRS 395.001. Definition of "fiduciary."** — The term "fiduciary" as used in this chapter means any person, association, or corporation meeting the requirements of KRS 395.005 (other than assignee or trustee for an insolvent



debtor or a guardian under the uniform veterans' guardianship act) appointed by, or under the control of, or accountable to, the district court, including executors, administrators, administrators with the will annexed, testamentary trustees, curators, guardians and conservators.

Rice v. Floyd explained the importance of this distinction.

"This Court notes that the guardian is answerable to a court and must file accountings at least annually. The attorney-in-fact is answerable and accountable only to the principal who may be mentally disabled. It is obvious that there must be adequate safeguards and control on the person who manages an incompetent's estate and that a great disparity exists between the durable power of attorney and a guardian.

A guardian must comply with K.R.S. 389A.010 *et seq.* whenever the sale of real property is involved. The attorney-in-fact may sell real estate as if it were his own. The guardian must also file biennial accounts with the district court. K.R.S. 387.670 and K.R.S. 387.710. An attorney-in-fact is not a fiduciary as defined in K.R.S. 395.001, nor is he a fiduciary subjected to the reporting requirements of K.R.S. 387.500 *et seq.* The attorney-in-fact is accountable only to his principal, who in this case appears to be incompetent."

Rice v. Floyd (768 S.W.2d 57, 59 Ky. 1989).

1. The principal should consider naming a successor attorney-in-fact in the event the first named attorney-in-fact is unable or unwilling to continue managing the affairs of the principal.
2. To eliminate possible future conflicts, language terminating the appointment of the attorney-in-fact upon the occurrence of a triggering event (e.g., upon divorce or dissolution) could be included in the power of attorney.

#### B. Effective Now or Later?

1. Springing Powers become effective upon the happening of a specified triggering event.

KRS 386.093 authorizes the creation of a springing durable power of attorney and specifies the triggering event, if not spelled out in the document:

(5) If the power of attorney is to become effective upon the disability or incapacity of the principal, the principal may specify the conditions under which the power is to become effective and may designate the person, persons, or institution responsible for making the determination of disability or incapacity. If the principal fails to so specify, the power shall become

effective upon a written determination by two (2) physicians that the principal is unable, by reason of physical or mental disability, to prudently manage or care for the principal's person or property, which written determination shall be conclusive proof of the attorney in fact's power to act pursuant to the power of attorney. The two (2) physicians making the determination shall be licensed to practice medicine.

### C. General or Limited?

1. A limited power of attorney authorizes an agent to act in specified areas or to take specific action defined in the instrument. One common use of a limited power of attorney is to authorize the agent to transfer assets to an existing trust created by the principal.

2. General powers of attorney are the most common and grant broad powers to the attorney-in-fact to act in connection with all of the principal's affairs.

### D. Where will the attorney-in-fact use the power of attorney?

The requirements for the creation and recognition of a power of attorney vary from state to state. Therefore, it is important to know where the agent will be acting to ensure that the power is effective. Some states have statutes specifying who can act as attorney-in-fact.

## III. Specific Powers

### A. The power to make gifts should be specifically considered and addressed.

The ability of the attorney-in-fact to make gifts of the principal's property is an important function often included in the power of attorney. Gifting can accomplish many objectives of the principal such as reducing the size of the principal's estate or continuing a plan of gifting begun by the principal.

1. The principal may wish to limit the amount gifts, the class eligible to receive gifts, or the specific property eligible to be gifted.

2. Gifting could create conflict between expectant heirs and the attorney-in-fact. In order to protect the attorney-in-fact, the principal should specify in the document the authority to make gifts. The court in Wabner v. Black, 7 S.W.3d 379 (Ky. 1999) declined adopt a *per se* rule that an attorney-in-fact may not make gifts of the principal's property to himself or herself. This position was reiterated in Ingram v. Cates, "In Wabner v. Black, the court refused to adopt a strict rule of law prohibiting attorneys-in-fact from making gifts to themselves without explicit written authorization by the grantor pursuant to a durable power of attorney. Instead, the court adopted an

"utmost good faith" standard to be used to judge the acts of the attorney-in-fact. If determined to be within the exercise of authority granted by the power of attorney, then whether the attorney-in-fact acted with utmost good faith becomes a jury question." Ingram v. Cates, 2000-CA-002481-MR (Ky. App. 4-19-2002).

3. Tax issues regarding gifts made pursuant to a power of attorney.

The IRS has maintained the position that if a decedent could have the gifts made by an attorney-in-fact restored, then the decedent maintained the power to revoke the gifts. Thus, such gifts are included in the decedents federal taxable estate under §2038. (See PLR8635007 where the power of attorney did not specify the authority of the attorney-in-fact to make gifts and under Michigan law the principal could recover such gifts from the attorney-in-fact). On the other hand, the IRS has recognized gifts made pursuant to a power of attorney when the authority to make gifts is expressly stated the power of attorney. (See PLR 8623004).

Planning Note: Although the power of attorney expressly provides that the attorney-in-fact is authorized to make gifts, the attorney-in-fact must be sure to deliver the gifts and take steps to end the decedent's dominion and control over the property to be sure the gifts are completed gifts. Incomplete gifts will be included in the decedent's estate. See Estate of Devlin, T.C. Memo. 1999-406.

B. The attorney-in-fact should be given specific authority to execute a valid "Qualified Disclaimer" on behalf of the principal.

KRS 394.610 provides that the power to disclaim an interest in property for the principal may be granted to an attorney-in-fact, however the power of attorney must expressly provide this authority.

**KRS 394.610(3)** No disclaimer by a living person's legal representative, except for the person's attorney-in-fact, shall be made unless the court having jurisdiction of the estate of the disabled, incapacitated, or protected person has authorized the disclaimer. No disclaimer by the person's attorney-in-fact shall be made unless the instrument governing the attorney-in-fact authority expressly authorizes a disclaimer.

C. The attorney-in-fact should be given express authority to handle tax matters on behalf of the principal. A tax return which is filed, but not personally signed by the taxpayer is not properly filed. If an agent signs a return on behalf of a taxpayer, but does not have a valid power of attorney to do so, the return is not considered to have been signed. See Elliott v. Commissioner, 113 T.C. 125 (1999).

D. Compensation for the attorney-in-fact should be addressed expressly in the power of attorney.

E. The power of attorney should recite the preference of the principal in the event of a court appointed fiduciary. In Kentucky, the attorney-in-fact is subordinate to a court appointed guardian. (Kentucky is in the minority on this point.)

"Proceeding with a guardianship petition does not infringe upon any civil or constitutional right of the principal. Rather it aids the principal in the proper judicial consideration of the rights of the parties. The durable power of attorney is not comprehensive enough to replace the provisions of Chapter 387 in regard to the administration of the estates of incompetents. The purpose of K.R.S. 387.500 is to appoint a person to take care of the day-to-day personal business of an incompetent. The scope of authority, duties and accountability of a guardian is much broader than that of a traditional power of attorney, even one intended to survive disability. The crucial phrase of K.R.S. 386.093 is found in the last sentence which states that, "If a fiduciary is thereafter appointed by the court for the principal, the power of the attorney in fact shall thereupon terminate and he shall account to the court's appointed fiduciary."

Rice v. Floyd (768 S.W.2d 57, 59 Ky. 1989).

#### IV. Recording the power of attorney.

Kentucky law requires that if the documents of a property transaction must be recorded to become valid against purchasers and creditors, then a power of attorney relating to the transaction must also be recorded in the same office and in the same manner as the record of the transaction.

**KRS 382.370. Power of attorney to convey or release property — Recording — Revocation.** — Powers of attorney to convey or release real or personal property, or any interest therein, may be acknowledged, proved and recorded in the proper office, in the manner prescribed for recording conveyances. If the conveyance made under a power, is required by law to be recorded or lodged for record, to make the same valid against creditors and purchasers, then the power must be lodged or recorded in like manner, and no such power so recorded shall be deemed to be revoked by any act of the party by whom it was executed, except from the time when there has been lodged for record in the office in which the power is recorded a written revocation, executed and proved or acknowledged in the manner prescribed for conveyances, or a memorandum of revocation made on the margin of the record thereof, which memorandum is signed by the party executing the same, and attested by the clerk.

## V. Designation of Health Care Surrogate and Living Will

KRS 311.623 is the statutory authorization to make a living will directive and to designate a health care surrogate.

**KRS 311.623. Living will directive — Eligible persons — Scope — Effect — Recognition of person's desire not to be resuscitated.** (1) An adult with decisional capacity may make a written living will directive that does any or all of the following: (a) Directs the withholding or withdrawal of life-prolonging treatment; or (b) Directs the withholding or withdrawal of artificially provided nutrition or hydration; or (c) Designates one (1) or more adults as a surrogate or successor surrogate to make health care decisions on behalf of the grantor. During any period in which two (2) or more surrogates are serving, all decisions shall be by unanimous consent of all the acting surrogates unless the advance directive provides otherwise; or (d) Directs the giving of all or any part of the adult's body upon death for any purpose specified in KRS 311.185. (2) Except as provided in KRS 311.633, a living will directive made pursuant to this section shall be honored by a grantor's family, regular family physician or attending physician, and any health care facility of or in which the grantor is a patient. (3) For purposes of KRS 311.621 to 311.643, notification to any emergency medical responder as defined by KRS Chapter 211 or any paramedic as defined by KRS Chapter 311, of a person's authentic wish not to be resuscitated shall be recognized only if on a standard form or identification approved by the Kentucky Board of Medical Licensure, in consultation with the Cabinet for Health Services.

**KRS 311.625. Form of living will directive.** (1) A living will directive made pursuant to KRS 311.623 shall be substantially in the following form, and may include other specific directions which are in accordance with accepted medical practice and not specifically prohibited by any other statute. If any other specific directions are held by a court of appropriate jurisdiction to be invalid, that invalidity shall not affect the directive. "Living Will Directive My wishes regarding life-prolonging treatment and artificially provided nutrition and hydration to be provided to me if I no longer have decisional capacity, have a terminal condition, or become permanently unconscious have been indicated by checking and initialing the appropriate lines below. By checking and initialing the appropriate lines, I specifically: \_\_\_\_\_ Designate \_\_\_\_\_ as my health care surrogate(s) to make health care decisions for me in accordance with this directive when I no longer have decisional capacity. If \_\_\_\_\_ refuses or is not able to act for me, I designate \_\_\_\_\_ as my health care surrogate(s). Any prior designation is revoked. If I do not designate a surrogate, the following are my directions to my attending physician. If I have designated a surrogate, my surrogate shall comply with my wishes as indicated below: \_\_\_\_\_ Direct that treatment be withheld or withdrawn, and that I be permitted to die naturally with only the administration of medication or the performance of any medical treatment deemed

necessary to alleviate pain. \_\_\_\_\_ DO NOT authorize that life-prolonging treatment be withheld or withdrawn. \_\_\_\_\_ Authorize the withholding or withdrawal of artificially provided food, water, or other artificially provided nourishment or fluids. \_\_\_\_\_ DO NOT authorize the withholding or withdrawal of artificially provided food, water, or other artificially provided nourishment or fluids. \_\_\_\_\_ Authorize my surrogate, designated above, to withhold or withdraw artificially provided nourishment or fluids, or other treatment if the surrogate determines that withholding or withdrawing is in my best interest; but I do not mandate that withholding or withdrawing. \_\_\_\_\_ Authorize the giving of all or any part of my body upon death for any purpose specified in KRS 311.185. \_\_\_\_\_ DO NOT authorize the giving of all or any part of my body upon death. In the absence of my ability to give directions regarding the use of life-prolonging treatment and artificially provided nutrition and hydration it is my intention that this directive shall be honored by my attending's physician, my family, and any surrogate designated pursuant to this directive as the final expression of my legal right to refuse medical or surgical treatment and I accept the consequences of the refusal. If I have been diagnosed as pregnant and that diagnosis is known to my attending physician, this directive shall have no force or effect during the course of my pregnancy. I understand the full import of this directive and I am emotionally and mentally competent to make this directive. Signed this \_\_\_\_ day of \_\_\_\_\_, 19\_\_\_. Signature and address of the grantor. In our joint presence, the grantor, who is of sound mind and eighteen (18) years of age, or older, voluntarily dated and signed this writing or directed it to be dated and signed for the grantor. Signature and address of witness. Signature and address of witness. OR STATE OF KENTUCKY) \_\_\_\_\_ COUNTY) Before me, the undersigned authority, came the grantor who is of sound mind and eighteen (18) years of age, or older, and acknowledged that he voluntarily dated and signed this writing or directed it to be signed and dated as above. Done this \_\_\_\_ day of \_\_\_\_\_, 19\_\_\_. Signature of Notary Public or other officer. Date commission expires: \_\_\_\_\_ Execution of this document restricts withholding and withdrawing of some medical procedures. Consult Kentucky Revised Statutes or your attorney." (2) An advance directive shall be in writing, dated, and signed by the grantor, or at the grantor's direction, and either witnessed by two (2) or more adults in the presence of the grantor and in the presence of each other, or acknowledged before a notary public or other person authorized to administer oaths. None of the following shall be a witness to or serve as a notary public or other person authorized to administer oaths in regard to any advance directive made under this section: (a) A blood relative of the grantor; (b) A beneficiary of the grantor under descent and distribution statutes of the Commonwealth; (c) An employee of a health care facility in which the grantor is a patient, unless the employee serves as a notary public; (d) An attending physician of the grantor; or (e) Any person directly financially responsible for the grantor's health care. (3) A person designated as a surrogate pursuant to an advance directive may resign at any time by giving written notice to the grantor; to the immediate successor surrogate, if any; to the attending physician; and to any health care facility which is then waiting for the surrogate to make a health care decision. (4) An employee, owner, director, or

officer of a health care facility where the grantor is a resident or patient shall not be designated or act as surrogate unless related to the grantor within the fourth degree of consanguinity or affinity or a member of the same religious order.

1. Be sure to follow the guidelines of KRS 311.625(2) regarding who is to witness these documents or to serve as notary.
2. Discuss the ability to included directions for the donations of organs or donations for broader education and scientific purposes may be included in these documents.
3. It is important that if two separate documents are executed, the two documents should be consistent.

## GENERAL POWER OF ATTORNEY

**KNOW EVERYONE BY THESE PRESENTS**, which are intended to constitute a Durable General Power of Attorney, **THAT I, Sample Client**, having an address at \_\_\_\_\_, hereby make, constitute and appoint **Joe Sample**, having an address at \_\_\_\_\_, or if **Joe Sample** is unable, unwilling or unavailable to act, then **Mary Sample**, having an address at \_\_\_\_\_, as my attorney-in-fact TO ACT in my name, place and stead in any way which I could do, if I were personally present, to the extent that I am permitted by law to act through an agent:

(a) to ask, demand, sue for, recover and receive all manner of goods, chattels, debts, rents, interest, sums of money and demands whatsoever, due or to become due, and to execute, acknowledge and deliver acquittances, receipts, releases, satisfactions or other discharges for the same;

(b) to make, execute, endorse, accept and deliver in my name or in the name of my attorney-in-fact all checks, notes, drafts, warrants, securities, stock certificates, certificates of deposit, bonds, acknowledgments, and any other agreements, certificates or instruments of any nature, as my attorney-in-fact may deem necessary or appropriate;

(c) to cause securities or other property to be held or registered in the name of a nominee or nominees or in any other form; to vote any and all shares of stock or other securities and to execute proxies or other instruments with respect to such stock or securities;

(d) to deposit and withdraw any sums to or from any bank, savings or similar account maintained by me; to open or cause to be opened any safe deposit box in my name and to examine and remove any or all of the contents of such box; and to conduct such other banking transactions as my attorney-in-fact may deem necessary or appropriate;

(e) to deal with all matters relating to insurance, including the procurement and maintenance thereof; however, notwithstanding the powers given my attorney-in-fact in this and other provisions of this power of attorney, my attorney-in-fact shall have no incidents of ownership in any life insurance policy in which I own an interest and which insures the life of my attorney-in-fact;

(f) to enter and take possession of any real or personal property belonging to me or to which I may be entitled, and to receive and take for me and in my name any rents, issues and profits of any such property; and to purchase, invest in, reinvest in, sell, exchange, lease, grant options upon, convey, assign, transfer, encumber or otherwise dispose of any real or personal



property of any nature and wherever situate; and to execute, acknowledge and deliver all contracts, deeds, leases, mortgages, transfers to trusts, bills of sale, assignments, extensions, satisfactions, releases, waivers, consents, and any other agreements, writings and instruments of any nature affecting any real or personal property, as my attorney-in-fact may deem necessary or appropriate;

(g) to commence any actions or proceedings, for the recovery of any real or personal property or for any other purpose; to appear in, answer and defend any actions or proceedings commenced against me; and to prosecute, maintain, appeal, discontinue, compromise, settle and adjust all actions, proceedings, accounts, dues and demands that now or hereafter may exist, as my attorney-in-fact may deem necessary or appropriate;

(h) to create, amend or terminate one or more trusts, partnerships, corporations, co-tenancies or any other form of ownership or entity for the purpose of dealing with any property or property interest of any nature that I may have or hereafter acquire, under such terms and with such provisions as my attorney-in-fact may deem necessary or appropriate; and to transfer any or all property in which I have an interest into any trusts, partnerships, corporations, co-tenancies or other entities, whether created by me or my attorney-in-fact or otherwise (and, in this regard, that my attorney-in-fact may be a remainderman, partner, shareholder, co-tenant or beneficiary of any such entity shall not affect the validity of any action hereunder, and shall not, by itself, constitute a breach of fiduciary duty); and to remove property from any such entity; and to give to any such entity, or to any person acting as agent or trustee under any instrument executed by me or on my behalf, such instructions or authorizations as I may have the right to give;

(i) to take all steps and remedies necessary or appropriate for the conduct and management of my business and personal affairs, and for recovering, obtaining and holding all real or personal property including debts, interest, demands, duties, sums of money or any other things whatsoever, as aforesaid, that are thought to be due, owing, belonging or payable to me in my own right or otherwise;

(j) to employ such agents, attorneys, accountants, investment counsel, trustees, caretakers and other persons and entities, and to delegate duties hereunder and pay such compensation, as my attorney-in-fact may deem necessary or appropriate; and

(k) to do, execute, perform and finish for me and in my name all things which my attorney-in-fact shall deem necessary or appropriate, in and about or concerning my property or any part thereof.

In addition, I specifically authorize my attorney-in-fact to make gifts, outright or in trust, of my property to or for the benefit of such persons within the class of permitted donees hereafter described as, in the opinion of my attorney-in-fact, would be the donees I might choose, having in mind the resources, both public and private, available for my care after the making of such gifts, and having in mind the objective of preserving the largest amount of my property for my family as a whole. The class of permitted donees shall consist solely of my wife, my children and more remote issue, the spouses of my children and more remote issue, or any custodian or guardian for the benefit of any of the foregoing or any trust for the benefit of any of the foregoing. The gifts to each donee shall not exceed in aggregate, in any calendar year, the amount excludible from gifts for gift tax purposes by virtue of Section 2503(b) of the Internal Revenue Code, or any successor thereto, in effect in the year in question (currently \$10,000 subject to adjustment for inflation), provided that during any time that I am married the gift to each donee shall not exceed twice the amount so excludible (currently \$20,000 subject to adjustment for inflation). I authorize my attorney-in-fact to consent to splitting gifts with my wife so that the annual exclusions, unified credits, and generation-skipping transfer tax exemptions and exclusions of both my wife and myself may be used. Gifts in excess of said limit may be made to pay tuition costs and medical expenses so long as the payment of such gifts is made in a manner so as not to be subject to gift or generation-skipping transfer taxes pursuant to Sections 2503(e) and 2611(b)(1) of the Internal Revenue Code, or any successor thereto. Notwithstanding the foregoing, any gifts that are made to my attorney-in-fact, or to the creditors of my attorney-in-fact, or to the estate of my attorney-in-fact, or to the creditors of the estate of my attorney-in-fact, pursuant to the foregoing power (1) shall in no event exceed in aggregate (with respect to each attorney-in-fact) the greater of \$5,000 or five percent of all assets subject to this power in a given calendar year, on a non-cumulative basis, and (2) may be made only during the first ninety (90) days after the effective date of this power of attorney or during the first ninety (90) days of each calendar year thereafter while this power of attorney is in effect.

In addition, I specifically authorize my attorney-in-fact to revoke or amend any revocable living trust which I have heretofore or hereafter establish.

In addition, I specifically authorize my attorney-in-fact to transfer any property or funds to the trustees of the following trust: Sample Client Living trust, dated July \_\_\_, 2002.

In addition, I specifically authorize my attorney-in-fact to deal with tax authorities, to execute and sign on my behalf any and all Federal, state, local and foreign income and gift tax returns, including estimated returns and interest, dividends, gains and transfer returns, for all periods between 1975 and 2050, and to pay any taxes, penalties and interest due thereon; to allocate generation-skipping transfer tax exemptions (within the meaning of Section 2642(a) of the Internal Revenue Code) and to make tax elections; to represent me or to sign an Internal Revenue Service Form 2848 (Power of Attorney or Declaration of Representative) or Form 8821 (Tax Information Authorization), or comparable authorization, appointing a qualified lawyer, certified public accountant or

enrolled agent (including my attorney-in-fact if so qualified) to represent me before any office of the Internal Revenue Service or any state, local or foreign taxing authority with respect to the types of taxes and years referred to above, and to specify on said authorization said types of taxes and years; to receive from or inspect confidential information in any office of the Internal Revenue Service or state, local or foreign tax authority; to receive and deposit, in any one of my bank accounts, or those of any revocable trust of mine, checks in payment of any refund of Federal, state, local or foreign taxes, penalties and interest; to pay by check drawn on any bank account of mine or of any revocable trust of mine and have accounts to permit my attorney-in-fact to draw checks for payment of said items; to execute waivers (and offers of waivers) of restrictions on assessment or collection of deficiencies in taxes and waivers of notice of disallowance of a claim for credit or refund; to execute consents extending the statutory period for assessment or collection of such taxes; to execute offers in compromise and closing Agreements under Section 7121 or comparable provisions of the Internal Revenue Code or any Federal, state, local or foreign tax statutes or regulations; to delegate authority or to substitute another representative for any one previously appointed by me or my attorney-in-fact; and to receive copies of all notices and other written communications involving my Federal, state, local or foreign taxes at such address as my attorney-in-fact may designate.

In addition, I authorize my attorney-in-fact to make voluntary contributions to, transfer assets between, and withdraw amounts from any qualified retirement benefit plan or IRA; to waive spousal rights on any such plan or IRA; to make elections with respect to the timing, method and amounts of withdrawals, distributions and/or rollovers, methods of calculating minimum required distributions, and methods of distribution as a beneficiary of another's plan or IRA; and to take any other actions with respect to any such plan or IRA as I could take.

This power of attorney is a durable power of attorney, and it shall not be affected by my becoming disabled, incompetent or incapacitated or the lapse of time. It is my intent that the authority conferred herein shall be exercisable notwithstanding my physical disability or mental incompetence.

It is my desire and request that no guardian or conservator of my person or property be appointed in the event of my disability or incapacity. If, however, a guardian or conservator of my person or property is to be appointed for me, I hereby nominate and appoint my attorney-in-fact hereunder to serve as guardian and conservator without bond.

To induce any third party to act hereunder, I hereby agree that any third party receiving a duly executed copy or facsimile of this power of attorney may act hereunder, and that revocation or termination hereof shall be ineffective as to such third party unless and until actual notice or knowledge of such revocation or termination shall have been received by such third party. I, for myself and my heirs, executors, legal representatives and assigns, hereby agree to indemnify and hold harmless any such third party from and against any and all claims that may arise against such third party by reason of such third

**IN WITNESS WHEREOF**, I have executed this power of attorney this \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_.

---

**B - 13**



## SPRINGING GENERAL POWER OF ATTORNEY

**KNOW EVERYONE BY THESE PRESENTS**, which are intended to constitute a General Power of Attorney, **THAT I, Sample Client**, having an address at \_\_\_\_\_, hereby make, constitute and appoint **Joe Sample**, having an address at \_\_\_\_\_, or if **Joe Sample** is unable, unwilling or unavailable to act, then **Mary Sample**, having an address at \_\_\_\_\_, as my attorney-in-fact TO ACT in my name, place and stead in any way which I could do, if I were personally present, to the extent that I am permitted by law to act through an agent:

(a) to ask, demand, sue for, recover and receive all manner of goods, chattels, debts, rents, interest, sums of money and demands whatsoever, due or to become due, and to execute, acknowledge and deliver acquittances, receipts, releases, satisfactions or other discharges for the same;

(b) to make, execute, endorse, accept and deliver in my name or in the name of my attorney-in-fact all checks, notes, drafts, warrants, securities, stock certificates, certificates of deposit, bonds, acknowledgments, and any other agreements, certificates or instruments of any nature, as my attorney-in-fact may deem necessary or appropriate;

(c) to cause securities or other property to be held or registered in the name of a nominee or nominees or in any other form; to vote any and all shares of stock or other securities and to execute proxies or other instruments with respect to such stock or securities;

(d) to deposit and withdraw any sums to or from any bank, savings or similar account maintained by me; to open or cause to be opened any safe deposit box in my name and to examine and remove any or all of the contents of such box; and to conduct such other banking transactions as my attorney-in-fact may deem necessary or appropriate;

(e) to deal with all matters relating to insurance, including the procurement and maintenance thereof; however, notwithstanding the powers given my attorney-in-fact in this and other provisions of this power of attorney, my attorney-in-fact shall have no incidents of ownership in any life insurance policy in which I own an interest and which insures the life of my attorney-in-fact;

(f) to enter and take possession of any real or personal property belonging to me or to which I may be entitled, and to receive and take for me and in my name any rents, issues and profits of any such property; and to purchase, invest in, reinvest in, sell, exchange, lease, grant options upon, convey, assign, transfer, encumber or otherwise dispose of any real or personal

property of any nature and wherever situate; and to execute, acknowledge and deliver all contracts, deeds, leases, mortgages, transfers to trusts, bills of sale, assignments, extensions, satisfactions, releases, waivers, consents, and any other agreements, writings and instruments of any nature affecting any real or personal property, as my attorney-in-fact may deem necessary or appropriate;

(g) to commence any actions or proceedings, for the recovery of any real or personal property or for any other purpose; to appear in, answer and defend any actions or proceedings commenced against me; and to prosecute, maintain, appeal, discontinue, compromise, settle and adjust all actions, proceedings, accounts, dues and demands that now or hereafter may exist, as my attorney-in-fact may deem necessary or appropriate;

(h) to create, amend or terminate one or more trusts, partnerships, corporations, co-tenancies or any other form of ownership or entity for the purpose of dealing with any property or property interest of any nature that I may have or hereafter acquire, under such terms and with such provisions as my attorney-in-fact may deem necessary or appropriate; and to transfer any or all property in which I have an interest into any trusts, partnerships, corporations, co-tenancies or other entities, whether created by me or my attorney-in-fact or otherwise (and, in this regard, that my attorney-in-fact may be a remainderman, partner, shareholder, co-tenant or beneficiary of any such entity shall not affect the validity of any action hereunder, and shall not, by itself, constitute a breach of fiduciary duty); and to remove property from any such entity; and to give to any such entity, or to any person acting as agent or trustee under any instrument executed by me or on my behalf, such instructions or authorizations as I may have the right to give;

(i) to take all steps and remedies necessary or appropriate for the conduct and management of my business and personal affairs, and for recovering, obtaining and holding all real or personal property including debts, interest, demands, duties, sums of money or any other things whatsoever, as aforesaid, that are thought to be due, owing, belonging or payable to me in my own right or otherwise;

(j) to employ such agents, attorneys, accountants, investment counsel, trustees, caretakers and other persons and entities, and to delegate duties hereunder and pay such compensation, as my attorney-in-fact may deem necessary or appropriate; and

(k) to do, execute, perform and finish for me and in my name all things which my attorney-in-fact shall deem necessary or appropriate, in and about or concerning my property or any part thereof.

In addition, I specifically authorize my attorney-in-fact to make gifts, outright or in trust, of my property to or for the benefit of such persons within the class of permitted donees hereafter described as, in the opinion of my attorney-in-fact, would be the donees I might choose, having in mind the resources, both public and private, available for my care after the making of such gifts, and having in mind the objective of preserving the largest amount of my property for my family as a whole. The class of permitted donees shall consist solely of my wife, my children and more remote issue, the spouses of my children and more remote issue, or any custodian or guardian for the benefit of any of the foregoing or any trust for the benefit of any of the foregoing. The gifts to each donee shall not exceed in aggregate, in any calendar year, the amount excludible from gifts for gift tax purposes by virtue of Section 2503(b) of the Internal Revenue Code, or any successor thereto, in effect in the year in question (currently \$10,000 subject to adjustment for inflation), provided that during any time that I am married the gift to each donee shall not exceed twice the amount so excludible (currently \$20,000 subject to adjustment for inflation). I authorize my attorney-in-fact to consent to splitting gifts with my wife so that the annual exclusions, unified credits, and generation-skipping transfer tax exemptions and exclusions of both my wife and myself may be used. Gifts in excess of said limit may be made to pay tuition costs and medical expenses so long as the payment of such gifts is made in a manner so as not to be subject to gift or generation-skipping transfer taxes pursuant to Sections 2503(e) and 2611(b)(1) of the Internal Revenue Code, or any successor thereto. Notwithstanding the foregoing, any gifts that are made to my attorney-in-fact, or to the creditors of my attorney-in-fact, or to the estate of my attorney-in-fact, or to the creditors of the estate of my attorney-in-fact, pursuant to the foregoing power (1) shall in no event exceed in aggregate (with respect to each attorney-in-fact) the greater of \$5,000 or five percent of all assets subject to this power in a given calendar year, on a non-cumulative basis, and (2) may be made only during the first ninety (90) days after the effective date of this power of attorney or during the first ninety (90) days of each calendar year thereafter while this power of attorney is in effect.

In addition, I specifically authorize my attorney-in-fact to revoke or amend any revocable living trust which I have heretofore or hereafter establish.

In addition, I specifically authorize my attorney-in-fact to transfer any property or funds to the trustees of the following trust: Sample Client Living trust, dated July \_\_\_, 2002.

In addition, I specifically authorize my attorney-in-fact to deal with tax authorities, to execute and sign on my behalf any and all Federal, state, local and foreign income and gift tax returns, including estimated returns and interest, dividends, gains and transfer returns, for all periods between 1975 and 2050, and to pay any taxes, penalties and interest due thereon; to allocate generation-skipping transfer tax exemptions (within the meaning of Section 2642(a) of the Internal Revenue Code) and to make tax elections; to represent me or to sign an Internal Revenue Service Form 2848 (Power of Attorney or Declaration of Representative) or Form 8821 (Tax Information Authorization), or comparable authorization, appointing a qualified lawyer, certified public accountant or



enrolled agent (including my attorney-in-fact if so qualified) to represent me before any office of the Internal Revenue Service or any state, local or foreign taxing authority with respect to the types of taxes and years referred to above, and to specify on said authorization said types of taxes and years; to receive from or inspect confidential information in any office of the Internal Revenue Service or state, local or foreign tax authority; to receive and deposit, in any one of my bank accounts, or those of any revocable trust of mine, checks in payment of any refund of Federal, state, local or foreign taxes, penalties and interest; to pay by check drawn on any bank account of mine or of any revocable trust of mine and have accounts to permit my attorney-in-fact to draw checks for payment of said items; to execute waivers (and offers of waivers) of restrictions on assessment or collection of deficiencies in taxes and waivers of notice of disallowance of a claim for credit or refund; to execute consents extending the statutory period for assessment or collection of such taxes; to execute offers in compromise and closing Agreements under Section 7121 or comparable provisions of the Internal Revenue Code or any Federal, state, local or foreign tax statutes or regulations; to delegate authority or to substitute another representative for any one previously appointed by me or my attorney-in-fact; and to receive copies of all notices and other written communications involving my Federal, state, local or foreign taxes at such address as my attorney-in-fact may designate.

In addition, I authorize my attorney-in-fact to make voluntary contributions to, transfer assets between, and withdraw amounts from any qualified retirement benefit plan or IRA; to waive spousal rights on any such plan or IRA; to make elections with respect to the timing, method and amounts of withdrawals, distributions and/or rollovers, methods of calculating minimum required distributions, and methods of distribution as a beneficiary of another's plan or IRA; and to take any other actions with respect to any such plan or IRA as I could take.

This power of attorney shall take effect upon my becoming physically disabled, mentally incompetent or otherwise incapacitated. Any third party may rely upon the written declaration of my attorney-in-fact that such contingency has occurred.

It is my desire and request that no guardian or conservator of my person or property be appointed in the event of my disability or incapacity. If, however, a guardian or conservator of my person or property is to be appointed for me, I hereby nominate and appoint my attorney-in-fact hereunder to serve as guardian and conservator without bond.

To induce any third party to act hereunder, I hereby agree that any third party receiving a duly executed copy or facsimile of this power of attorney may act hereunder, and that revocation or termination hereof shall be ineffective as to such third party unless and until actual notice or knowledge of such revocation or termination shall have been received by such third party. I, for myself and my heirs, executors, legal representatives and assigns, hereby agree to indemnify and hold harmless any such third party from and against any and all claims that may arise against such third party by reason of such third party having relied upon the provisions of this power of attorney.

## SAMPLE CLIENT

---

**B - 19**



## LIVING WILL DIRECTIVE

Directive made this \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_.

I, **Sample Client**, presently residing at \_\_\_\_\_, and being an adult of sound mind, willfully and voluntarily make known my desire that my life shall not be artificially prolonged under the circumstances set forth below, and I hereby declare:

If at any time I have a terminal condition or become permanently unconscious, I direct that life-prolonging treatment be withheld and withdrawn and that I be permitted to die naturally with only the administration of medication or the performance of any medical procedure deemed necessary to keep me comfortable and to relieve pain. The procedures and treatment to be withheld and withdrawn include, without limitation, surgery, antibiotics, cardiac and pulmonary resuscitation, and respiratory support.

I realize that situations could arise in which the only way to allow me to die would be to discontinue artificial nutrition and hydration. In carrying out any instruction I have given hereunder, I authorize that artificial nutrition and hydration not be started or, if started, be discontinued. (yes) (no) (Circle your choice and initial below.)

Initials: \_\_\_\_\_

If, upon my death, any of my tissue or organs would be of value for transplantation, therapy, advancement of medical or dental science, research, or other medical, educational or scientific purpose as specified in KRS 311.185, I freely give my permission to the donation of such tissue or organs pursuant to KRS 311.185.

In the absence of my ability to give directions regarding the use of life-prolonging treatment, it is my intention that this directive shall be honored by my family, physicians, health care facilities and all concerned with my care as the final expression of my legal right to refuse medical or surgical treatment including without limitation the administration of life-prolonging treatment. I accept the consequences of such refusal.

I understand the full import and meaning of this directive, and I am aware that this directive authorizes a physician to withhold and withdraw life-prolonging treatment. I am at least eighteen years of age and I am emotionally and mentally competent to make this directive.

---

**SAMPLE CLIENT**



Prepared By:

---

Melissa H.P. Palmer  
Rigsby Law Group, PLC  
P.O. Box 34106  
Lexington, Kentucky 40588-4106

**NOTICE AND WARNING TO PERSON EXECUTING THIS DOCUMENT --**

**THIS IS AN IMPORTANT LEGAL DOCUMENT.** BEFORE EXECUTING THIS DOCUMENT YOU SHOULD KNOW THESE IMPORTANT FACTS:

EXCEPT AS YOU OTHERWISE SPECIFY IN THIS DOCUMENT, THIS DOCUMENT GIVES THE PERSON YOU DESIGNATE AS YOUR HEALTH CARE SURROGATE THE POWER TO MAKE HEALTH CARE DECISIONS FOR YOU WHEN YOU ARE NO LONGER CAPABLE OF MAKING HEALTH CARE DECISIONS FOR YOURSELF. YOUR HEALTH CARE SURROGATE MUST ACT CONSISTENTLY WITH YOUR DESIRES AS STATED IN THIS DOCUMENT OR OTHERWISE MADE KNOWN. UNLESS YOU STATE OTHERWISE, YOUR HEALTH CARE SURROGATE HAS THE SAME AUTHORITY TO MAKE DECISIONS ABOUT YOUR HEALTH CARE AS YOU WOULD HAVE HAD.

YOUR HEALTH CARE SURROGATE HAS THE POWER TO MAKE A BROAD RANGE OF HEALTH CARE DECISIONS FOR YOU. THE PERSON YOU APPOINT AS YOUR HEALTH CARE SURROGATE SHOULD BE SOMEONE YOU KNOW AND TRUST. YOU SHOULD DISCUSS THIS DOCUMENT WITH YOUR HEALTH CARE SURROGATE.

EXCEPT AS YOU OTHERWISE SPECIFY IN THIS DOCUMENT, THIS DOCUMENT GIVES YOUR HEALTH CARE SURROGATE THE POWER TO CONSENT TO YOUR PHYSICIAN NOT GIVING TREATMENT OR STOPPING TREATMENT NECESSARY TO KEEP YOU ALIVE.

NOTWITHSTANDING THIS DOCUMENT, YOU HAVE THE RIGHT TO MAKE MEDICAL AND OTHER HEALTH CARE DECISIONS FOR YOURSELF SO LONG AS YOU CAN GIVE INFORMED CONSENT WITH RESPECT TO THE PARTICULAR DECISION. NO TREATMENT MAY BE GIVEN TO YOU OVER YOUR OBJECTION AT THE TIME, AND HEALTH CARE NECESSARY TO KEEP YOU ALIVE MAY NOT BE STOPPED OR WITHHELD IF YOU OBJECT AT THE TIME.

THIS DOCUMENT GIVES YOUR HEALTH CARE SURROGATE AUTHORITY TO CONSENT, TO REFUSE TO CONSENT, OR TO WITHDRAW CONSENT TO ANY CARE, TREATMENT, SERVICE, OR PROCEDURE TO MAINTAIN, DIAGNOSE, OR TREAT A PHYSICAL OR MENTAL CONDITION. THIS POWER IS SUBJECT TO ANY STATEMENT OF YOUR DESIRES AND ANY LIMITATIONS THAT YOU INCLUDE IN THIS DOCUMENT. YOU MAY SPECIFY IN THIS DOCUMENT ANY TYPES OF TREATMENT THAT YOU DO OR DO NOT DESIRE.

IN ADDITION, A COURT CAN TAKE AWAY THE POWER OF YOUR HEALTH CARE SURROGATE TO MAKE HEALTH CARE DECISIONS FOR YOU IF YOUR HEALTH CARE SURROGATE AUTHORIZES ANYTHING THAT IS ILLEGAL, OR ACTS CONTRARY TO YOUR KNOWN DESIRES AS STATED IN THIS DOCUMENT.

YOU HAVE THE RIGHT TO REVOKE THE AUTHORITY OF YOUR HEALTH CARE SURROGATE OR TO REVOKE THIS DOCUMENT ENTIRELY BY NOTIFYING YOUR

HEALTH CARE SURROGATE OR YOUR ATTENDING PHYSICIAN, HOSPITAL, OR OTHER HEALTH CARE PROVIDER ORALLY OR IN WRITING OF THE REVOCATION.

THIS DOCUMENT REVOKES ANY PRIOR DURABLE POWER OF ATTORNEY FOR HEALTH CARE, UNLESS YOU INDICATE OTHERWISE IN THIS DOCUMENT.

UNLESS YOU OTHERWISE SPECIFY IN THIS DOCUMENT, THIS DOCUMENT GIVES YOUR HEALTH CARE SURROGATE THE POWER AFTER YOU DIE TO DONATE YOUR BODY OR PARTS THEREOF FOR TRANSPLANT OR THERAPEUTIC, EDUCATIONAL OR SCIENTIFIC PURPOSES, AND TO DIRECT THE DISPOSITION OF YOUR REMAINS.

IT IS IMPORTANT THAT YOU UNDERSTAND THE NATURE AND RANGE OF DECISIONS THAT MAY BE MADE ON YOUR BEHALF. IF THERE IS ANYTHING IN THIS DOCUMENT THAT YOU DO NOT UNDERSTAND, YOU SHOULD ASK YOUR ATTORNEY OR PHYSICIAN TO EXPLAIN IT TO YOU. YOU SHOULD DISCUSS THIS DOCUMENT WITH YOUR HEALTH CARE SURROGATE.

YOUR HEALTH CARE SURROGATE MAY NEED THIS DOCUMENT IMMEDIATELY IN CASE OF AN EMERGENCY THAT REQUIRES A DECISION CONCERNING YOUR HEALTH CARE. EITHER KEEP THIS DOCUMENT WHERE IT IS IMMEDIATELY AVAILABLE TO YOUR HEALTH CARE SURROGATE AND ALTERNATE HEALTH CARE SURROGATE OR GIVE EACH OF THEM AN EXECUTED COPY OF THIS DOCUMENT. YOU ALSO MAY WANT TO GIVE YOUR PHYSICIAN AN EXECUTED COPY OF THIS DOCUMENT.





## DESIGNATION OF HEALTH CARE SURROGATE

**TO:** My family, physicians and all  
those concerned with my care

I, **Sample Client**, presently residing at \_\_\_\_\_, and being an adult of sound mind, hereby appoint and authorize my wife, **Mrs. Sample Client**, presently residing at \_\_\_\_\_, or if my wife is unable, unwilling or unavailable to act, then **Joe Sample**, presently residing at \_\_\_\_\_, as my health care surrogate to act for me and in my name to make and communicate any and all decisions about or relating to my receipt or refusal to accept medical treatment, hospitalization, health care or personal care, in any situation in which, as the result of illness, disease, mental deterioration or injury, I am incapable of making or communicating a decision with respect to my treatment or care. This authorization includes the right to refuse and direct the withdrawal of medical treatment which would prolong my life, and to communicate health care decisions to all persons including without limitation my physicians, health care providers and family.

If at any time I have a terminal condition or become permanently unconscious, I direct that life-prolonging treatment be withheld and withdrawn and that I be permitted to die naturally with only the administration of medication or the performance of any medical procedure deemed necessary to keep me comfortable and to relieve pain. The procedures and treatment to be withheld and withdrawn include, without limitation, surgery, antibiotics, cardiac and pulmonary resuscitation, and respiratory support.

I realize that situations could arise in which the only way to allow me to die would be to discontinue artificial nutrition and hydration. In carrying out any instruction I have given hereunder, I authorize that artificial nutrition and hydration not be started or, if started, be discontinued. (yes) (no) (Circle your choice and initial below.)

Initials: \_\_\_\_\_

I further delegate to my health care surrogate the power and authority to select, employ and discharge health care personnel, such as physicians, nurses, therapists, hospice care and home health care providers, and other medical professionals; to admit or discharge me (including transfer from another facility) from any hospital, hospice, nursing home, adult home or other medical care facility; and to apply for public benefits to defray the cost of health care, and to contract in my name and on my behalf for all health care services, including without limitation medical, nursing and hospital care, as my health care surrogate may deem appropriate. I confirm that I shall be and remain personally liable for the payment of all such care and services to the same extent as if I had personally contracted therefor.

I authorize my health care surrogate to donate all or any part of my body for transplantation, therapy, advancement of medical or dental science, research, or other medical, educational or scientific purpose, or to otherwise direct the disposition of my

remains.

I further authorize my health care surrogate to request, receive and review any information regarding my physical or mental health, including without limitation medical and hospital records; to execute on my behalf any releases or other documents that may be required in order to obtain this information; and to consent to the disclosure of this information. I authorize my health care surrogate to execute on my behalf any documents necessary or desirable to implement the health care decisions that my health care surrogate is authorized to make pursuant to this document, including without limitation all documents pertaining to a refusal to permit medical treatment, or authorizing the leaving of a medical facility against medical advice, or any waivers or releases from liability required by a physician or health care provider.

This document is a durable power of attorney and the authority of my health care surrogate shall not terminate if I become disabled, incompetent or incapacitated.

Any designation of a health care surrogate which I previously executed is hereby revoked.

**IN WITNESS WHEREOF**, I have executed this instrument, as my free and voluntary act and deed, this        day of \_\_\_\_\_, 20\_\_\_\_.

\_\_\_\_\_  
**SAMPLE CLIENT**

We, \_\_\_\_\_ and \_\_\_\_\_, the witnesses, each hereby attest and declare under penalty of perjury under the laws of the Commonwealth of Kentucky that: (1) the foregoing instrument was personally signed by Sample Client in my presence, and thereupon I, at his request and in his presence and in the presence of the other witnesses, have hereunto subscribed my name as a witness; (2) I did not sign the above signature of Sample Client for or at his direction; (3) I personally know Sample Client and believe him to be of sound mind and under no constraint, duress, fraud or undue influence; (4) I am not related to Sample Client by blood, marriage or adoption; (5) I am not entitled (to the best of my knowledge and belief) to any portion of the estate of Sample Client upon his death under any will or codicil of Sample Client or by operation of law; (6) I do not have any present or inchoate claim against any portion of the estate of Sample Client; (7) I do not have any financial responsibility for the medical care of Sample Client; (8) I am not a physician or an employee of any physician, and I am not an operator or employee of, or patient in, any hospital, health care provider, residential care facility, community care facility or similar institution; (9) I am not a person named as health care surrogate in this instrument; and (10) I and Sample Client are both at least 18 years of age.

Dated: \_\_\_\_\_, 2002

---

COMMONWEALTH OF KENTUCKY )  
 )SS  
COUNTY OF \_\_\_\_\_ )

SUBSCRIBED, SWORN TO, AND ACKNOWLEDGED before me, the undersigned authority, a notary public within and for the State and County aforesaid, by **Sample Client**, known personally to me and who personally appeared before me and subscribed, swore to, and acknowledged the foregoing instrument as his free and voluntary act and deed on this      day of \_\_\_\_\_, 20\_\_\_\_.

**My commission expires:**

Notary Public  
Commonwealth of Kentucky

Prepared By:

Melissa H.P. Palmer  
Rigsby Law Group, PLC  
P.O. Box 34106  
Lexington, Kentucky 40588-4106



# **“THINGS YOU GOTTA KNOW ABOUT MARITAL DEDUCTIONS”**

*Paul J. Dyar  
Wyatt, Tarrant & Combs, LLP  
Louisville, Kentucky*

Copyright 2002. Paul J. Dyar. All Rights Reserved.

## **SECTION C**



## **“THINGS YOU GOTTA KNOW ABOUT MARITAL DEDUCTIONS”**

INTRODUCTION .....	C-1
I. Requirements For Marital Deduction .....	C-2
A. Legally Married At Time Of Death .....	C-2
B. Survivorship Requirement For Spouse .....	C-2
C. Surviving Spouse Must Be A U.S. Citizen .....	C-2
D. Interest Passing To Surviving Spouse Must Be Includable In Decedent's U.S. Gross Estate .....	C-2
E. Passing Requirement .....	C-3
F. Not A Nondeductible Terminable Interest .....	C-3
II. Devices For The Use Of The Marital Deduction .....	C-4
A. Disclaimers Under IRC Section 2518 .....	C-4
B. QTIP Trust .....	C-6
C. Life Estate With Power Of Appointment .....	C-7
D. Qualified Domestic Trusts (“QDOT”) .....	C-7
E. Formulas Used To Fund Marital Deductions .....	C-9
III. Effect Of EGTRRA On The Marital Deduction .....	C-10
A. Changes Made By EGTRRA .....	C-10
B. Effect Of EGTRRA On Marital Deduction Formulas .....	C-11
C. Drafting Ideas With EGTRRA In Mind .....	C-12





## **Introduction**

The marital deduction under Internal Revenue Code of 1986, as amended ("IRC"), § 2056 is one of most basic tools of any estate plan. If all the requirements of the deduction are satisfied, the deduction is unlimited. However, for the most part, the marital deduction is a deferral of tax from the death of the first to die until the surviving spouse's death and not an exclusion of tax. The rules for the marital deduction are the same for estate and gift tax. The following is a brief discussion of the requirements of the marital deduction along with a discussion of the effects of the "Economic Growth and Tax Relief Reconciliation Act of 2001" ("EGTRRA") on the use of the marital deduction.

I. Requirements for Marital Deduction

- A. Decedent must be legally married at the time of his or her death.
  - 1. Validity and existence of marriage is a question of local law, such as common law marriages.
  - 2. Marriage continues until a final divorce decree is entered by the court. Eccles v. Commissioner 19 T.C. 1049 (1953), aff'd on other grounds, 208 F2d 796 (4th Cir. 1954).
- B. Survivorship Requirement for Spouse.
  - 1. Local law will govern the determination of survivorship in the case of simultaneous death and in the absence of provision in the decedent's will.
  - 2. Uniform Simultaneous Death Act presumes that each spouse survived the other, which results in each estate receiving one half of the joint property.
- C. Surviving Spouse Must be a U.S. Citizen
  - 1. The surviving spouse must be or become a U.S. citizen by the time the federal estate tax return is filed.
  - 2. In the absence of citizenship, the marital deduction is allowed only for property placed in a qualified domestic trust ("QDOT") before the estate tax is filed.
- D. Interest Passing to Surviving Spouse Must be Includable in Decedent's U.S. Gross Estate.
  - 1. An interest is nondeductible to the extent that it is not included in the decedent's gross estate.
  - 2. Examples of property not included in gross estate are property subject to a special power of appointment and irrevocable life insurance trust.

E. Passing Requirement.

1. "Passing" is defined broadly to include almost any way in which a surviving spouse may receive assets of a decedent as a result of the decedent's own action or as a result of the spouse's exercise of rights under local law, such as dower, curtesy, or inheritance. IRC §2056(c).
2. The requirement generally is not satisfied if the spouse's interest is created by the action of third parties. See, e.g. Estate of Dowell, 72 TCM 1155 (1996), Estate of Allen 60 TCM 904 (1990).

F. Not a Nondeductible Terminable Interest.

1. Terminable interest defined as an interest in property that will terminate or fail with "the lapse of time on the occurrence of an event or contingency to occur." IRC §2056(b)(1).
2. A terminable interest is nondeductible if the result is to allow someone else to possess or enjoy any of the property after the termination of the spouse's interest without giving full consideration for his or her interest. IRC §2056(b)(1).
3. Examples of Terminable Interests
  - a. Credit shelter trust which benefits the surviving spouse during his or her lifetime but which the distribution of corpus and income is discretionary to the trustee.
  - b. Life estates are generally nondeductible terminable interests unless they satisfy the qualified terminable interest property requirements or are coupled with a general power of appointment.
  - c. Spousal allowances and similar claims generally are deductible depending on the state law. If at the termination of the

allowance, the interest passes on to the spouse's estate then it will be deductible.

- d. Interests acquired for the spouse for the executor are nondeductible terminable interests even though no interest in the property subject to the terminable interest passes to anyone other than the spouse.
- e. Joint wills may create a nondeductible terminable interest if under state law the surviving spouse has a legal obligation to comply with the successorship provision in a joint will.

4. Exceptions to Disqualification of Terminate Interests.

- a. Spouse may be required to survive for a limited time of up to six months. IRC §2056(b)(3).
- b. Spouse may be given a life estate in and a general power of appointment over property IRC §2056(b)(5).
- c. A trust may be created exclusively for spouse and his estate.
- d. Spouse may be given an interest in a qualified terminable interest property ("QTIP") trust IRC §2056(b)(7).
- e. Spouse may be given an interest in a qualified charitable remainder trust. IRC §2056(b)(8).

II. Devices for the Use of the Marital Deduction

A. Disclaimers under IRC §2518.

- 1. Requirements under IRC §2518 for a qualified disclaimer.

- a. Must be an irrevocable and unqualified refusal by a person to accept an interest in property.
- b. Must be in writing.
- c. Must be received by the transferor, his or her legal representative or the holder of legal title within 9 months of when the transfer creating the interest is made or within 9 months in which the transferee reaches age 21.
- d. The disclaimant has not accepted the interest or any of its benefits.
- e. As a result of the disclaimer, the interest passes without any direction on the part of the disclaimant and passes either to the spouse of the decedent or to a person other than the person making the disclaimer.

2. Use of Disclaimer in Marital Deduction Planning.

- a. Likely scenario: Leave everything in will outright to the surviving spouse but provide for a credit shelter trust in case the spouse disclaims.
- b. Advantages: Gives spouse flexibility to use up decedent's unified credit yet have use of the property. Spouse can decide if they have enough property.
- c. Disadvantages:
  - (i) Surviving spouse may change his or her mind and be unwilling to disclaim.
  - (ii) Surviving spouse might inadvertently accept benefits before disclaiming, thereby frustrating the attempt to disclaim.
  - (iii) The decision must be made within 9 months after the decedent's death.

B. QTIP Trust

1. Requirements under IRC §2056(b)(7).
  - a. Property which passes from the decedent;
  - b. The surviving spouse has a qualifying income interest for life;
  - c. The decedent's personal representative makes an election to treat the property as QTIP.
  - d. "Qualifying income interest" means the surviving spouse is entitled to all the income from the property and no person has the power to appoint any part of the property to any person other than the surviving spouse.
2. Annuities. A joint and survivor annuity is automatically treated as QTIP if the surviving spouse is the only recipient until the spouse's death, unless an election out is made.
3. Partial Election. A partial election may be made for a portion of potential QTIP property. IRS §2056(b)(7)(C).
4. Reverse QTIP Election. A reverse QTIP election is useful in generation-skipping tax ("GST") situations.
  - a. The first decedent is considered to be the transferor for GST purposes.
  - b. Allows the use of the GST exemptions in both estates.
  - c. Use of three trusts - credit shelter, reverse QTIP and marital deduction.
    - (i) Used when GST exemption is greater than the estate tax exemption.

- (ii) Due to EGTRRA may not need since GST exemption and estate tax exemption are to be the same starting in 2004.

C. Life Estate with Power of Appointment

1. Requirements under IRC 2056(b)(5).

- a. Spouse must be given income for life from the entire interest or a specific portion thereof.
  - (i) Income distribution requirement is satisfied if the trust gives the spouse "substantially that degree of beneficial enjoyment of the trust property during her life that the principles of the law of trusts accord to a ... life beneficiary." Treas. Reg. § 20.2056(5)-5(f)(1).
  - (ii) If the Trustee has discretion over income distributions, the interest does not qualify for the marital deduction.
  - (iii) Must be paid at least annually or at lesser intervals.
- b. Spouse must be given a power to appoint the entire interest, or such specific portion, exercisable in favor of spouse or his or her estate.
  - (i) Spouse must be given a power of appointment that is exercisable by him or her "alone and in all events" IRC § 2056(b)(5).
  - (ii) Power may be inter vivos or testamentary but not need not be both.

D. Qualified Domestic Trusts ("QDOT")

1. Treatment of estate where spouse is non-citizen.

- a. No marital deduction is allowable with respect to property passing to a spouse who is not a citizen except in the case of assets transferred to a QDOT. IRC § 2056(d).



- b. Applies even if non-citizen spouse is a resident of the United States.
- 2. Requirements of a QDOT.
  - a. Trust instrument must require that there be a U.S. Trustee.
  - b. Trust instrument must give the U.S. Trustee the right to withhold the appropriate tax on any principal distributions.
  - c. The trust must be an ordinary trust whose administration is governed by U.S. law.
  - d. Regulations require that the U.S. Trustee be a bank or that the trust post a bond or letter of credit to secure payment of the tax. Treas. Reg. § 20.2056A-2(d).
- 3. QDOT is not an independent means of qualifying for the marital deduction.
  - a. QDOT is an exception to the rule disallowing the marital deduction in the case of a noncitizen spouse.
  - b. In addition to satisfying the QDOT rules, the trust must also satisfy the normal rules for properly qualifying for the estate tax marital deduction.
- 4. Personal representative must elect to qualify a trust as a QDOT.
  - a. Election made on the estate tax return.
  - b. No requirement that the return be timely, but the election cannot be made on a return filed more than one year after the original due date of return including extensions. IRC § 2056A(d)

5. Tax treatment of QDOT

- a. Marital deduction allowed on decedent's estate.
- b. Trust taxed on spouse's death or if it fails to continue to qualify as a QDOT, during spouse's lifetime.
- c. Tax on any principal distributions to spouse unless made because of hardship or to reimburse the spouse for income taxes paid by the spouse on items of income to which the spouse is not entitled.
- d. Taxes are computed by reference to decedent's estate thus effectively postponing the taxes on the decedent's estate.
- e. If spouse is a resident, taxes can be avoided if spouse becomes a citizen before the estate return is filed.

E. Formulas Used to Fund Marital Deductions. Two types of formula clauses - pecuniary and fractional.

1. Pecuniary. A pecuniary formula clause makes a gift of money.

Ex: I give the smallest pecuniary amount that if allowed as a federal estate tax marital deduction, would result in the least possible federal estate tax being payable by reason of my death.

2. Fractional. A fractional share formula clause makes a gift of assets.

Ex: I give a fractional share of my residuary estate of which (a) the numerator is the smallest amount that, if allowed as a federal estate tax marital deduction, would result in the least possible federal estate tax being payable by

reason of my death, and (b) the denominator is the value of my residuary estate as finally determined for federal estate tax purposes.

3. Different forms of Pecuniary Formulas.

- a. "True Worth Pecuniary" is method in which assets distributed in kind are valued at their date of distribution values.
- b. "Fairly Representative Pecuniary" is a method under which each asset is valued for funding purposes at its basis for federal income tax purposes, with the requirement that the assets selected for distribution be fairly representative of the appreciation and depreciation between the decedent's death and the dates of funding of all assets available for distribution.
- c. "Minimum Worth Pecuniary" is a method in which each asset is valued for funding purposes at the lesser of its date of distribution value or its basis for federal income tax purposes.
- d. "Reverse Pecuniary" is a method under which the pecuniary gift is made to the trustee of the nonmarital trust and the residuary estate comprises the marital deduction gift.

III. Effect of EGTRRA on the Marital Deduction

A. Changes made by EGTRRA which effect marital deduction planning.

1. Rate Changes. EGTRRA reduces the estate tax rate as follows:

<u>Year</u>	<u>Rate</u>
2001	55%
2002	50%
2003	49%

2004	48%
2005	47%
2006	46%
2007-2009	45%
2010	0
2011	55%

2. Exemption Amounts. EGTRRA changes the exemption amounts through 2009 as follows:

<u>Year</u>	<u>Estate Tax Exemption Amount</u>
2001	\$695,000
2002-2003	\$1 Million
2004-2005	\$1.5 Million
2006-2008	\$2 Million
2009	\$3.5 Million
2010	N/A
2011	\$1 Million

3. Somewhat related is the rules regarding carryover basis which apply for 2010 when the estate tax is repealed.

- a. Basis of a person acquiring property from a decedent will be the lesser of (1) the adjusted basis of the decedent, or (2) the fair market value of the property at the date of the decedent's death.
- b. There is an allowance of up to \$1.3 Million of step-up in basis for each estate.
- c. Additional allowance of up to \$3 Million step-up in basis for certain transfers to a surviving spouse.

B. Effect of EGTRRA on Marital Deduction Formulas. Wills and other documents may need to be revised due to the effect of the changes of the exemption amount on marital deduction formulas.

1. Disappearing Marital Deduction Bequest. If the will is drafted with a reduced to zero pecuniary bequest -

i.e., having the smallest amount necessary to lower the estate tax to zero - no property would pass under that clause to the surviving spouse once the estate tax was deducted.

2. Disappearing Credit Shelter Bequest. If the will is drafted with a reduced to zero pecuniary applicable exclusion bequest with a residuary marital deduction bequest, if the estate tax is no longer applicable, all the property would pass to the residuary marital bequest.
3. Loss of Marital Bequest Due to Clause Restricting Transfer. If a bequest for a spouse, whether pecuniary or residuary, provides that "the trustee shall not designate any asset as to which my estate would not be allowed a marital deduction," no property would pass under that clause to the surviving spouse if the estate tax is no longer applicable.
4. Lower Marital Bequest with Rise of Exemption Amount. With the exemption equivalent of the unified credit increasing from \$675,000 to \$3,500,000 the amount passing under a reduced to zero pecuniary marital deduction bequest will be increased to \$2,825,000. This may not be consistent with the intentions of the decedent.

C. Drafting Ideas with EGTRRA in Mind.

# **THE ESSENTIALS OF ETHICS FOR AN ESTATE & TRUST LAWYER**

**A “Laundry List” Of Issues & Potential Answers**

*Sheldon G. Gilman  
Lynch, Cox, Gilman & Mahan, P.S.C.  
Louisville, Kentucky*

Copyright 2002. Sheldon G. Gilman. All Rights Reserved.

## **SECTION D**



# THE ESSENTIALS OF ETHICS FOR AN ESTATE & TRUST LAWYER

## A "Laundry List" Of Issues & Potential Answers

<b>1.</b>	<b>Long Term Care Planning Problems</b>	<b>D-1</b>
1.1	Primary Sources of Long Term Care Options	D-1
1.2	Problems Of Long Term Care	D-1
1.3	Medicaid Estate Planning	D-2
1.4	Medicaid Planning is Complex	D-2
1.5	Health Insurance Portability and Accountability Act of 1996	D-2
1.6	Balanced Budget Act of 1997	D-2
1.7	<i>New York State Bar Ass'n v. Reno</i>	D-2
1.8	Competing Ethics' Requirements	D-3
1.9	Alternative Course of Actions	D-3
<b>2.</b>	<b>Asset Protection Planning &amp; Professional Responsibility</b>	<b>D-4</b>
2.1	Applicable Rules of Professional Conduct	D-4
2.2	Key Terms	D-7
2.3	Civil Liability	D-8
2.4	American Bar Association Ethics Opinion 92-366, August 8, 1992	D-8
2.5	Case Example	D-10
<b>3.</b>	<b>Confidentiality Issues</b>	<b>D-10</b>
3.1	Disclosure of Client's Confidences After Death	D-10
3.2	Disclosure of Client Assets - Florida Opinion 72-40, November 10, 1972	D-12
3.3	Withholding Evidence - Florida Opinion 65-54, August 27, 1965	D-12
<b>4.</b>	<b>Obligations to Surviving Spouse - Florida Bar Opinion 76-16</b>	<b>D-13</b>
4.1	Does the lawyer for the personal representative have the right to inform the surviving spouse of his or her entitlement to family allowance, exempt property, or right to claim an elective share?	D-13
4.2	Is the lawyer obligated to inform the surviving spouse of such rights?	D-14
4.3	Assuming that the personal representative is someone other than the surviving spouse, are the rights or obligations of the lawyer in 1 and 2, above, different if the personal representative objects to the lawyer's informing the surviving spouse of her entitlement?	D-14



4.4	Assuming that the personal representative is someone other than the surviving spouse, would the answer to 3, above, be different if the lawyer had represented the decedent and spouse for a number of years? .....	D-15
4.5	Assuming that the personal representative is someone other than the surviving spouse, would the answer to 3, above, be different if the personal representative's opposition to the spouse claiming an elective share or statutory entitlements is based upon the personal representative's desire to increase his own distributive share? .....	D-15
<b>5.</b>	<b>Representation of Spouses - Do You Understand the Risks? .....</b>	<b>D-15</b>
5.1	Identify the Client .....	D-15
5.2	Spouse Issues - Joint Representation Issues - Florida Opinion 95-4 May 30, 1997 .....	D-16
5.3	Gilman Suggested Spousal Representation Forms .....	D-19
<b>6.</b>	<b>Representation of Fiduciary Issues .....</b>	<b>D-22</b>
6.1	KBA-Opinion 404 .....	D-22
6.2	Suggested Letter to Fiduciary .....	D-26
6.3	Suggested Letter to Beneficiary .....	D-27
<b>7.</b>	<b>Fees; Referral Fees; Commissions &amp; Outside Sources of Income .....</b>	<b>D-28</b>
7.1	Client Files - KBA Ethics Opinion E-395, January 5, 1998 .....	D-28
7.2	Sale of Life Insurance - KBA E-376 .....	D-29
7.3	Lawyers Receiving Commissions - KBA E-390 .....	D-30
7.4	Donating Legal Services to Charity - KBA E-388 .....	D-32
7.5	Association with Financial Planner - Texas Opinion 446, May 1987 .....	D-32
7.6	Financial Services Firm Practicing Law - KBA U-50, June 17, 1997 .....	D-33
7.7	Fee Agreement Inserted in Will - Florida Bar Opinion 64-15, March 25, 1964 .....	D-34
7.8	Division of Fees - Florida Bar Opinion 90-8, March 1, 1991 .....	D-35
<b>8.</b>	<b>Client Disability .....</b>	<b>D-37</b>
8.1	Rule 1.14 - Client Under a Disability .....	D-37
8.2	Florida Opinion 85-4, 10/1/1985 - Reconsidered & Approved on 9/10/1998 .....	D-38
8.3	ABA Commission 2000 Report .....	D-38

## SECTION D

<b>9.</b>	<b>Estate Planning Opinions of Interest .....</b>	<b>D-38</b>
9.1	Retention of Client Wills - New York Opinion 724 -11/30/99 .....	D-39
9.2	Preparation of Questionable Document - Florida Opinion 76-35, October 17, 1977 .....	D-40
9.3	Conflict in Will Preparation. Texas Opinion 439, 1987 .....	D-41
9.4	Necessity of Personal Client Contact .....	D-42
9.5	Purchase of Property From an Estate. Opinion KBA E-217 .....	D-42

## SECTION D



***The Essentials of Ethics For An Estate & Trust Lawyer:***

***A "Laundry List" of Issues & Potential Answers<sup>1</sup>***

by  
**Sheldon G. Gilman**  
**Louisville, Kentucky**

---

**1. Long Term Care Planning Problems<sup>2</sup>**

**1.1 Primary Sources of Long Term Care Options.**

**1.1(a)** Medicare - Its limited coverage does not offer long term care for chronic illness and disability that many elderly Americans need. There are no income or asset requirements; all social security recipients may receive it.

**1.1(b)** Out of Pocket Payments - Nursing home care is expensive - anywhere from \$4,000 to \$8,000 a month, and costs for home health care could be \$80,000 a year, and supervision problems do exist.

**1.1(c)** Private LTC Insurance - Insurance that takes effect when the policyholder cannot perform two of the activities of daily living as outlined in the policy. LTC is expensive and may not be an option for those with a pre-existing medical condition.

**1.1(d)** Medicaid - is a welfare program that covers most medical costs, it does not impose strict time limits on treatment, etc. To qualify for Medicaid, individuals must meet both an income test and a resource test.

**1.2 Problems Of Long Term Care.** As the cost for care escalates the other spouse becomes concerned that the use of their accumulated estate should not be consumed for health care needs. Further, the children become concerned that they may be deprived of their "rightful" inheritance if the family's assets are consumed by the needs of their parents - and in most cases the children

---

<sup>1</sup> This Outline contains suggested engagement letters and other forms and all of the examples of suggested language are presented for discussion purposes only. The suggested forms are not gospel; nor does the author make any representations or warranties regarding their use.

<sup>2</sup> The primary source of materials for this portion are from two excellent law review articles; (i) Joire, After New York Sate Bar Ass'n v. Reno: Ethical Problems in Limiting Medicaid Estate Planning, 12 The Georgetown Journal of Legal Ethics #4 at 789 (1999); and (ii) Martin, Funding Long-Term Care: Some Risk-Spreaders Create More Risks Than They Cure, 16 J. Contemp. Health L. & Pol'y 355 (2000).

become most emblazoned by their demands that someone support their ill parent other than themselves out of the family estate.

### **1.3 Medicaid Estate Planning - Has been defined as:**

“The manipulation of Medicaid eligibility rules by non-poor elderly persons, their heirs, and *their attorneys* to obtain Medicaid coverage for nursing-home care while protecting significant amounts of wealth.”

**1.4 Medicaid Planning is Complex** - Estate planning usually occurs to qualify a family's parent for benefits by making certain asset transfers and certain trust transfers before applying for Medicaid benefits. The “look back periods” are 36 months for asset transfers and 60 months for trust transfers.

**1.4(a)** Common Medicaid planning techniques include conversion, pre-eligibility gift giving, use of annuities and other financial instruments.

**1.4(b)** Disadvantages of Medicaid Planning - include nursing home discrimination, loss of nursing home space during hospitalization, transfer to another bed in another wing when Medicare ceases to cover costs, etc.

**1.5 Health Insurance Portability and Accountability Act of 1996** - known as “*Granny Goes to Jail*” Act - imposes penalties of \$25,000 and five years imprisonment if a person makes asset transfers and makes an application for medicaid during the period of ineligibility.

**1.6 Balanced Budget Act of 1997** - repealed the “*Granny Goes to Jail*” Act and the new law is referred to as the “*Granny's Lawyer Goes to Jail*” Act.

**1.6(a)** The new law transfers liability to the individual's lawyer by making it a misdemeanor for anyone who: for a fee knowingly and willfully counsels or assists an individual to dispose of assets in order for the individual to become eligible for medical assistance under a State plan.

**1.6(b)** Individuals are not subject to any criminal penalties for restructuring their assets to qualify for Medicaid. However, attorneys found guilty of such counseling will be fined up to \$10,000, imprisoned for up to one year, or both.

***Restructuring your assets is legal, but a lawyer counseling a client on how to restructure their assets in order to qualify for benefits is illegal!***

**1.7 New York State Bar Ass'n v. Reno.**<sup>3</sup> In 1997 the New York Bar brought a constitutional

---

<sup>3</sup> 999 F. Supp. 710 (N.D.N.Y. 1998).

challenge to the law asserting that the law restricted attorneys' freedom of speech. In 1998, Janet Reno informed Congress that she would not defend the constitutionality of the law and would not enforce its criminal provisions. However, the court reasoned that despite the Attorney General's insistence that she will not enforce the law, *attorneys would be ethically bound to uphold it*. The court granted a permanent injunction, and attorneys in up-state New York are protected.

## **1.8 Competing Ethics' Requirements.**

### **1.8(a)** Rule 1.2. *Scope of Representation*, as follows.

(a) A lawyer shall abide by a client's decision concerning the objectives of representation, subject to paragraphs (c), (d) and (e), and shall consult with the client as to the means by which they are to be pursued. . . .

(b) . . . .

(c) A lawyer may limit the objectives of the representation if the client consents after consultation.

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

(e) When a lawyer knows that a client expects assistance not permitted by the Rules of Professional Conduct or other law, the lawyer shall inform the client regarding the relevant limitations on the lawyer's conduct.

### **1.8(b)** Rule 1.1. *Competence*, as follows.

A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

### **1.8(c)** Rule 1.3. *Diligence*, as follows.

A lawyer shall act with reasonable diligence and promptness in representing a client.

## **1.9 Alternative Course of Actions.**

**1.9(a)** Attempt to Limit Liability - Have your client agree not to incur a period of ineligibility as condition of representation. However, this course of action appears to be in violation of Rule 1.8(h), attorneys may not "make an agreement prospectively limiting the lawyer's liability for malpractice unless permitted by law and the client is independently represented in making the agreement."

**1.9(b)** Do *Not* Charge a Fee - If the lawyer performs the service for free there is no technical violation of the statute.

**1.9(c)** Ignore the Law - Contest the law - but what about the professional responsibility issues?

## **2. Asset Protection Planning & Professional Responsibility**

### **2.1 Applicable Rules of Professional Conduct.**

**2.1(a)** Rule 1.2(d), *Scope of Representation*, is as follows:

(d) A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.

**2.1(b)** Rule 1.6, *Confidentiality of Information*, as follows:

(a) A lawyer shall not reveal information relating to representation of a client unless the client consents after consultation, except for disclosures that are impliedly authorized in order to carry out the representation, and except as stated in paragraph (b).

(b) A lawyer may reveal such information to the extent the lawyer reasonably believes necessary:

(1) To prevent the client from committing a criminal act that the lawyer believes is likely to result in imminent death or substantial bodily harm; or

(2) To establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; or

(3) To comply with other law or a court order.

Comment: Disclosure Adverse to Client

[9] The confidentiality rule is subject to limited exceptions. In becoming privy to information about a client, a lawyer may foresee that the client intends serious harm to another person. However, to the extent a lawyer is required or permitted to disclose a client's purposes, the client will be inhibited from revealing facts which would enable the lawyer to counsel against a wrongful course of action. The public is better protected if full and open communication by the client is encouraged than if it is inhibited.

[10] Several situations must be distinguished.

[11] First, the lawyer may not counsel or assist a client in conduct that is criminal or fraudulent. See Rule 1.2(d). Similarly, a lawyer has a duty under Rule 3.3(a)(4) not to use false evidence. This duty is essentially a special instance of the duty prescribed in Rule 1.2(d) to avoid assisting a client in criminal or fraudulent conduct.

[12] Second, the lawyer may have been innocently involved in past conduct by the client that was criminal or fraudulent. In such a situation the lawyer has not violated Rule 1.2(d), because to “counsel or assist” criminal or fraudulent conduct requires knowing that the conduct is of that character.

[13] Third, the lawyer may learn that a client intends prospective conduct that is criminal and likely to result in imminent death or substantial bodily harm. As stated in paragraph (b)(1), the lawyer has professional discretion to reveal information in order to prevent such consequences. The lawyer may make a disclosure in order to prevent homicide or serious bodily injury which the lawyer reasonably believes is intended by a client. It is very difficult for a lawyer to “know” when such a heinous purpose will actually be carried out, for the client may have a change of mind.

[14] The lawyer’s exercise of discretion requires consideration of such factors as the nature of the lawyer’s relationship with the client and with those who might be injured by the client, the lawyer’s own involvement in the transaction and factors that may extenuate the conduct in question. Where practical, the lawyer should seek to persuade the client to take suitable action. In any case, a disclosure adverse to the client’s interest should be no greater than the lawyer reasonably believes is necessary to the purpose. A lawyer’s decision not to take preventive action permitted by paragraph (b)(1) does not violate this Rule.

Comment: Withdrawal

[15] If the lawyer’s services will be used by the client in materially furthering a course of criminal or fraudulent conduct, the lawyer must withdraw, as stated in Rule 1.16(a)(1).

[16] After withdrawal the lawyer is required to refrain from making disclosure of the clients’ confidences, except as otherwise provided in Rule 1.6. ***Neither this rule nor Rule 1.8(b) nor Rule 1.16(d) prevents the lawyer from giving notice of the fact of withdrawal, and upon withdrawal the lawyer may also withdraw or disaffirm any opinion, document, affirmation, or the like.*** (Emphasis added.)

**2.1(c)** Rule 1.16, *Declining or Terminating Representation*, as follows:

(a) Except as stated in paragraph (c), a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if:

- (1) The representation will result in violation of the Rules of Professional Conduct or other law;
- (2) The lawyer's physical or mental condition materially impairs the lawyer's ability to represent the client; or
- (3) The lawyer is discharged.

(b) Except as stated in paragraph (c), a lawyer may withdraw from representing a



client if withdrawal can be accomplished without material adverse effect on the interests of the client, or if:

- (1) The client persists in a course of action involving the lawyer's services that the lawyer reasonably believes is criminal or fraudulent;
  - (2) The client has used the lawyer's services to perpetrate a crime or fraud;
  - (3) The client insists upon pursuing an objective that the lawyer considers repugnant or imprudent;
  - (4) The client fails substantially to fulfill an obligation to the lawyer regarding the lawyer's services and has been given reasonable warning that the lawyer will withdraw unless the obligation is fulfilled;
  - (5) The representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client; or
  - (6) Other good cause for withdrawal exists.
- (c) When ordered to do so by a tribunal, a lawyer shall continue representation notwithstanding good cause for terminating the representation.
- (d) Upon termination of representation, a lawyer shall take steps to the extent reasonably practicable to protect a client's interests, such as giving reasonable notice to the client, allowing time for employment of other counsel, surrendering papers and property to which the client is entitled and refunding any advance payment of fee that has not been earned.

**2.1(d)** Rule 1.13, *Organization as Client*, as follows:

(a) A lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents.

(b) If a lawyer for an organization knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is a violation of a legal obligation to the organization, or a violation of law which reasonably might be imputed to the organization, and is likely to result in substantial injury to the organization, the lawyer shall proceed as is reasonably necessary in the best interest of the organization. In determining how to proceed, the lawyer shall give due consideration to the seriousness of the violation and its consequences, the scope and nature of the lawyer's representation, the responsibility in the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters and any other relevant considerations. Any measures taken shall be designed to minimize disruption of the organization and the risk of revealing information relating to the representation to persons outside the organization. Such measures may include among others:

- (1) Asking reconsideration of the matter;
- (2) Advising that a separate legal opinion on the matter be sought for presentation to appropriate authority in the organization; and
- (3) Referring the matter to higher authority in the organization, including, if warranted by the seriousness of the matter, referral to the highest authority that can act in behalf of the organization as determined by applicable law.

(c) If, despite the lawyer's efforts in accordance with paragraph (b), the highest authority that can act on behalf of the organization insists upon action, or a refusal to act, that is clearly a violation of law and is likely to result in substantial injury to the organization, the lawyer may resign in accordance with Rule 1.16.

(d) In dealing with an organization's directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when it is apparent that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing.

(e) A lawyer representing an organization may also represent any of its directors, officers, employees, members, shareholders or other constituents, subject to the provisions of Rule 1.7. If the organization's consent to the dual representation is required by Rule 1.7, the consent shall be given by an appropriate official of the organization other than the individual who is to be represented, or by the shareholders.

**2.1(e)** The provisions of Rule 4.1, *Truthfulness in Statements to Others*, are very helpful and should be understood, as follows.

**2.1(e)(1)** The provisions of the Kentucky Rule.

In the course of representing a client a lawyer shall not knowingly make a false statement of material fact or law to a third person.

**2.1(e)(2)** The provisions of the Comment.

#### Misrepresentation

[1] A lawyer is required to be truthful when dealing with others on a client's behalf, but generally has no affirmative duty to inform an opposing party of relevant facts. A misrepresentation can occur if the lawyer incorporates or affirms a statement of another person that the lawyer knows is false. Misrepresentations can also occur by failure to act.

#### Statements of Fact

[2] This Rule refers to statements of fact. Whether a particular statement should be regarded as one of fact can depend on the circumstances. Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact. Estimates of price or value placed on the subject of a transaction and a party's intentions as to an acceptable settlement of a claim are in this category, and so is the existence of an undisclosed principal except where nondisclosure of the principal would constitute fraud.

## 2.2 Key Terms.

**2.2(a)** “Belief” or “believes” denotes that the person involved actually supposed the fact in question to be true. A person’s belief may be inferred from circumstances.

**2.2(b)** “Fraud” or “fraudulent” denotes conduct having a purpose to deceive and not merely negligent misrepresentation or failure to apprise another of relevant information.

**2.2(c)** “Knowingly,” “known,” or “knows” denotes actual knowledge of the fact in question. A person’s knowledge may be inferred from circumstances.

### **2.3 Civil Liability.**

**2.3(a)** *McElhanon v. Hing*, 151 Ariz. 386, 728 P.2d 256 (Ct.App. 1985), affirmed in part and vacated in part in *McElhanon v. Hing*, 151 Ariz. 403, 728 P.2d 542 (Ct.App. 1986).

**2.3(a)(1)** Attorney Hing represented defendants Harris and Greer in a shareholder dispute. The day after the court entered judgment against Hing’s clients, Hing and his clients discussed transferring corporate interests among themselves. Hing then drafted an agreement resulting in the transfer of assets at less than fair value.

**2.3(a)(2)** Noting that Hing (1) participated in the discussion of the fraudulent transfer, (2) drafted the agreement carrying out the fraudulent transfer, (3) knew the transferor was or would be rendered insolvent by the transfer, (4) knew that the transferee who was to make payment for the transfer was either insolvent or financially unstable, and (5) knew that consideration was inadequate, the court found that attorney Hing had the actual intent to hinder, delay and defraud the judgment creditor. Judgment in the amount of \$286,000 was awarded against Hing.

**2.3(b)** *Pearce v. Stone*, 149 Ariz. 567, 720 P.2d 542 (Ct.App. 1986).

**2.3(b)(1)** Attorney Stone assisted his client to create a trust, transfer real property into the trust, and encumber the real property, all immediately after the client received demand letters threatening litigation.

**2.3(b)(2)** The Court of Appeals reversed summary judgment for the attorney, holding that there was sufficient evidence of the attorney’s conspiracy to commit a fraudulent conveyance to try the case. Further, the court held that the attorney - client privilege for communications between Stone and his client was defeated by the showing of a prima facie fraud on the part of the client. At issue in this case was a claim against Stone for over \$450,000.

### **2.4 American Bar Association Ethics Opinion 92-366, August 8, 1992.**

**2.4(a)** Facts: Lawyer learns that officers of corporate client have participated in a fraudulent scheme to alter corporate contracts to inflate corporate earnings. The lawyer had prepared a legal opinion for the corporation regarding the contracts and the lawyer's statements were relied upon by the bank which loaned money to the company. The corporate officers are not willing to prepare corrected financial statements, they have advised the lawyer that they intend to retain a new lawyer, and to try correct the situation by improving the company's future profits. The officers have asked the lawyer to remain as corporate counsel so that the lawyer may assist the company's survival efforts in ways that would not directly implicate the lawyer's legal opinion. The lawyer advised the Board of Directors and they decided to do nothing because they think the company's officers can work out the problem.

**2.4(b)** Query: What should a lawyer do when the lawyer learns that the lawyer's work product is used to perpetrate a fraud; is continuing to use it, or plans to use the work product in the future?

**2.4(c)** Opinion:

**2.4(c)(1)** First, the lawyer *must* withdraw from any representation of the client that, directly or indirectly, would have the effect of assisting the client's continuing or intended future fraud.

**2.4(c)(2)** Second, the lawyer *may* withdraw from all representation of the client, and *must* withdraw from all representation if the fact of such representation is likely to be known to and relied upon by third persons to whom the continuing fraud is directed, and the representation is therefore likely to assist in the fraud.

**2.4(c)(3)** Third, the lawyer may disavow any of her work product to prevent its use in the client's continuing or intended future fraud, even though this may have the collateral effect of disclosing inferentially client confidences obtained during the representation. In some circumstances, such a disavowal of work product (commonly referred to as a "noisy" withdrawal) may be necessary in order to effectuate the lawyer's withdrawal from representation of the client.

**2.4(c)(4)** Fourth, if the fraud is completed, and the lawyer does not know or reasonably believe that the client intends to continue the fraud or commit a future fraud by use of the lawyer's services or work product, the lawyer may withdraw from representation of the client but may not disavow any work product.

**2.4(d)** Dissent:

**2.4(d)(1)** The opinion . . . has imported the likelihood of the bank's knowledge of and reliance upon the fact of unrelated continuing representation; has assumed conclusively that such knowledge will "lull" the bank; and has assumed further that this

lulling effect of the bank's knowledge will result in the lawyer's unwitting assistance in the client's future fraud on the bank; and that "assistance" will violate Rule 1.2(d), triggering mandatory withdrawal under Rule 1.16(a)(1). Aside from the practical impossibility of the lawyer being able to know or rationally predict the likelihood of the bank's experiencing all these sensations, that simply is not the Model Rule.

**2.4(d)(2)** Having thus redefined the words of the Model Rules to support its goal of finding a way to disavow the old letter, the opinion is not reticent to permit what it hopes will be a loud and clear signal to others that the client is a defrauder - "information relating to the representation" and hence protected by Model Rule 1.6 (while, of course, maintaining that the lawyer is not really engaged in disclosure of client data, but only in frantic signaling and flag-waving). The fact that the "noisy withdrawal" option is a clear departure from the strictures of Model Rule 1.6, and yet is found only in the Comment to that Model Rule and not in its text, has been no deterrent here. Neither is the fact that, as Professor Geoffrey C. Hazard - . . . has conceded in his treatise, the option is:

buried disingenuously in the final version of the Official Comment, [and] has a potentially broad scope. Indeed, unless it is narrowed by interpretation in light of the general principle of Rule 1.6, it threatens to create an exception broader than any ever proposed by the Kutak Commission.

## **2.5 Case Example:**

**2.5(a)** Facts: A doctor has decided to "go bare" and forego malpractice insurance. He comes to you for advice on how to arrange his personal and business affairs to minimize the ability of claimants to collect against him on malpractice claims. He also wants to make appropriate provisions to protect his wife, and children. He tells you that there are no pending malpractice suits against him (although he has had a few in the past). He also tells you he is not aware of any pending or potential claims but acknowledges that there is a significant risk that a malpractice action may be brought in the future.

**2.5(b)** Questions:

**2.5(b)(1)** Can you ethically discuss with him or implement an offshore trust; a FLP; QTIP trust planning or other devices to protect his assets?

**2.5(b)(2)** What are your ethical and other potential exposures?

## **3. Confidentiality Issues**

### **3.1 Disclosure of Client's Confidences After Death.**

**3.1(a)** Rule 1.6, *Confidentiality of Information*, as follows:

(a) A lawyer shall not reveal information relating to representation of a client unless the client consents after consultation, except for disclosures that are impliedly authorized in order to carry out the representation, and except as stated in paragraph (b).

(b) A lawyer may reveal such information to the extent the lawyer reasonably believes necessary:

(1) To prevent the client from committing a criminal act that the lawyer believes is likely to result in imminent death or substantial bodily harm; or

(2) To establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; or

(3) To comply with other law or a court order.

**3.1(b)** The *ACTEC* Commentaries.<sup>4</sup>

In general, the lawyer's duty of confidentiality continues after the death of a client. Accordingly, a lawyer ordinarily should not disclose confidential information following a client's death. *However, if consent is given by the client's personal representative, or if the decedent had expressly or impliedly authorized disclosure, the lawyer who represented the deceased client may provide an interested party, including a potential litigant, with information regarding a deceased client's dispositive instruments and intent, including prior instruments and communications relevant thereto. A lawyer may be impliedly authorized to make appropriate disclosure of client confidential information that would promote the client's estate plan, forestall litigation, preserve assets, and further family understanding of the decedent's intention.* Disclosures should ordinarily be limited to information that the lawyer would be required to reveal as a witness. (At page 124 - 125.) [Emphasis added.]

**3.1(c)** *Swidler & Berlin v. U.S.*, 524 U.S. 399, 118 S. Ct. 2081, 141 L.Ed.2d 379 (1998). The United States Supreme Court opined that the general rule with respect to confidential communications is that such communications are privileged during a testator's lifetime and, also, after the testator's death unless sought to be disclosed in litigation between the testator's heirs. The Court also stated that the testamentary disclosure was permissible because the privilege, which normally protects the client's interest, could be impliedly waived in order to fulfill the client's testamentary intent.

**3.1(d)** *In re Estate of Hamilton v. Morris*, 67 S.W.3d 786 (2001). The Tennessee Court

---

<sup>4</sup> ACTEC (American College of Trust and Estate Counsel) Commentaries On The Model Rules of Professional Conduct, Third Edition (1999).

of Appeals held that confirmed the application of the *Swidler* case in a case pertaining to matters when it may further the client's intent.

### **3.2 Disclosure of Client Assets - Florida Opinion 72-40, November 10, 1972.**

**3.2(a) Facts:** Firm was retained by a client for estate planning services. During the representation the client disclosed that he owned a large amount of bearer bonds, registered jointly with his wife, and kept in a strongbox. The firm advised the client that the bonds would have to be included in his gross estate and reported on his death tax return. The client told the lawyers to forget about the bonds. The client's Will was prepared and sent to the bank who is to act as the sole executor of the client's estate. The bank may seek to retain the same law firm as attorney for the executor.

**3.2(b) Questions:** The bank has asked the firm for an inventory of the client's assets and the firm asks two questions:

**3.2(b)(1)** In response to the bank's present request, should the law firm disclose the client's ownership of the bonds?

**3.2(b)(2)** On the client's death should the disclosure be made to the bank as executor if the firm becomes attorney or should the firm decline to represent the bank as executor?

**3.2(b)(3)** Should a disclosure be made even if the law firm does not represent the bank as executor?

**3.2(c) Opinion:**

**3.2(c)(1)** Absent written consent from the client, the firm cannot answer the bank's request. The client's present ownership of the bonds involves neither fraud nor a crime and, accordingly, it is the firm's duty to preserve the client's confidences. Absent the client's consent, the firm should inform the bank that, on instructions from the client, it was not answering the request.

**3.2(c)(2)** If the client has not consented to a full disclosure prior to his death, the firm should not act as attorney for the client's executor and should not make any disclosure regarding the bonds to anyone unless ordered by a court of competent jurisdiction to do so. The duty to preserve a client's confidences survives his death and his executor could not be represented without violating such confidences. The facts, as stated in the inquiry, show no present intention of the client to defraud the government, hence, the normal rule regarding preservation of the client's confidences is applicable.

### **3.3 Withholding Evidence - Florida Opinion 65-54, August 27, 1965.**

**3.3(a) Facts:** The value of decedent's shares of a closely held corporation has become significant for estate tax purposes, and one of the controversial points is whether the value of the stock must be based upon the value of the corporation's underlying assets. In order to evaluate the importance of the controversy, the attorney caused an appraisal to be made of the corporation's underlying assets as of the date of the decedent's death. The IRS has requested that the lawyer make the appraisal available to the IRS, and the lawyer has declined to do so, on the belief that the appraisal is a privileged communication or the attorney's work product, or both. The appraisal was not procured for use in preparation of the estate tax return, and it is emphasized that the appraisal was not even of estate assets but of assets owned by a corporation, part of whose capital stock is an estate asset. The appraisal was procured to assist the attorney in advising his client on the significance of a known, existing controversy with the IRS over the proper method of valuing an estate asset.

**3.3(b) Opinion:** A lawyer does not act unethically when he refuses to divulge to a governmental administrative or investigatory agency information concerning a client's affairs, if the lawyer in good faith believes that he may have legal grounds for withholding the information under the concepts of attorney-client privileged communication or attorney's work product, or otherwise, and if he believes that such withholding is in the best interest of his client. A lawyer has a duty to withhold information concerning a client's affairs where he has legal grounds to do so and where disclosure would or may be detrimental to the client.

#### **4. Obligations to Surviving Spouse - Florida Bar Opinion 76-16**

**4.1 Does the lawyer for the personal representative have the right to inform the surviving spouse of his or her entitlement to family allowance, exempt property, or right to claim an elective share? YES.**

**4.1(a)** The purpose of the Florida Probate Code is to provide a procedure to pay a decedent's debts and taxes and transfer and distribute the remaining assets as efficiently and inexpensively as possible to those entitled to them under the will or by intestacy. It is normal in most instances that the persons entitled to those assets will look to the personal representative or the lawyer for the estate to find out what they may expect to receive from the estate.

**4.1(b)** We believe that the lawyer for the personal representative has the right to provide those persons with that information and to provide the surviving spouse with information about his or her rights under the Probate Code. This is to be distinguished from counseling or giving legal advice.

**4.1(c)** The surviving spouse frequently is the personal representative. In claiming an elective share, a family allowance or exempt property we believe the surviving spouse is exercising a right provided by statute and is not acting in conflict with his or her duties as personal representative of the estate. Section 733.504(9), dealing with causes of removal of a



personal representative because of a conflict of interest, specifically exempts as reasons for removal the surviving spouse's claiming an elective share or statutory entitlements. We believe that in most instances the lawyer for the personal representative prepares the papers by which the surviving spouse elects against the will or claims statutory entitlements. We see no ethical problem with this, provided there is no *legal* objection to claiming an elective share or entitlements.

**4.1(d)** *If the surviving spouse claims one or more of the rights provided by statute, the result may be less for other beneficiaries. But the fact that claiming an elective share or statutory entitlements may alter the manner in which the estate is distributed does not, in the Committee's opinion, create a conflict of interest that requires the personal representative or his lawyer to refuse to provide any information about the existence of those rights and, in effect, to treat the surviving spouse as an adverse party.*

**4.1(e)** Such a result could force the surviving spouse to seek independent legal advice. We do not believe that the Probate Code intended to create a proliferation of lawyers; its purpose was just the opposite.

**4.1(f)** The Committee recognizes that there may be situations where it is apparent from the outset that there will be a dispute between a personal representative and a surviving spouse - a will contest, for example. In such situations, the lawyer for the personal representative should advise the surviving spouse that an actual or potential conflict of interest exists and suggest that he or she obtain independent legal advice.

**4.1(g)** Even where there is an actual or potential conflict of interest between personal representative and surviving spouse, we do not think the lawyer for the personal representative should refuse to furnish information about the surviving spouse's legal rights under the Florida Probate Code.

#### **4.2 Is the lawyer obligated to inform the surviving spouse of such rights?**

**4.2(a)** The lawyer is not necessarily required to inform the surviving spouse of such rights, but the Committee believes that it would be advisable to do so in most instances.

**4.2(b)** When the personal representative is someone other than the surviving spouse, the surviving spouse may be looking to the lawyer for the personal representative for information even though there is no attorney-client relationship between them. If the lawyer knows this, we believe he may have a duty to inform the surviving spouse of these statutory rights. If the surviving spouse has retained a lawyer, there is probably no need to. When the surviving spouse is the personal representative, we believe the lawyer should advise the surviving spouse of these rights.

#### **4.3 Assuming that the personal representative is someone other than the surviving spouse,**

**are the rights or obligations of the lawyer in 1 and 2, above, different if the personal representative objects to the lawyer's informing the surviving spouse of her entitlement? NO.**

**4.3(a)** *The right to claim an elective share, or family allowance or exempt property are, as stated above, rights provided by statute.*

**4.3(b)** *The personal representative has the duty to administer the estate according to law. He has no duty to try to prevent the exercise of those rights.*

**4.4 Assuming that the personal representative is someone other than the surviving spouse, would the answer to 3, above, be different if the lawyer had represented the decedent and spouse for a number of years? NO.**

**4.4(a)** The fact that the lawyer previously represented the decedent and spouse does not automatically create a duty to inform the surviving spouse of his or her statutory rights.

**4.4(b)** But, as stated in part of our answer to 2, above, the lawyer for the personal representative may have a duty, as distinguished from a right, to inform a surviving spouse of certain statutory rights if the lawyer has represented the decedent and spouse previously and knows the surviving spouse is looking to him for information.

**4.5 Assuming that the personal representative is someone other than the surviving spouse, would the answer to 3, above, be different if the personal representative's opposition to the spouse claiming an elective share or statutory entitlements is based upon the personal representative's desire to increase his own distributive share? NO.**

*A personal representative is a fiduciary, and his private desires vis-a-vis the estate are immaterial.*

## **5. Representation of Spouses - Do You Understand the Risks?**

### **5.1 Identify the Client.**

**5.1(a)** Do you represent the Husband, the Wife, or both? If you have always represented the husband and his employer, will you do the wife's estate planning?

**5.1(b)** In second marriages what will you do regarding the following:

**5.1(b)(1)** Will you recommend gift splitting?

**5.1(b)(2)** If one spouse's estate is "small," will you recommend use of such spouse's equivalent exemption amount created by applicable credit?

**5.1(b)(3)** How will you handle husband and wife's qualified retirement benefits?

**5.1(b)(4)** How do you handle children from prior marriage?

**5.1(b)(5)** How do you explain and then handle spouse's marital rights and actions to avoid taking against the Will? Post-marital agreements?

**5.1(c)** What do you do about confidential communications? Will you report it to both spouses or will you keep such communications confidential?

**5.2 Spouse Issues - Joint Representation Issues - Florida Opinion 95-4 May 30, 1997.**

**5.2(a)** Facts:

**5.2(a)(1)** Lawyer has represented Husband and Wife for many years in a range of personal matters, including estate planning. Husband and Wife have substantial individual assets, and they also own substantial jointly-held property. Recently, Lawyer prepared new updated wills that Husband and Wife signed. Like their previous wills, the new wills primarily benefit the survivor of them for his or her life, with beneficial disposition at the death of the survivor being made equally to their children (none of whom were born by prior marriage). Husband, Wife, and Lawyer have always shared all relevant asset and financial information. Consistent with previous practice, Lawyer met with Husband and Wife together to confer regarding the changes to be made in updating their wills. At no point since Lawyer first started to represent them did either Husband or Wife ever ask Lawyer to keep any information secret from the other, and there was never any discussion about what Lawyer might do if either of them were to ask Lawyer to maintain such a separate confidence.

**5.2(a)(2)** Several months after the execution of the new wills, Husband confers separately with Lawyer. Husband reveals to Lawyer that he has just executed a codicil (prepared by another law firm) that makes substantial beneficial disposition to a woman with whom Husband has been having an extra-marital relationship. Husband tells Lawyer that Wife knows about neither the relationship nor the new codicil, as to which Husband asks Lawyer to advise him regarding Wife's rights of election in the event she were to survive Husband.

**5.2(a)(3)** Lawyer tells Husband that Lawyer cannot under the circumstances advise him regarding same. Lawyer tells Husband that Lawyer will have to consider Lawyer's ethical duties under the circumstances. Lawyer tells Husband that, after consideration, Lawyer may determine to withdraw from representing Husband and Wife. Lawyer further tells Husband that, after consideration, Lawyer may determine to disclose to Wife the substance of Husband's revelation if Husband does not do so himself.

**5.2(b) Questions Presented.**

**5.2(b)(1)** Prior to Husband's recent disclosure, did Lawyer owe any ethical duty to counsel Husband and Wife concerning any separate confidence which either Husband or Wife might wish for Lawyer to withhold from the other?

**5.2(b)(2)** Assuming that Husband does not make disclosure of the information to Wife:

**5.2(b)(2)(A)** Is Lawyer required to reveal voluntarily the information to Wife?

**5.2(b)(2)(B)** May Lawyer in Lawyer's discretion determine whether or not to reveal the information to the Wife? If so, what are the relevant factors which Lawyer may or should consider?

**5.2(b)(2)(C)** If Lawyer does not reveal the information to Wife, is Lawyer required to withdraw from the representation? If so, what explanation, if any, should Lawyer give to Wife?

**5.2(b)(3)** May Lawyer continue to represent Husband alone if Lawyer notifies Wife that Lawyer is withdrawing from the joint representation and will no longer represent Wife? If so, is disclosure to Wife necessary in order to obtain her informed consent to Lawyer's continued representation of Husband?

**5.2(b)(4)** Assuming that adequate disclosure is made to Wife, may Lawyer continue to represent both Husband and Wife if they both wish for Lawyer to do so?

**5.2(c)** Opinion: The Lawyer's representation of Husband and Wife is a "joint representation."

**5.2(c)(1)** From the inception of the representation until Husband's communication to Lawyer of the information concerning the codicil and the extra-marital relationship (hereinafter the "separate confidence"), there was no objective indication that the interests of Husband and Wife diverged, nor did it objectively appear to Lawyer that any such divergence of interests was reasonably likely to arise. Such situations involving joint representation of Husband and Wife do not present a conflict of interests and, therefore, do not trigger the conflict of interest disclosure-and-consent requirements of Rules 1.7(a) and 1.7(b).

**5.2(c)(2)** Lawyer is not ethically obligated to discuss with Husband and Wife Lawyer's obligations with regard to separate confidences. While such a discussion is not

ethically required, in some situations it may help prevent the type of occurrence that is the subject of this opinion.

**5.2(c)(3)** We now turn to the central issue presented, which is the application of the confidentiality rule in a situation where confidentiality was not discussed at the outset of the joint representation. A lawyer is ethically obligated to maintain in confidence all information relating to the representation of a client. A lawyer, however, also has a duty to communicate to a client information that is relevant to the representation. These duties of communication and confidentiality harmoniously coexist in most situations. In the situation presented, however, Lawyer's duty of communication to Wife appears to conflict with Lawyer's duty of confidentiality to Husband. Thus, the key question for our decision is: Which duty must give way? We conclude that, under the facts presented, Lawyer's duty of confidentiality must take precedence. Consequently, if Husband fails to disclose (or give Lawyer permission to disclose) the subject information to Wife, Lawyer is not ethically required to disclose the information to Wife and does not have discretion to reveal the information. To the contrary, Lawyer's ethical obligation of confidentiality to Husband *prohibits* Lawyer from disclosing the information to Wife.

**5.2(c)(4)** It has been suggested that, in a joint representation, a lawyer who receives information from the "communicating client" that is relevant to the interests of the non-communicating client may disclose the information to the latter, even over the communicating client's objections and even where disclosure would be damaging to the communicating client. The committee is of the opinion that disclosure is not permissible and therefore rejects this "no-confidentiality" position. The argument for a "no-confidentiality" approach -- which is a departure from the usual rule of lawyer-client confidentiality -- is premised on two bases: (1) that joint clients have an expectation that everything relating to the joint representation that is communicated by one client to the joint lawyer will be shared by the lawyer with the other client (i.e., that joint clients have no expectation of confidentiality within the joint representation); and (2) that the law governing the evidentiary attorney-client privilege sets (or should set) the standard for the lawyer's ethical duties in the joint representation setting. Both of these foundations, in the committee's opinion, are flawed.

**5.2(c)(5)** It is important to note that the ethical duty of confidentiality is broader than the evidentiary attorney-client privilege. This distinction holds true even in a joint client setting. The ethical duty of confidentiality assures a client that, throughout the course of the representation and beyond, the lawyer ordinarily may not voluntarily reveal information relating to the representation to anyone else without the client's consent. In contrast, the evidentiary privilege becomes relevant only after legal proceedings have begun. The privilege is a limited exception to the general principle that, in formal legal proceedings, the legal system and society should have all relevant information available as part of the search for truth. Thus, there are different purposes underlying the concepts of confidentiality and privilege. The committee is of the opinion that the law of privilege

does not, and should not, set the ethical standard of lawyer-client confidentiality.

**5.2(c)(6)** It has been argued in some commentaries that the usual rule of lawyer - client confidentiality does not apply in a joint representation and that the lawyer should have the *discretion* to determine whether the lawyer should disclose the separate confidence to the non-communicating client. This result is favored by the American College of Trusts and Estates in its *Commentaries on the Model Rules of Professional Conduct* (2d ed. 1995) (hereinafter the "ACTEC Commentaries"). The *ACTEC Commentaries* do not cite any supporting authority for this proposition. The committee rejects the concept of discretion in this important area. Florida lawyers must have an unambiguous rule governing their conduct in situations of this nature. *We conclude that Lawyer owes duties of confidentiality to both Husband and Wife, regardless of whether they are being represented jointly. Accordingly, under the facts presented Lawyer is ethically precluded from disclosing the separate confidence to Wife without Husband's consent.*

**5.2(c)(7)** The committee further concludes that Lawyer must withdraw from the joint representation under the facts presented. An adversity of interests concerning the joint representation has arisen. This creates a conflict of interest. Many conflicts can be cured by obtaining the fully informed consent of the affected clients. Some conflicts, however, are of such a nature that it is not reasonable for a lawyer to request consent to continue the representation. In the situation presented, the conflict that has arisen is of an personal and, quite likely, emotionally-charged nature. Lawyer's continued representation of both Husband and Wife in estate planning matters presumably would no longer be tenable. Rule 1.16 thus requires Lawyer's withdrawal from representation of both Husband and Wife in this matter. In withdrawing from the representation, Lawyer should inform Wife and Husband that a conflict of interest has arisen that precludes Lawyer's continued representation of Wife and Husband in these matters. Lawyer may also advise both Wife and Husband that each should retain separate counsel. As discussed above, however, Lawyer may not disclose the separate confidence to Wife. The committee recognizes that a sudden withdrawal by Lawyer almost certainly will raise suspicions on the part of Wife. This may even alert Wife to the substance of the separate confidence. Regardless of whether such surmising by Wife occurs when Lawyer gives notice of withdrawal, Lawyer nevertheless has complied with the Rules of Professional Conduct and has not violated Lawyer's duties to Husband.

### **5.3 Gilman Suggested Spousal Representation Forms.<sup>5</sup>**

#### **5.3(a) Letter:**

---

<sup>5</sup> These materials presented here is for discussion purposes only and should not be used without serious consideration of all the issues.

Dear Bill and Hillary:

It was a pleasure for me to meet with Bill to discuss your estate planning matters. I have enclosed a copy of my notes from our meeting and I would appreciate your review of my meeting notes. Please let me know if you have any questions or comments.

As this is our firm's initial representation of your interests it is necessary that I advise you that the Kentucky Rules of Professional Conduct, the lawyer ethics' rules, require that I provide you with a written explanation of my professional responsibilities to you with regards to your estate planning matters, and an explanation of my law firm's fee policies. In order to avoid the possibility of a misunderstanding, and in order for me to be in compliance with the Kentucky Rules of Professional Conduct, please accept this correspondence as an explanation of these matters.

*Alternative #1*

I understand I will represent both of you; that is, Bill and Hillary, and during the course of the estate planning process it is possible, although most unlikely, that legal conflicts of interest may arise between the two of you. Conflicts of interest might arise because of your desired disposition of your separate property, your joint tenancy (with right of survivorship) property, marital property, disposition of qualified retirement benefits, and your marital rights under Kentucky's laws of descent and distribution, etc. If there are differences of opinion on the disposition of such property then the lawyer Rules of Ethics might not permit me to continue to represent both of you. If there are differences of opinion then it would be better for each of you to have separate, independent counsel in order to avoid the possibility that my advice to one of you may be influenced by my representation of the other. If conflicts arise between the two of you that make it impossible, in my judgement, for me to continue to perform my obligations to each of you, then I will withdraw from all further dual representation and advise one or both of you to obtain independent counsel.

As I will be serving as the lawyer for each of you, anything that either one of you tell me will *not* be disclosed by me to the other without your permission. If I conclude that such confidential information is or may be detrimental to the interests of the other then I will maintain such information as confidential and not disclose it to anyone; however, it is most probable that I will resign from the mutual representation. While these types of conflict issues are most unlikely to arise, I am required to inform you of these matters and make sure you understand your legal rights. Further, if during the preparation of this current edition of your estate planning documents or after the completion of this current edition, either one of you advise me of facts that make a continued joint representation impossible or very uncomfortable, I will then withdraw from the joint representation.

*Alternative #2*

As I have represented Bill, and his company, the United States, Inc., for many years, I will continue to do so; however, at your joint request I will also prepare estate

planning documents for both of you. At this time I do not perceive any conflict of interest that might possibly arise because of your individual desires for the disposition of your separate property, your joint tenancy (with right of survivorship) property, marital property, disposition of qualified retirement benefits, and your marital rights under Kentucky's laws of descent and distribution, etc. If there are differences of opinion on the disposition of such property then the lawyer Rules of Ethics require that I advise Hillary to employ separate counsel to do her estate planning as I will continue to represent Bill and his company. We discussed these issues during our office conference and both of you felt comfortable with our discussion on the matter. If either of you have a change of mind or if I sense a conflict then we will proceed to disengage and Hillary will employ separate counsel.

I must presume that both of you will not disclose to me any information that you will not want disclosed to the other; hence, if either one of you disclose any information to me I *will* disclose it to the other. Further, if I conclude that any such information is or may be detrimental to the interests of the other I will report such information to both of you and then I will terminate my assistance to Hillary and advise her to seek separate counsel. Further, if during the preparation of this current edition of your estate planning documents or after the completion of this current edition, either one of you advise me of facts that make the preparation of your estate planning documents uncomfortable, I will advise Hillary to obtain separate counsel.

#### *Continuation of Letter*

After we complete the estate planning process, and your estate planning documents are signed, it is appropriate that you review these matters in the future to determine if the decisions you are making today remain appropriate in light of future developments. Please understand it is not possible for me to undertake to keep you advised of future changes in the law. *The rest of the letter presents a fee discussion.*

#### **5.3(b) Client Memorandum:**

When our law firm represents a husband and wife we are required to advise them that during the course of the estate planning process, it is possible, although unlikely, that legal conflicts of interest may arise. Conflicts of interest might arise because of each spouse's desired disposition of their separate property, property owned as joint tenants with right of survivorship, marital property, disposition of qualified retirement benefits, and how your marital rights are affected by Kentucky's laws of descent and distribution, etc.

If there are differences of opinion, the lawyer Rules of Ethics would not permit us to continue to represent both the husband and the wife. If there are differences of opinion, each spouse should have their own lawyer in order to avoid the possibility that our advice to the wife or the husband may be influenced by our representation of the other. If conflicts arise between the two of you that make it impossible, in our judgment, for us to continue to perform our obligations to each of you, then we will withdraw from all further dual representation and advise each of you to have your own lawyer.

As a matter of law, married persons have the legal right to a designated percentage of their spouse's estate; a wife's rights in her husband's property is called "dower," and a



husband's rights in his wife's property is called "curtesy." For example, a wife (or husband) may elect to take her (his) statutory share of the deceased spouse's estate, notwithstanding the written terms of the Will. These marital rights may be limited or terminated by entering into an agreement to ensure that the deceased spouse's Will or Trust does not become irrelevant. If you would like to learn more about these important legal rights please ask. The important point is to recognize that unless you take action to limit your spouse's rights, then your surviving spouse may effectively destroy your estate plan. Oral agreements to limit a spouse's rights are not enforceable.

When we serve as your lawyer, anything either one of you tell us will *not* be disclosed by us to the other without your permission. If we conclude that such confidential information is or may be detrimental to the interests of the other, then we will maintain such information as confidential and not disclose it to anyone; however, it is most probable that we would resign from the mutual representation. While it is most unlikely that conflict issues will arise, we are required to inform you of these matters.

After we complete the estate planning process, you should continue to review all of these matters to determine if the decisions you are making today remain appropriate in light of future developments; such as increases or decreases in the size of your estate, marital rights, changes in the law and the needs of your family. We are not able to undertake a responsibility to keep you advised of future changes in the law, but we would be pleased to work with you to consider any changes or the status of your matters when called upon by you to do so.

## **6. Representation of Fiduciary Issues**

### **6.1 KBA - Opinion 404.**

The Committee has been asked to address the applicability of the Kentucky Rules of Professional Conduct with respect to a lawyer's representation of the fiduciary of a decedent's estate or trust, and the lawyer's responsibilities to the beneficiaries of estates and trusts. In order to provide the requested advice, explain the Committee's position on these issues, and to give insight into the applicable Rules of Professional Conduct, the following questions are presented for response and discussion.

Question 1: Does a lawyer's representation of a fiduciary of a decedent's estate or trust expand or limit the lawyer's obligation to the fiduciary under the Rules of Professional Conduct?

Answer: No.

Question 2: Does a lawyer's representation of a fiduciary of a decedent's trust or estate impose on the lawyer obligations to the beneficiaries of the decedent's trust or estate that the lawyer would not have toward third parties?

Answer: No.

Question 3: Is the lawyer's obligation to preserve client confidences under Rule 1.6 altered by the fact that the client is a fiduciary?

Answer: No.

Question 4: May the lawyer for the fiduciary also represent the beneficiaries of the decedent's trust or estate?

Answer: Qualified Yes.

References: ABA Formal Op. 94-380 (1994); *Privilege and Confidentiality Issues When a Lawyer Represents a Fiduciary*, 30 Real Property, Probate and Trust Journal 541 (1996); *ACTEC Commentaries on the Model Rules of Professional Conduct*, 28 Real Property, Probate and Trust Journal 865 (1994); *Developments Regarding the Professional Responsibility of the Estate Administration Lawyer: The Effect of the Model Rules of Professional Conduct*, 26 Real Property, Probate and Trust Journal 1 (1991); *When Loyalties Collide: Courts Resolve Conflicting Duties*, 135 Trusts & Estates 22 (1996); *Professional Responsibility Issues Keep Practitioners on Their Toes*, 135 Trusts & Estates 22 (1996); and *The Fiduciary, His Counsel And The Attorney - Client Privilege*, 136 Trusts & Estates 29 (1997); §§73, *Duty to Certain Non-Clients*, Restatement, The Law Governing Lawyers.

### OPINION

From time to time Kentucky lawyers have requested advice from the Committee regarding a lawyer's responsibilities in the context of the administration of trusts and estates. The primary problem in answering such questions arises from the fundamental question: Whom does the lawyer represent? Does the lawyer represent the beneficiaries of the estate or trust; does the lawyer represent the estate or trust entity or does the lawyer represent the fiduciary? The complexity of this problem is acknowledged in Comment 12 to Rule 1.7, which states:

Conflict questions may also arise in estate planning and estate administration. A lawyer may be called upon to prepare wills for several family members, such as husband and wife, and, depending upon the circumstances, a conflict of interest may arise. In estate administration the identity of the client may be unclear under the law of a particular jurisdiction. Under one view, the client is the fiduciary; under another view the client is the estate or trust, including its beneficiaries. The lawyer should make clear the relationship to the parties involved.

By issuing this Opinion it is the Committee's intent to clarify a Kentucky lawyer's obligations under the Rules of Professional Conduct.

The examination of these issues must focus on Rule 1.7, Conflict of Interest: General Rule, and the problems generated by a lawyer's multiple representation of clients. The American College of Trust and Estate Counsel, hereafter referred to as "ACTEC," adopted Commentaries to the Model Rules of Professional Conduct in October 1993, and their Commentaries and the Reporter's Notes on the ACTEC Commentaries are helpful to this analysis. The Reporter's Notes contained the following statements:

Lawyer for Fiduciary. Under the majority view, a lawyer who represents a fiduciary ... stands in a lawyer-client relationship with the fiduciary and not with respect to the fiduciary estate or the beneficiaries. ...

**Duties to Beneficiaries.** The lawyer who represents a fiduciary generally is not usually considered also to represent the beneficiaries. However, most courts have concluded that the lawyer owes some duties to them. Some courts subject the lawyer to the duties because the beneficiaries are characterized as the lawyer's "joint," "derivative" or "secondary" clients. Other courts do so because the lawyer stands in a fiduciary relationship with respect to the fiduciary, who, in turn, owes fiduciary duties to the beneficiaries. The duties, commonly called "fiduciary duties," arise largely because of the nature of the representation and the relative positions of the lawyer, fiduciary, and beneficiaries. However, note that the existence and nature of the duties may be affected by the nature and extent of the representation that a lawyer provides to a fiduciary. Thus, a lawyer who represents a fiduciary individually regarding a fiduciary estate may owe few, if any, duties to the beneficiaries apart from the duties that the lawyer owes to other nonclients.

In addition to the Reporter's Notes, this Committee finds the following comments from the ACTEC Commentaries on Model Rule 1.7 instructive for purposes of clarifying the lawyer's obligations to the fiduciary, to the beneficiaries of an estate or trust, and the problems of multiple representation.

**General Nonadversary Character of Estates and Trusts Practice: Representation of Multiple Clients.** It is often appropriate for a lawyer to represent more than one member of the same family in connection with their estate plans, more than one beneficiary with common interests in an estate or trust administration matter.... In some instances the clients may actually be better served by such a representation, which can result in more economical and better coordinated estate plans prepared by counsel who has a better overall understanding of all of the relevant family and property considerations. ... Multiple representation is also generally appropriate because the interests of the clients in cooperation, including obtaining cost effective representation and achieving common objectives, often clearly predominate over their limited inconsistent interests. ...

**Disclosures to Multiple Clients.** Before, or within a reasonable time after, commencing the representation, a lawyer who is consulted by multiple parties with related interests should discuss with them the implications of a joint representation (or a separate representation if the lawyer believes that mode of representation to be more appropriate and separate representation is permissible under the applicable local rules). In particular, the prospective clients and the lawyer should discuss the extent to which material information imparted by either client would be shared with the other and the possibility that the lawyer would be required to withdraw if a conflict in their interests developed to the degree that the lawyer could not effectively represent both of them. The information may be best understood by the clients if it is discussed with them in person and also provided to them in written form, as in an engagement letter or brochure.

This Committee adopts the ACTEC Commentaries because the Commentaries properly set forth a lawyer's ethical obligations. Further, this Committee agrees with ABA Formal Opinion 94-380, and adopts the majority view; that is, that a lawyer who represents a fiduciary does not also represent the beneficiaries. We reject the view that a lawyer who represents a fiduciary also owes fiduciary obligations to the beneficiaries that in some circumstances will

override obligations otherwise owed by the lawyer to the fiduciary, such as the obligation of confidentiality. We also reject the view that when a lawyer represents a fiduciary in a trust or estate matter, the client is not the fiduciary, but is the trust estate. We adopt the following comments made in the ABA's Formal Opinion:

When the fiduciary is the lawyer's client all of the Model Rules prescribing a lawyer's duties to a client apply. The scope of the lawyer's representation is defined by and limited by Model Rule 1.2. The lawyer must diligently represent the fiduciary, *see* Model Rule 1.3, preserve in confidence communications between the lawyer and the fiduciary, *see* Model Rule 4.1(a). The fact that the fiduciary client has obligations toward the beneficiaries does not impose parallel obligations on the lawyer, or otherwise expand or supersede the lawyer's responsibilities under the Model Rules of Professional Conduct.

A lawyer's duty of confidentiality to a client is not lessened by the fact that the client is a fiduciary. Although the Model Rules prohibit the lawyer from actively participating in criminal or fraudulent activity or active concealment of a client's wrongdoing, they do not authorize the lawyer to breach confidences to prevent such wrongdoing.

The ABA's Opinion, in Footnote 6, included the following important caveats:

6. The Model Rules impose a number of limitations on a lawyer representing a fiduciary. For example, a lawyer may not participate in a breach of fiduciary duty by the fiduciary that involves fraud or criminal activity because the lawyer's conduct is limited by Model Rule 1.2(d), which provides that a lawyer may not actively participate in a client's criminal or fraudulent activity. This rule applies to all lawyers, not just those representing fiduciaries. Lawyers are also prohibited from actively concealing client breaches of fiduciary duty, or actively assisting in such concealment, by Model Rules 4.1(a) (a lawyer shall not lie to third parties) and 3.3(a)(1) and (2) (a lawyer shall not lie to or conceal information from a tribunal). If a lawyer knows that a breach of fiduciary duty has occurred, and that an accounting is misleading in that it hides wrongdoing committed by the fiduciary, the lawyer is expressly prohibited by Model Rule 3.3(a) from presenting the accounting to the court. Further, the lawyer is prohibited by Model Rule 4.1(a) from representing to the beneficiaries that a false accounting is accurate. These rules apply to a lawyer with a fiduciary client to the same extent as, but no farther than, they apply in any other lawyer/tribunal/third party scenario.

Continuing in the text of the Opinion, the ABA Ethics Committee then made the following comments:

Although a lawyer may not disclose confidences of the fiduciary, if the fiduciary insists on continuing a course of fraudulent or criminal conduct, the lawyer may be required to terminate the representation because the lawyer's services will be involved in that conduct, so as to invoke Rule 1.16(a)(1), or may have the option of a voluntary withdrawal under Rule 1.16(b)(1). If either of these provisions of Rule 1.16 applies, this will be not because the client is a fiduciary, but because the client is acting in the manner described by the Rule. The client's status is irrelevant.

Based upon the instructive comments of the ACTEC Commentaries and the ABA Formal Opinion, this Committee concludes with the following advice for Kentucky lawyers.

1. In representing a fiduciary the lawyer's client relationship is with the fiduciary and not with the trust or estate, nor with the beneficiaries of a trust or estate.

2. The fact that a fiduciary has obligations to the beneficiaries of the trust or estate does not in itself either expand or limit the lawyer's obligations to the fiduciary under the Rules of Professional Conduct, nor impose on the lawyer obligations toward the beneficiaries that the lawyer would not have toward other third parties.

3. The lawyer's obligation to preserve client's confidences under Rule 1.6 is not altered by the circumstance that the client is a fiduciary.

4. A lawyer has a duty to advise multiple parties who are involved with a decedent's estate or trust regarding the identity of the lawyer's client, and the lawyer's obligations to that client. A lawyer should not imply that the lawyer represents the estate or trust or the beneficiaries of the estate or trust because of the probability of confusion. Further, in order to avoid such confusion, a lawyer should not use the term "lawyer for the estate" or the term "lawyer for the trust" on documents or correspondence or in other dealings with the fiduciary or the beneficiaries.

5. A lawyer may represent the fiduciary of a decedent's estate or a trust and the beneficiaries of an estate or trust if the lawyer obtains the consent of the multiple clients, and explains the limitations on the lawyer's actions in the event a conflict arises, and the consequences to the clients if a conflict occurs. Further, a lawyer may obtain the consent of multiple clients only after appropriate *consultation* with the multiple clients at the time of the commencement of the representation.

## **6.2 Suggested Letter to Fiduciary.**

The Kentucky Rules of Professional Conduct require that I confirm with you the terms of our firm's employment to represent you in your fiduciary capacity, as a personal representative of Mr. Lincoln's Estate. Our representation will be limited to the representation of your interests and we will not represent any of the beneficiaries of Mr. Lincoln's estate or trust. While you have a fiduciary duty to the beneficiaries of the estate and the trust, our firm's responsibility is limited to representing your interests. We will assist you in the fulfillment of your duties and obligations as fiduciary, and we will advise you with regards to the rights and property interests of the beneficiaries.

From time to time I will advise you about your duties to the beneficiaries; however, that does not make me or my law firm their lawyer or give them any contractual rights with me. If you think it is appropriate we could advise the beneficiaries to retain their own counsel about their own interests.

While we do not anticipate any problems with regard to the beneficiaries, and we expect everyone's full cooperation and assistance, it is necessary that I explain the rules of

confidentiality to you. With regard to matters relating to the welfare of the beneficiaries, in the absence of disputes with them, our communications on matters of their interests are not privileged from them -- they are entitled to know what you and I have said or written to each other about their affairs. With respect to these matters it is not possible for us to keep these matters secret. With regard to matters that the beneficiaries may engage in a dispute with you which attacks you personally because of your work as a fiduciary, our efforts will be in helping you defend any attack. With respect to these matters it is our opinion that the beneficiaries do not have any right to our communications; this information is privileged and is protected.<sup>6</sup>

If there is ever a question whether information shared between us is confidential; that is, where we claim such information is confidential and the beneficiaries claim it is not, then a court will have to decide such questions. Finally, this firm's work product in preparing ourselves to assist you in dealing with the Estate, the Trust and the beneficiaries is privileged and no person is entitled to this information and preparation material.

### 6.3 Suggested Letter to Beneficiary.

The Kentucky Rules of Professional Conduct, which contain the lawyer rules of ethics, recommend that an attorney give his client and the beneficiaries of an estate a written explanation of the nature of the lawyer's responsibilities to the fiduciary of an estate, and to the beneficiaries of an estate. In order for our firm to avoid the possibility of misunderstandings we have prepared this letter to advise you as a beneficiary of \_\_\_\_\_ (describe relationship) estate.

We have been employed by \_\_\_\_\_ (name of fiduciary) and we will serve as \_\_\_\_\_'s (name of fiduciary) lawyer. \_\_\_\_\_ is a fiduciary and \_\_\_\_ (he, she, it) has duties to you as a beneficiary. We serve to advise \_\_\_\_\_, and to assist (him, her, it) in performing their required fiduciary duties in the administration of the estate, and to assist \_\_\_\_\_ (name of fiduciary) in their duties to you.

In accordance with the lawyer ethics' rules we are required to advise you that we are *not* your lawyer nor are we the lawyer for the "Estate." We will advise \_\_\_\_\_ (name of fiduciary) about (his, her, its) duties to you as a beneficiary of the Estate. Our firm's work product in preparing ourselves to assist \_\_\_\_\_ (name of fiduciary) in dealing with the Estate, and the beneficiaries is privileged and, in our opinion, no person is entitled to our work product. As we are *not* serving as your lawyer we understand that you may decide to retain your own lawyer to advise you about your own interests. If you do decide to hire your own lawyer, please advise us so that we can make sure that your lawyer is appropriately advised regarding matters pertaining to the Estate.

One of the most important duties that \_\_\_\_\_ (name of fiduciary) has is a duty of full disclosure to the beneficiaries, and we will try to assist in providing the beneficiaries with the appropriate required information.

You have important legal rights and if you have a question please call us to discuss your \_\_\_\_\_

<sup>6</sup>Issues of this sort are, like most matters, subject to court interpretation and the court's discretion.

question or concern. If we can help you we will do so; if we are not permitted to assist you then we will recommend that you seek advice from your own lawyer. It is imperative when you have a question or concern regarding the Estate that you advise \_\_\_\_\_ (name of fiduciary) or me of your question or concern.

## **7. Fees; Referral Fees; Commissions & Outside Sources of Income**

### **7.1 Client Files - KBA Ethics Opinion E-395, January 5, 1998.**

**7.1(a)** Question: May a lawyer hold a client's file because of a fee dispute?

**7.1(b)** Opinion:

KRPC 1.16(d) provides that "upon termination of representation" a lawyer shall "take steps to the extent reasonably practicable to protect a client's singular interest ... surrendering papers and property to which the client is entitled ...." Comment (10) to KRPC 1.16(d) states that "[t]he lawyer may retain papers as security for a fee only to the extent permitted by law." Whether a lien is permitted by law is a question of law. In Kentucky, a charging lien on the funds or property recovered in a lawsuit is authorized by statute law, but the Committee is not aware of any statute or case that provides a Kentucky lawyer with a retaining lien. In KBA E-235 the Committee answered with a qualified "yes" to the question, "[w]hen a lawyer has been discharged by a client may he refuse to deliver certain items in the file to the client?" The Committee cited with approval ABA Formal Opinion 1376, which set forth specific materials that had to be returned to the client in a trademark case:

- A. Notes and memos to the file prepared by the attorney containing recitals of facts, conclusions, recommendations;
- B. Correspondence between attorney and client;
- C. Correspondence between attorney and third party;
- D. Material furnished by the client ... ;
- E. Application, receipts, affidavits filed, in respect to use, etc. ...;
- F. Searches made at the expense of the client;
- G. Copies of the pleadings and the like filed in an administrative or court proceeding; and
- H. Legal research embodied in the memos or briefs.

However, the above opinion was predicated on the assumption that the lawyer's fee had been paid. KBA E-280 extended the above opinion by answering a "qualified yes" to the questions, "[m]ay a lawyer charge a fee for duplication of the client's file after the lawyer has been discharged?" The Committee determined "that a discharged lawyer may charge his former client for the actual costs involved in the duplication of a file, provided the lawyer does not charge a fee disproportionate to the actual costs of such duplication." The Committee added, however, that the lawyer may withhold materials within the lawyer's "work product privilege" from the client in the event of discharge. Together these opinions, along with KRPC 1.16(d), make it clear that the lawyer must turn over the file to the client or the client's attorney except for "work product."

Documents or other relevant evidence, the original of which may be required for trial preparation or as evidence for trial, must be surrendered in the original form. The lawyer does not have a statutory lien for the costs of duplication, but the lawyer is permitted to charge for the reasonable costs of duplication. Under no circumstances may the lawyer hold hostage the file. While the lawyer is entitled to reimbursement for costs incurred “including filing fees, service fees and costs for obtaining medical records,” the lawyer should “surrender” the file even if reimbursement is not forthcoming.

**7.1(c) Gilman Provision for Inclusion in Suggested Engagement Letter:**

If our firm’s representation terminates, and you would like to have a copy of any of the materials that are in our files, then we will be glad to accommodate your request and make the necessary arrangements to have another copy prepared for you or your new lawyer pending satisfactory arrangements for the pre-payment of the actual costs of duplicating the file materials, and subject to the payment of all outstanding fees to the firm.

**7.2 Sale of Life Insurance - KBA E-376**

**7.2(a) Question:** A member of a law firm asks the following questions:

1. May I sell insurance to a client, and receive a commission for it, when the sale of insurance is related to my representation of the client, and the legal representation involves estate and employee benefit planning?
2. Is disclosure to my client of my receipt of a commission necessary?
3. May I make the sale if there is no relationship between the insurance and the legal representation?
4. Is disclosure to my client of my receipt of a commission necessary?
5. May I prospect for insurance clients who are not now legal clients? What if they desire to become legal clients in the future?
6. Can I adjust my legal fees (discount) or would that be considered a rebate of commissions in violation of insurance statutes?
7. Can insurance commissions be considered partnership income, even if the commission is paid directly to me as an individual?
8. May I receive a referral fee from another insurance agent if I refer a client to him/her in connection with a legal matter? What disclosures are necessary to the client and to the insurance agent?
9. Are the answers to the above questions altered by using a low-load insurance product?



## **7.2(b) Opinion:**

**7.2(b)(1)** Without further comment on law-related services generally, the Committee believes that the Kentucky Rules of Professional Conduct permit the lawyer to sell life insurance products to the lawyer's clients when the sale of such insurance is related to the legal matter being handled by the lawyer, provided the applicable Rules of Professional Conduct are followed. The idea of selling insurance is already allowed with respect to the title insurance, and it is apparent that the client might benefit from such transactions. *On the other hand we find that the sale of life insurance products to clients constitutes a business transaction with a client, and that there is the potential for conflicts of interest; for example, the client's needs to maintain confidentiality regarding the client's health, and an insurer's need to have complete disclosure of all health questions.* Accordingly, the lawyer must be satisfied of compliance with Rules 1.7, 1.8(a). See Michigan Op., RI-135 (1992). Further, all fees and commissions must be disclosed to the client, and the client should consent to such arrangement in writing.

**7.2(b)(2)** Further, to make our position as clear as possible, we emphasize that a lawyer has a duty of loyalty to the client, and that advising a client about the disposition of the client's estate after death, and the sale of life insurance raises inherent problems of conflicts of interest as the insurer pays the agent (lawyer) to maximize insurance sales, and the lawyer's responsibility to maintain independence may be compromised; accordingly, it is necessary for the lawyer to disclose all of these matters in writing to the client, and to obtain the client's consent. The disclosure should advise the client that it is appropriate to obtain independent advice, counsel, in these unique circumstances.

**7.2(b)(3)** We emphasize that the lawyer may not solicit legal business personally or by telephone from current or former insurance customers unless they are also current or former clients. Michigan Op. RI-135. "Prospecting" for insurance clients from the lawyer's law office is inconsistent with our earlier opinions regarding the separation of other businesses from the lawyer's law practice, and invites misunderstandings and possible violations of the advertising rules. For this reason, Question 5 is answered with a "Qualified No." The answer is qualified because if the insurance business is sufficiently separate from the lawyer's law practice then that business may advertise for insurance customers purchasers like any other insurance agency. However, the separate business may not be used to circumvent the rules governing lawyer advertising.

**7.2(b)(4)** In the opinion of the Committee the lawyer should not accept referral fees for referring clients to other insurance agents. There is no apparent justification for accepting such fees as the lawyer is providing no substantial additional service to the client, and the suggested practice is difficult to reconcile with Rules 1.7 and 1.8(a). We also fear that such arrangements might lead to improper "feeding" of business.

## **7.3 Lawyers Receiving Commissions - KBA E -390.**

**7.3(a)** Question: May a lawyer, after disclosure to and consent by the client, receive compensation, structures as a percentage share of a recurring account management fee, for the lawyer's referral of the client to an investment advisor?

### **7.3(b) Opinion:**

**7.3(b)(1)** A question has been raised whether a lawyer may ethically affiliate with an investment advisor in an arrangement whereby the lawyer refers the client to the investment advisor in exchange for a percentage share of the investment advisor's recurring management fees (based on the amount of client's assets under management), even assuming arguendo, the lawyer has fully disclosed the referral fee arrangement and has obtained the client's written consent. In the opinion of the Committee, this arrangement presents a serious conflict of interest and is likely to involve circumstances where it is impossible for the lawyer to make sufficient disclosure to properly inform the client's consent.

**7.3(b)(2)** The referral fee arrangement raises concerns under a number of KBA Rules, including, among others, Rules 1.1 (requirement of competent counsel), 1.7(b) (prohibition of representation that may be materially limited by the lawyer's own interests), 1.8 (prohibition of business transactions with the client), 2.1 (requirement of professional independence) and 5.4 (prohibition of fee-sharing with non-lawyers). The prospect of the lawyer's referral compensation, supplementary to the legal fee already being paid by the client, is likely to interfere materially, on a continual basis, with the lawyer's independent professional judgment in objectively considering the client's best interests. Moreover, in many instances the lawyer's affiliation with the investment advisor and the resultant client referrals could involve the lawyer in matters beyond his professional competence, and, indeed, raises difficult questions regarding state and federal investment advisor registration and examination requirements. See, e.g., KRS 292.330; 808 KAR 10:260. Consequently, it would be difficult, if not impossible, for the lawyer to disclose fully and fairly to the client the consequences of pursuing the recommended course instead of other alternatives that the lawyer is unlikely to have evaluated or considered. These issues obviously become even more troublesome in the common situation where the client requests advice in the investment of funds obtained during the representation, funds which in many instances constitute the bulk of the client's personal assets. Should the client suffer the loss of these assets, the lawyer will be challenged to explain satisfactorily that his advice was based on his independent professional judgment and was not in any sense clouded by his own pecuniary interest in the management of the client's assets by the particular investment advisor to whom he referred the client.

**7.3(b)(3)** In conclusion, reference should be made to KBA E-264, which states that a lawyer could not ethically participate in an arrangement in which the lawyer would refer clients to a bank in exchange for a percentage fee based on the amount of deposited by those clients in bank-sponsored Individual Retirement Accounts. The opinion provides, "whether they are called referral fees or commissions or even kickbacks, they have one common characteristic, they are payments to an attorney for allowing that person or organization to make a profit from his client" and "attorneys are cautioned that a presumption exists that such referral fees are, even with full disclosure to the client and with his consent, unethical because they lend themselves to the appearance of impropriety."

#### **7.4 Donating Legal Services to Charity - KBA E-388.**

**7.4(a)** Question: May a lawyer advertise or otherwise promote the fact that he or she will donate a percentage of his or her fees to charities designated by the lawyer's clients?

**7.4(b)** Opinion: This practice would result in a violation of Rule 5.4(a). It would also result in violations of Rule 7.20(2), as it would encourage and condone referrals from charities in return for contributions. Lawyers are encouraged to make charitable contributions. But a majority of the Committee believes that making contributions part and parcel of advertising and business-getting is a negative development.

#### **7.5 Association with Financial Planner - Texas Opinion 446, May 1987.**

**7.5(a)** Question: May an attorney allow a financial planning organization to refer its members to him for preparation of wills and trusts and accept payment of part or all of his fee from the organization?

**7.5(b)** Facts:

**7.5(b)(1)** An organization that provides financial planning services conducts seminars which, among others things stress the importance of setting financial goals, making a will, choosing the right type of insurance, etc. Individual services consist of a review of a member's income tax returns, insurance review and advice, and investment counseling. No legal advice or legal services are rendered by the organization but in explaining to prospective members the services that are offered, a member is advised that \$150 of his membership fee goes towards the preparation of a will and living trust for the member and his spouse. Prospective members are told that if they are represented by local counsel, the organization will forward \$150 of the membership fee to their local counsel after the member consults with the attorney of his choice concerning terms and provisions which the financial planning group deems to be advantageous for the member. If the attorney's fee exceeds the \$150 paid by the organization, that fee is billed to the member by the attorney.

**7.5(b)(2)** If a prospective member is not represented by counsel, the organization provides the member with a list of attorneys with whom it has communicated and informs the member that the attorneys on the list have agreed to prepare two fairly simple wills and one living trust for \$150. The organization then forwards to an attorney in the area pertinent financial information pertaining to the member and the member is told that the attorney will contact the member to verify the financial information and ask any additional questions the attorney deems advisable.

**7.5(b)(3)** The organization contacts attorneys to inquire as to whether they are willing to make their services available to members of the financial planning group at the rate specified but promises no work and no referrals to attorneys. The organization does submit to the prospective attorneys a proforma copy of the simple wills and living trust recommended by the organization to its members, but the drafting of the wills and trust

agreements for a member are left entirely to the attorney.

**7.5(c) Opinion:**

**7.5(c)(1)** The relevant disciplinary rules are DR 2103, DR 2106, DR 3102 and DR 5107. DR 2103(E)(5) expressly allows an attorney to cooperate in a dignified manner with the legal services activities of a bona fide organization that recommends, furnishes or pays for legal services to its members or beneficiaries provided the conditions therein are satisfied. This is conditioned, of course, upon the fact that the lawyer's independent professional judgment is exercised in behalf of his client without interference or control by the organization.

**7.5(c)(2)** The financial planning organization described above derives no profit from the legal services rendered by lawyers to whom its members are referred. There is no indication that any lawyer to whom referrals are made initiated or promoted the formation of the organization or that it is operated for the purpose of procuring legal work or financial benefit for any lawyer as a private practitioner. The inquiry upon which this opinion is based clearly indicates that the member of the organization, and not the organization, is recognized as the client of the lawyer. If the statement of the services to be rendered for the flat fee of \$150 is not misleading or deceptive and the member is free to select an attorney of his choice, or reject an attorney whose name has been recommended by the organization, the guidelines under which the organization is operated appear to comport with the requirements of DR 2103(E)(5). To eliminate the possibility of a violation of DR 2101(A)(1), the organization must clearly inform its members that the \$150 does not necessarily cover the entire fee of an attorney for preparing the wills and trust agreement.

**7.5(c)(3)** DR 5107 is intended to prohibit a lawyer from being influenced by others than his client. Under the facts presented, the client has full knowledge that \$150 of the attorney's fee is being paid by the financial planning organization and there is no indication that the organization attempts to direct or regulate the attorney's professional judgment in rendering legal services to one of its members.

**7.5(c)(4)** No violation of the disciplinary rules results from an attorney allowing a financial planning organization to recommend him to a member of the organization who has no attorney or accepting payment for part or all of his fee for services rendered to a member under the facts set out above.

**7.6 Financial Services Firm Practicing Law - KBA U-50, June 17, 1997**

**7.6(a)** Question: May a financial and tax consulting firm, with lawyer and non-lawyer employees, solicit estate planning business and for a fee prepare estate planning documents for individual customers? Answer: No.

**7.6(b) Opinion:**

**7.6(b)(1)** The preparation and execution of wills and powers of attorney, and the

drafting and funding of living trusts involve legal knowledge and advise, and therefore constitute the practice of law. SCR 3.202; *Kentucky State Bar Association v. Holland*, 411 S.W.2d 674 (Ky. 1967). Such services affect the legal rights of, and involve the risk of financial harm to, the individual who received such services and to that individual's heirs and beneficiaries. The public interest demands that estate planning services be rendered only by lawyers, who are held to high standards of competence, ethics, and confidentiality, and who tailor documentation to their client's needs. The performance of and solicitation for such services by non-lawyers constitutes the unauthorized practice of law in violation of KRS 524.130.

**7.6(b)(2)** Estate planning marketing schemes are typically misrepresented as the cure for all family and tax bills, are aimed at the elderly, and result in canned documents prepared by lawyer or non-lawyer employees of the financial services marketer who have little knowledge or and no loyalty to the customer. *In re Mid-America Living Trust Associates, Inc.*, 927 S.W.2d 855 (S. Ct. Mo. 1996).

**7.6(b)(3)** The employment of staff attorneys by marketers to prepare wills, trusts, and powers of attorney does not avoid the unauthorized practice of law. Neither corporations nor their salaried employee attorneys may offer legal services to the public. *Kentucky Bar Association v. Tussey*, 476 S.W.2d 177 (Ky. 1972); *Frazee v. Citizens Fidelity Bank & Trust Co.*, 393 S.W.2d 778 (Ky. 1965).

**7.6(b)(4)** Practicing attorneys who review documents prepared by non-lawyer employees of such marketers, or who share fees with such marketers, aid the unauthorized practice of law in violation of SCR 3.130(5.5)(b) and 3.470. See *In re Mid-America Living Trust Associates, Inc.*, 927 S.W.2d 855, 867-869 (Mo. S.Ct. 1996).

## **7.7 Fee Agreement Inserted In Will - Florida Bar Opinion 64-15, March 25, 1964.**

**7.7(a)** Facts: A client retains lawyer to prepare Will in which he leaves all of his property to two non-resident children who are designated as joint executors. The estate will have a gross value for probate purposes in excess of \$100,000, the assets are almost entirely liquid, and a limited amount of probate work will be involved. The client has asked the lawyer to handle the estate and represent the executors although he is not known to them. The client wishes him to set a fee with him presently under a binding agreement to be inserted in the will or covered by separate agreement. He inquires whether a violation of professional ethics is indicated.

**7.7(b)** No question of ethics is presented. A lawyer can make such arrangement regarding his fee as might be reasonable under the circumstances. Certainly, however, he is under no duty to fix his fees in advance and he would be justified in naming a fee large enough to cover all of the complexities which might reasonably be expected to arise. There is considerable doubt whether a provision in the will regarding fees would have validity since the joint executors have the right to select counsel of their own choosing. Similarly, a contract might have no legal efficacy except perhaps to work an estoppel against a later claim for larger fees. Before making any agreement with the client, it might be well to suggest there may be a lack of wisdom in entering into such a contract from the viewpoint of the client. Portions of this opinion refer to matters which are legal in nature. Our authority is limited to the ethical matters only and our

opinions are purely advisory.

## **7.8 Division of Fees - Florida Bar Opinion 90-8, March 1, 1991.**

**7.8(a)** Question Presented: The Committee has been asked to render an opinion whether a Florida attorney may ethically divide a fee with a non-Florida attorney. This inquiry has been made by a number of Florida Bar members who have questioned the propriety of sharing, usually in a referral context, a fee with an attorney who is not admitted to The Florida Bar. Four possible fee division scenarios will be discussed. They are:

**7.8(a)(1)** A member of an out-of-state bar lives in a condominium in Florida. A resident of the condominium who needs legal advice talks to the out-of-state attorney. The attorney refers the resident to a Florida attorney.

**7.8(a)(2)** A resident of another state consults an attorney out of state regarding a criminal matter in Florida. The out-of-state attorney decides that a Florida attorney must be associated on the matter.

**7.8(a)(3)** A resident of another state is injured in Florida while on vacation. The injured person consults with an attorney in the person's home state. That attorney refers the case to a Florida attorney who charges a contingent fee.

**7.8(a)(4)** A Florida attorney refers a case to a non-Florida law firm to be prosecuted in a foreign jurisdiction. That jurisdiction has a rule which permits a 50% "referral fee."

**7.8(b)** Florida Rule 4-1.5. Paragraph (G) sets forth the requirements governing the division of fee in any type of case: Subject to the provisions of paragraph (F)(4)(d), a division of fee between lawyers who are not in the same firm may be made only if the total fee is reasonable and: (1) The division is in proportion to the services performed by each lawyer; or (2) By written agreement with the client: (a) Each lawyer assumes joint legal responsibility for the representation and agrees to be available for consultation with the client; and (b) The agreement fully discloses that a division of fees will be made and the basis upon which the division of fees will be made.

### **7.8(c) Answers to Four Questions.**

**7.8(c)(1)** In prior ethics opinions the Committee concluded that it would be improper for a Florida attorney to divide a fee with a non-Florida attorney who resides in Florida and refers a case to the Florida lawyer. The Committee stated that it may constitute aiding the unauthorized practice of law to accept cases referred by the non-Florida attorney. Additionally, the Committee stated that the restriction on dividing a fee with a non-lawyer prohibits a Florida attorney from sharing a fee with an inactive non-Florida lawyer residing in Florida. As noted above, the fee division provisions of Rule 4-1.5 require an attorney to either work on a matter or assume joint legal responsibility in order to receive a portion of a fee (depending upon whether the fee is on a contingent or non-contingent basis). Therefore, in hypothetical scenario one the Florida attorney could

not divide a fee with the resident non-Florida attorney who refers a case because, the non-Florida attorney cannot practice law in Florida or agree to assume joint responsibility as is required by the rules. A division of fee in such a case would constitute improper fee-sharing with a non-attorney and could constitute aiding in the unlicensed practice of law.

**7.8(c)(2)** Regarding the second and third hypothetical scenarios, in which a Florida attorney accepts a referral from an out-of-state attorney, the Florida attorney may divide a fee with the referring attorney provided the division is in compliance with Rule 4-1.5. Any case referred to a resident Florida Bar member practicing Florida law presumably will be related to Florida or Florida law. A member of The Florida Bar is obligated to comply with the Rules Regulating The Florida Bar, including the fee division rules. Therefore, it would be unethical for a Florida attorney to pay a referral fee to an out-of-state attorney absent compliance with the applicable fee division rules, regardless of whether the referring attorney is a member of The Florida Bar.

**7.8(c)(3)** In the second scenario the fee division is specifically governed by paragraph (G) of the Rule. Paragraph (F) is inapplicable because a fee in a criminal case cannot be contingent. Thus, the Florida attorney ethically may share a fee with the out-of-state attorney in this case either based on work done or by written agreement with the client in accordance with the requirements of paragraph (G). Unlike the non-Florida attorney who resides in Florida, a practicing out-of-state attorney would be able to legitimately provide some legal services to the out-of-state client, thereby avoiding the problems cited in Opinions 60-18 and 62-3.

**7.8(c)(4)** The third scenario triggers the application of paragraphs (F)(1), (F)(2) and F(4)(d) of Rule 4-1.5 because a contingent fee is involved. Accordingly, the attorney who assumes primary responsibility must receive a minimum of 75% of the total fee and the attorney assuming secondary responsibility may receive a maximum of 25% of the total fee. The fee division agreement must be reduced to writing and the client must consent in writing to the agreement. As in the second scenario, presumably the out-of-state attorney can provide services to the out-of-state client thus avoiding the problems noted in the cited ethics opinions.

**7.8(c)(5)** If, as in scenario four, a Florida attorney refers a case to an out-of-state attorney and participates in the fee, the referring attorney must comply with paragraph (G) of the Rule. In contingent fee cases paragraphs (F)(1) and (2) also apply. Furthermore, paragraph (F)(4)(d) is applicable in personal injury-type contingent fee cases. If the applicable fee division rules are followed, it will be ethical for the Florida attorney to divide a fee with the out-of-state attorney. In adopting the fee division limitations set forth in Rule 4-1.5(F)(4)(d), the Supreme Court of Florida stated that those limitations “will not apply to nonresident bar members unless those nonresidents practice in matters of Florida law.” 519 So.2d 971, 972. That is the only exception to the 25% limitation allowed by the court (aside from the exception contained in the rule itself for true co-counsel who obtain circuit court authorization for a different fee-division arrangement). Nothing in the Supreme Court’s order, the rule, or the comment to the Rule suggests that the 25% limitation is inapplicable when a Florida Bar member refers a case to an attorney in another state. Nevertheless, in cases where the referring Florida Bar member

participates in the trial of the out-of-state case, choice of law principles should determine whether the Florida contingent fee rule applies. In Opinion 88-10, the Committee considered a situation in which an out-of-state attorney with an out-of-state client and an out-of-state lawsuit sought to have a Florida attorney (who was either licensed in the other state or admitted there pro hac vice) participate in the trial of the case. The Committee opined that the other state had a more significant relationship to the client and the cause of action than did Florida; therefore, the Committee concluded that the other state's contingent fee rules were applicable.

## **8. Client Disability**

### **8.1 Rule 1.14 - *Client Under a Disability*.**

#### **8.1(a) Text:**

**8.1(a)(1)** When a client's ability to make adequately considered decisions in connection with the representation is impaired, whether because of [minority] age, mental disability or for some other reason, the lawyer shall, as far as reasonably possible, maintain a normal client-lawyer relationship with the client.

**8.1(a)(2)** A lawyer may seek the appointment of a guardian or take other protective action with respect to a client, only when the lawyer reasonably believes that the client cannot adequately act in the client's own interest.

#### **8.1(b) Comment:**

**8.1(b)(1)** The normal client-lawyer relationship is based on the assumption that the client, when properly advised and assisted, is capable of making decisions about important matters. When the client is a minor or suffers from a mental disorder or disability, however, maintaining the ordinary client-lawyer relationship may not be possible in all respects. In particular, an incapacitated person may have no power to make legally binding decisions. Nevertheless, a client lacking legal competence often has the ability to understand, deliberate upon, and reach conclusions about matters affecting the client's own well-being. Furthermore, to an increasing extent the law recognizes intermediate degrees of competence. For example, children as young as five or six years of age, and certainly those of ten or twelve, are regarded as having opinions that are entitled to weight in legal proceedings concerning their custody. So also, it is recognized that some persons of advanced age can be quite capable of handling routine financial matters while needing special legal protection concerning major transactions.

**8.1(b)(2)** The fact that a client suffers a disability does not diminish the lawyer's obligation to treat the client with attention and respect. If the person has no guardian or legal representative, the lawyer often must act as de facto guardian. Even if the person does have a legal representative, the lawyer should as far as possible accord the represented person the status of client, particularly in maintaining communication.

**8.1(b)(3)** If a legal representative has already been appointed for the client, the



lawyer should ordinarily look to the representative for decisions on behalf of the client. If a legal representative has not been appointed, the lawyer should see to such an appointment where it would serve the client's best interests. Thus, if a disabled client has substantial property that should be sold for the client's benefit, effective completion of the transaction ordinarily requires appointment of a legal representative. In many circumstances, however, appointment of a legal representative may be expensive or traumatic for the client. Evaluation of these considerations is a matter of professional judgment on the lawyer's part.

**8.1(b)(4)** If the lawyer represents the guardian as distinct from the ward, and is aware that the guardian is acting adversely to the ward's interest, the lawyer may have an obligation to prevent or rectify the guardian's misconduct. See Rule 1.2(d).

**8.1(b)(5)** Rules of procedure in litigation generally provide that minors or persons suffering mental disability shall be represented by a guardian or next friend if they do not have a general guardian. However, disclosure of the client's disability can adversely affect the client's interests. For example, raising the question of disability could, in some circumstances, lead to proceedings for involuntary commitment. The lawyer's position in such cases is an unavoidably difficult one. The lawyer may seek guidance from an appropriate diagnostician.

## **8.2 Florida Opinion 85-4, 10/1/1985 - Reconsidered & Approved on 9/10/1998.**

**8.2(a) Facts:** The inquiring attorney represents W, who is petitioning for dissolution of marriage. A settlement agreement had been made between W and H, her husband. However, before the settlement was complete, W began exhibiting signs of mental illness. The inquiring attorney suggested W seek professional help; however, W took this as evidence that the lawyer was possibly involved in a plot against her. W refuses to see a psychiatrist or psychologist. The attorney feels that it would not be in the best interests of W for her to withdraw from representation and states that she does not want to abandon her client by withdrawing. However, she does not believe that she could allow W to sign a stipulation or go to trial, or that she could divulge to a third party W's need for psychiatric help.

**8.2(b) Opinion:** "The inquiring attorney does not have to abandon her client by withdrawing. The attorney should do what she can to safeguard the interests of her client, including making prudent decisions in behalf of the client. If the attorney believes the settlement between H and W to be fair, the attorney may help W to exercise her rights in the dissolution. If the attorney believes that W cannot adequately act in her own interest, and that a guardian may be necessary to safeguard W's interests, the attorney may seek appointment of a legal guardian for W, even over W's objection if absolutely necessary. The inquiring attorney is in the best position to decide the proper course of action from the suggestions above. In proceeding, the attorney should be careful to respect the rights of her client, to act in the client's best interests, and to avoid overreaching.

## **8.3 ABA Commission 2000 Report.**

## **9. Estate Planning Opinions of Interest**

## **9.1 Retention of Client Wills - New York Opinion 724 - 11/30/99.**

**9.1(a) Question:** If a lawyer keeps custody of a client's original will, absent agreement does the lawyer have an obligation to learn of the client's death and, upon the client's death, to file the original will with an appropriate court?

**9.1(b) Opinion:**

**9.1(b)(1)** A lawyer who drafts a client's will has no obligation to maintain the original will for safekeeping. After the client executes the will, the lawyer may provide the original will to the client, along with appropriate advice concerning its safekeeping. The practice of safekeeping clients' wills appears to have become less routine over time, because clients increasingly believe themselves able to keep their own wills safe. Nevertheless, safekeeping the client's will remains an appropriate function for a lawyer to perform.

**9.1(b)(2)** Whether the lawyer will maintain the original will and, if so, what additional obligations the lawyer will assume, are primarily matters to be agreed upon by the lawyer and client after consultation. Contractual obligations may arise if there are express or implied agreements or understandings between the client and the lawyer in regard to the lawyer's duties and responsibilities in relation to the will. Thus, the lawyer and client may agree that the lawyer will undertake the responsibility to learn of the client's death (*e.g.*, by reading death notices). They may also agree that, upon learning of the client's death, the lawyer will file the will with the appropriate court. Ordinarily, a lawyer would be obligated to carry out such contractual undertakings, as would the lawyer's firm in the event the lawyer was unable to carry out the undertaking personally. *Cf.* N.Y. County 709 (1995). Whether or not a lawyer undertakes a contractual obligation of this nature in a particular situation raises questions of fact and law about which the Committee cannot provide guidance, since our role is limited to interpreting the Code of Professional Responsibility.

**9.1(b)(3)** When the lawyer does agree to retain the client's original will, the lawyer obviously may not destroy it, but must keep custody of it until the client requests it or the lawyer is legally obligated to produce it. The lawyer should discuss with the client what, if any, additional obligations the lawyer will assume. At least absent agreement to the contrary, there will ordinarily be an implied understanding that after the client's death, if the lawyer has maintained the original will and, as far as the lawyer knows, there is no later valid one, the lawyer must take steps to ensure that the executor and/or beneficiaries are aware of the will's existence. Thus, as we have previously observed, where a client has requested his lawyer to retain the original will for safekeeping, and the lawyer later learns of the client's death ... it would appear that the lawyer has an ethical obligation to carry out his client's wishes, and quite possibly a legal obligation ... to notify the executor or the beneficiaries under the will or any other person that may propound the will ... that the lawyer has it in his possession. Even though the duty of confidentiality under Disciplinary Rule ("DR") 4-101 ordinarily continues after the termination of the lawyer-client relationship and after the client's death, *see* Ethical Consideration ("EC") 4-6,

disclosure of the will's existence is permissible in this situation, because the disclosure was impliedly, if not explicitly, authorized by the client.

**9.1(b)(4)** Whether the lawyer who safeguards the client's will has additional obligations—*e.g.*, whether the lawyer must take steps to learn of the testator's death, or whether the lawyer must file the will with the court upon the testator's death—will be determined in the first instance not by the Code, but by the express or implied understanding between the lawyer and client at the time the lawyer agreed to safeguard the will or by any subsequent understanding. Therefore, the lawyer should make every effort to clarify precisely what the lawyer will and will not do in the event the lawyer maintains the original will. The lawyer has no ethical obligation to agree to read death notices, *see* Massachusetts Op. 76-7 (a lawyer “need not watch the obituary columns”), or to agree to file the original will with the court; the client may have good reason not to ask the lawyer to assume such obligations; and the lawyer generally has no ethical obligation later to undertake responsibilities vis-a-vis the original will in addition to those on which the lawyer and client agreed and those imposed by law. By clarifying the extent and limits of the lawyer's obligations, the lawyer will enable the client to make an informed decision whether the lawyer should safeguard the will and, if so, what additional steps the client should take (*e.g.*, whether to tell others, such as the executor or beneficiaries, where the will is to be found). Doing so will also reduce the risk that the lawyer will later fail to undertake a responsibility that, from the testator's perspective, the lawyer was obligated to undertake.

## **9.2 Preparation of Questionable Document - Florida Opinion 76-35, October 17, 1977.**

**9.2(a)** Facts: A lawyer has been asked to draft a document, and the lawyer is in doubt as to the legality of the instrument. He is also in doubt as to whether performance of certain conduct authorized by the instrument to be taken by a third party would be in violation of law, especially criminal law. The Committee assumes that the lawyer has an “absolute, genuine, good faith uncertainty” as to the legality of the instrument and as to the legality of that conduct so authorized to be taken by the third party. The Committee also assumes that the lawyer cannot, under the current state of the law, advise the client with any degree of assurance at all that the instrument is or is not lawful and that such third-party conduct would or would not be lawful.

### **9.2(b) Opinion:**

**9.2(b)(1)** EC 7-3 provides, in pertinent part: “Where the bounds of law are uncertain the action of the lawyer may depend on whether he is serving as an advocate or advisor ... [A] Lawyer serving as advisor primarily assists his client in determining the course of future conduct and relationships ... In serving a client as advisor, a lawyer in appropriate circumstances should give his professional opinion as to what the ultimate decisions of the courts would likely be as to the applicable law.” But EC 7-3 does not address the point, or provide specific guidance, as to what the lawyer should do in a situation where, due to genuine uncertainty as to the law, especially in areas without precedent, the lawyer cannot render an opinion in good faith with any degree of assurance that it will likely ultimately be consistent with the decisions of the courts. More specifically, as to the general facts of this inquiry, EC7-3 does not appear to provide

guidance as to the conduct of an attorney in preparing an instrument of the type described in this inquiry where the attorney has such genuine uncertainty as to the likely outcome in the courts in the event the instrument, or the conduct authorized thereby, is challenged. It is that point to which this Opinion of the Committee is directed. The disciplinary rules of the Code, in our view, are likewise not specifically directed to the subject matter of this inquiry, although DR7-102(A)(7) does say that a lawyer is specifically precluded from counseling or assisting his client ... "in conduct that the lawyer *knows* to be illegal or fraudulent."

**9.2(b)(2)** It is the Committee's opinion, taking into consideration the foregoing . . . , that the actions of the inquiring attorney in preparing the suggested instrument and in advising the client with respect to the instrument should be dictated and governed by the lawyer's evaluation of the state of the law and, in the event of genuine uncertainty on his part in that regard, he should give to the client his opinion to that effect, accompanied by full disclosure to the client of all of the relevant considerations and possible legal effects, including any possibility of civil or criminal liability on the part of anyone as a result of the instrument and conduct thereunder. The client should clearly be advised as to the possible liability of the third party who is designated to use the instrument and authorized thereby to engage in certain conduct. In addition, that third party should receive like advice from the attorney if the third party is not involved in the transaction or does not have his own counsel in that regard.

### **9.3 Conflict in Will Preparation. Texas Opinion 439, 1987.**

**9.3(a)** Facts: An attorney prepares a will, which is signed by two witnesses, with the attorney acting as notary. The attorney files the will for probate and acts as attorney for fiduciary. A will contest is filed, claiming that the will was not executed in accordance with the laws of the State, and that the Testatrix did not have testamentary capacity. A motion is filed to disqualify the attorney who prepared the will and notarized it.

**9.3(b)** Question: Is the attorney who prepared the will and notarized it disqualified to continue to act as attorney for the Independent Executrix and sole beneficiary under the will?

**9.3(c)** Opinion: DR 5-101 provides: "A lawyer shall not accept employment in contemplated or pending litigation if he knows or it is obvious that he or a lawyer in his firm ought to be called as a witness." There are certain exceptions to this and one exception is: "If refusal would work a substantial hardship on the client because of the distinctive value of the lawyer or his firm as counsel in the particular case." At the time the attorney was asked to accept employment in the will contest, he knew that he ought to be called as a witness in the case. The facts stated do not give rise to an exception to this rule. Disqualification is further imposed, even if it should be held that the attorney's employment in the matter began when he was hired to draw the will rather than at the time when the will contest was contemplated, or that the employment began when the attorney was hired to handle the probate of the will at a time when no contest was contemplated. Under DR 5-102(A), if after an attorney undertakes employment in contemplated or pending litigation it is learned or it is obvious that he or his firm may be called as a witness on behalf of his client, he must withdraw from the case. Not only must the attorney withdraw, but also his firm must withdraw from employment. There are exceptions, but again the

facts do not give rise to one of these exceptions. Opinion 234 faced issues similar to the issues faced here. In that case A's law partner, B, drafted a will, deed and contract for a client. After the death of the client, the instruments were attacked on grounds of fraud, undue influence and material incapacity of the deceased client. It was held that B's testimony would obviously be important in establishing mental capacity and in establishing the circumstances. It was held that it would be improper for the attorney to accept the case knowing that he would be a material witness. Therefore, the attorney was disqualified.

**9.3(d) Note - Model Rule Answer:** Rule 3.7, *Lawyer as Witness*, as follows:

(a) A lawyer shall not act as advocate at a trial in which the lawyer is likely to be a necessary witness except where:

- (1) The testimony relates to an uncontested issue;
- (2) The testimony relates to the nature and value of legal services rendered in the case; or
- (3) Disqualification of the lawyer would work substantial hardship on the client.

(b) A lawyer may act as advocate in a trial in which another lawyer in the lawyer's firm is likely to be called as a witness unless precluded from doing so by Rule 1.7 or Rule 1.9.

**9.4 Necessity of Personal Client Contact.**

**9.4(a)** Florida Bar Opinion 67-14, July 24, 1967.

**9.4(a)(1)** A lawyer may not accept employment by a real estate broker to prepare a deed for use by the broker in closing a real estate transaction when the lawyer would have no contact with either party to the transaction.

**9.4(a)(2)** On the facts before us, which in essence involve the intervention of a broker between the lawyer and the client, we have no hesitancy in concurring in Informal Opinion 508 of the American Bar Association (1962), disapproving this practice in essence on the ground that such a transaction is devoid of the personal contact which should exist between attorney and client.

**9.4(b)** Florida Bar Opinion 67-15, July 24, 1967. The rationale of Opinion 67-14 precludes a lawyer from preparing a trust pursuant to a referral from a trust company in the absence of direct contact with the client.

**9.5 Purchase of Property From An Estate. Opinion KBA E-217**

*Question #1:* May a lawyer who is either executor/administrator and/or attorney for an estate purchase real or personal property from the estate?

*Answer:* No.

*Question #2:* May an attorney obtain a proprietary interest in real estate as compensation for his

legal services in lieu of a monetary fee?

*Answer:* Qualified yes.

*References:* DR5-101(A), 5-103(A); CJ ABA Informal Opinion 804 (1964), 1145 (1970); EC 5-2, 503, 5-7

### Question 1

Although DR5-101(A) is not directly responsive to the question here, it does provide background for discussion of the issue: "Except with the consent of his client after full disclosure, a lawyer shall not accept employment if the exercise of his professional judgment on behalf of his client will be or reasonably may be affected by his own financial, business, property or personal interests." The effect of DR5-101(A) is to call upon the attorney for the estate to predict whether he or she will want to acquire assets of the estate at a future time. Moreover, the attorney who has determined the likelihood of a prospective interest in estate assets must fully disclose the extent of that interest to the client before accepting employment. The effect of rigidly enforcing DR5-101(A) would be for every attorney to make a full disclosure of a possible future interest in acquiring estate assets before accepting employment.

Besides the practical problems associated with DR5-101(A), the purchase of assets of an estate by the attorney for the estate or an attorney as executor/administrator is fraught with obvious appearances of impropriety and potential breaches of fiduciary duty to the estate. The attorney is "in position to effect the appraisal of the property and influence prospective bidders in one manner or another ..." (ABA Informal Opinion 804 (1964)).

The purchase of assets under these circumstances is probably proper when a testator has so provided in the will. Otherwise, however, the attorney would have to advise the beneficiaries to seek other counsel before he or she purchases assets. Even if counsel obtained the consent of all adult beneficiaries, a problem would arise with respect to the protection of all minor beneficiaries and unborn beneficiaries. That no unfair profit would inure to the attorney as a result of the purchase is no justification, for even the appearance of duress, fraud or deception is harmful to the legal profession. True, a personal representative may acquire an estate asset "for the best interests of the estate" and "for the best price obtainable," KRS 395.200. True, the sale of estate assets may be conducted publicly, as is discretionary regarding personalty (per KRS 395.195(6)) and mandatory regarding realty (per KRS 395.515). Still, the appearance of abusing confidences given the attorney is detrimental to the profession. Moreover, in this situation, there is a reasonable possibility that the attorney's professional judgment on behalf of his client before the purchase would be affected by his or her self-interest, DR5-101(A).

### Question 2

DR5-103(A) provides that an attorney "shall not acquire a proprietary interest in the cause of action or subject matter of litigation he is conducting for a client, except that he may: (1) acquire a lien granted by law to secure his fee or expenses." Unless he acquires a common law or statutory lien, an attorney cannot acquire a proprietary interest in the subject matter of litigation.

... After accepting employment, a lawyer carefully should refrain from acquiring a property right or assuming a position that would tend to make his judgment less protective of the interest of his client. [EC 5-2].

... After accepting employment, a lawyer should not acquire property rights that would adversely affect his professional judgment in the representation of his client. Even if the property interests of a lawyer do not presently interfere with the exercise of his independent judgment, but the likelihood of interference can reasonably be foreseen by him, a lawyer should explain the situation to his client and should decline employment or withdraw unless the client consents to the continuance of the relationship after full disclosure. [EC 5-3]

The possibility of an adverse effect upon the exercise of free judgment by a lawyer on behalf of his client during litigation generally makes it undesirable for the lawyer to acquire a proprietary interest in the cause of his client or otherwise to become financially interested in the outcome of the litigation. However, it is not improper for a lawyer to protect his right to collect a fee for his services by the assertion of legally permissible liens, even though by doing so may acquire an interest in the outcome of litigation ... [EC 5-7]

From a reading of the Code of Professional Responsibility, it appears that a lawyer may obtain a proprietary interest in real estate as compensation for his legal services as long as the real estate was not the subject matter of litigation he is conducting for the particular client.

# **THE TOTAL RETURN TRUST:**

## **The Big Points**

***Barton T. Rogers  
Frost Brown Todd LLC  
Lexington, Kentucky***

\* The author wishes to acknowledge the substantial contributions made to this material by Jack Cunningham, a fellow member of Frost Brown Todd LLC, Lexington, Kentucky.

Copyright 2002. Barton T. Rogers. All Rights Reserved.

## **SECTION E**





## **THE TOTAL RETURN TRUST: THE BIG POINTS**

<b>1.</b>	<b>Introduction .....</b>	<b>E-1</b>
<b>2.</b>	<b>Meeting The Objectives Of Grantors .....</b>	<b>E-2</b>
<b>3.</b>	<b>Historical Legal Framework .....</b>	<b>E-2</b>
A.	Kentucky's Prudent Man Rule .....	E-3
B.	The Prudent Investor Rule - Restatement (Third) Of Trusts .....	E-4
	§ 227 - General Standard of Prudent Investment .....	E-5
	§ 228 - Investment Provisions of Statute or Trust .....	E-6
	§ 229 - Duty with Respect to Original Investments .....	E-6
C.	Kentucky's Prudent Investor Rule - KRS 287.277 .....	E-7
D.	Kentucky's Revised Uniform Principal And Income Act (1962) .....	E-8
E.	The Revised Uniform Principal And Income Act (1997) .....	E-10
F.	KBA Probate Section Proposed Legislation (2002) .....	E-11
	(1) The Kentucky Uniform Prudent Investor Act .....	E-11
	(2) The Kentucky Uniform Principal And Income Act .....	E-11
<b>4.</b>	<b>Guidance From The Nonprofit Sector .....</b>	<b>E-11</b>
<b>5.</b>	<b>Alternatives To The Income Rule Trust .....</b>	<b>E-12</b>
A.	Discretionary Trusts .....	E-13
B.	Inflation Adjustment Trusts .....	E-13
C.	Total Return Unitrust .....	E-14
<b>6.</b>	<b>Tax Implications Of Total Return Trusts .....</b>	<b>E-17</b>
A.	Marital Deduction Trusts .....	E-18
B.	Taxation Of Capital Gains .....	E-19

### **SECTION E**

C.	GST Trusts .....	E-20
D.	Tax Summary .....	E-21
<b>7.</b>	<b>Conclusion .....</b>	<b>E-21</b>
	NOTES .....	E-22
	SAMPLE TOTAL RETURN UNITRUST .....	E-23
	BIBLIOGRAPHY .....	E-29

## SECTION E

## **The Total Return Trust**

### **1. Introduction**

Increased uses of trusts have expanded the number of beneficiaries critically watching every move of their trustees. Expectations of trust beneficiaries have evolved during recent economic trends – two decades of decreasing interest and dividend rates contrasted with increasing equity appreciation, notwithstanding the stock market downturns of 2000-2002. The standard trust arrangement finds a lifetime beneficiary seeking more current income and a remainder beneficiary seeking growth of corpus for future distributions. The robust growth of stocks in the 1990's created continuing and unrealistic expectations in the minds of younger generations who have discovered the power of compounded growth. These future beneficiaries expect trust asset growth to match their 401(k) accounts. At the same time, the income beneficiary finds current distributions unacceptable and expects the high income yields of yesteryear. The trustee finds a dilemma serving two masters. The legal duty of impartiality turns into a nightmare for the trustee. The duty becomes – as one commentator has called it – the “duty to disappoint equally.”<sup>1</sup>

The traditional approach for the trustee has been to divide the loyalties and allocate the portfolio between assets that produce regular returns of dividend, interest and other income, with the balance of the trust assets committed to growth-oriented assets – equities. The fixed-income assets have little or no appreciation potential, which displeases the remaindermen. In most cases, the next generation's share will be divided up, multiplying the perceived inequity among many family members and increasing the number of persons to put pressure on the trustee. At the same time, the equities may produce little current income, which displeases the life beneficiary, who considers himself or herself the primary beneficiary.

What is a prudent trustee to do? How can these competing objectives be satisfied? The “total return trust” is an attempt to change the traditional “income rule” trust model in a way to put the beneficiaries – income and remaindermen – and the trustee back on the same team. By adopting modern portfolio theory, as set forth in the Prudent Investor Rule, along with a newly revised Uniform Principal and Income Act, traditional distinctions between income and principal are blurred, if not obliterated, in an attempt to focus on the “total return” from all investments within an acceptable level of risk and to use that return for the good of all beneficiaries.

## **2. Meeting the Objectives of Grantors**

The total return trust should be viewed by the practitioner as another tool in the estate planning toolbox. It is not appropriate in all trust planning situations, as no single solution will ever apply. A multi-generational trust to maximize duration of assets in trust for large numbers of beneficiaries may benefit from a total return trust method. The total return trust may be appropriate for the surviving spouse, especially with the QTIP trust, where adequate provision for the children/remaindermen is an objective on par with lifetime income for the surviving spouse. As always, the marital trust brings special tax considerations, and those are discussed briefly below. The perpetual charitable trust designed exclusively for one or more charitable beneficiaries to receive annual distributions is an excellent total return trust candidate. The estate planner must carefully consider the grantor’s objectives before adopting the total return trust.

## **3. Historical Legal Framework**

Current Kentucky law impedes the total return trust. Customized drafting is required to accomplish the desired objectives. A review of relevant Kentucky law highlights the problem

facing the trustee in the traditional trust model. New uniform laws are in place – although adopted only in part in Kentucky – that will allow existing trusts and future trusts not drafted as total return trusts to be administered as total return trusts.

**A. Kentucky's Prudent Man Rule**

KRS 386.810 embodies the current version of Kentucky's standard of trust administration, including trustee investing, for *non-corporate fiduciaries*. Adopted in 1976, the statute states that "a trustee has the power to perform, without court authorization, every act which a prudent man would perform for the purposes of the trust . . . . (Emphasis added.) Long before the enactment of this statute, Kentucky courts have held to the Prudent Man Rule, and the enunciation of the rule has varied only slightly throughout the past century. In Citizens National Bank v. Jefferson,<sup>2</sup> the seminal Kentucky case concerning trustee investments, the application of the rule was stated as follows: "The prime object should be to make a safe investment, that will yield a reasonable income for the beneficiary for life, and, when this is done, the trustee has discharged his duty. . . . The true test is, have the trustees acted in good faith, and would the investment have been made by prudent businessmen with a view of securing a safe income for themselves or their families."<sup>3</sup> Although the "prudent businessman" standard found its way into certain Kentucky statutes in 1942, see e.g., KRS 386.020 and 386.070, the highest court of Kentucky adopted the Prudent Man Rule in 1943 verbatim as set forth in the Restatement of the Law of Trusts, § 174 (1935).<sup>4</sup>

Along with the general Prudent Man Rule to guide trustees, Kentucky statutes have contained lists of appropriate investments for over a century.<sup>5</sup> Unlike some jurisdictions that hold such "legal lists" as restrictive or prohibitive lists beyond which a trustee may not invest, Kentucky's statutes are best considered as "permissive lists" or "safe harbors" of authorized

investments representing a guideline for trustees under the broad umbrella of the Prudent Man Rule. Of interesting note is that the safe harbor of KRS 386.020 allows investments in common stock but with the requirement that such be "dividend-paying," which of necessity forces a review of each individual investment asset.

In summary, the Prudent Man Rule provides that each trust investment must be analyzed separately to determine its suitability for the trust portfolio. In addition, the trustee has no clear duty to diversify investments.<sup>6</sup> Finally, the trustee may not delegate investment responsibility.

#### **B. The Prudent Investor Rule – Restatement (Third) of Trusts**

The 1992 publication of the Third Restatement represented a substantial evolution and modernization of trust investment law. The new Prudent Investor Rule was designed to rectify the perceived chilling effect of judicial layering over the original "generality and adaptability of the Prudent Man Rule."<sup>7</sup> The new Rule is also designed to accommodate recent research in the concepts of financial investing, often denominated as "Modern Portfolio Theory," although the Introduction states that the Rule is not "endorsing or excluding any particular theories of economics or investment."<sup>8</sup>

The stated objectives of the new Rule "range from that of liberating expert trustees to pursue challenging, rewarding, nontraditional strategies when appropriate to the particular trust, to that of providing other trustees with reasonably clear guidance to safe harbors that are practical, adaptable, readily identifiable, and expectedly rewarding."<sup>9</sup> These new goals and objectives are reflected in the language of the new Rule:

## **§227 – General Standard of Prudent Investment**

The trustee is under a duty to the beneficiaries to invest and manage the funds of the trust as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the trust.

(a) This standard requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the trust portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the trust.

(b) In making and implementing investment decisions, the trustee has a duty to diversify the investments of the trust unless, under the circumstances, it is prudent not to do so.

(c) In addition, the trustee must:

(1) conform to fundamental fiduciary duties of loyalty (§170) and impartiality (§183);

(2) act with prudence in deciding whether and how to delegate authority and in the selection and supervision of agents (§171); and

(3) incur only costs that are reasonable in amount and appropriate to the investment responsibilities of the trusteeship (§188).



(d) The trustee's duties under this Section are subject to the rule of §228, dealing primarily with contrary investment provisions of the trust or statute.

#### **§228 – Investment Provisions of Statute or Trust**

In investing the funds of the trust, the trustee

(a) has a duty to the beneficiaries to conform to any applicable statutory provisions governing investment by trustees; and

(b) has the powers expressly or impliedly granted by the terms of the trust and, except as provided in §§ 165 through 168, has a duty to the beneficiaries to conform to the terms of the trust directing or restricting investments by the trustee.

#### **§229 – Duty with Respect to Original Investments**

The trustee is under a duty to the beneficiaries, within a reasonable time after the creation of the trust, to review the contents of the trust estate and to make and implement decisions concerning the retention and disposition of original investments in order to conform to the requirements of §§ 227 and 228.

On the heels of the Third Restatement came the Prudent Investor Act, adopted by the National Commissioners of Uniform State Laws on August 5, 1994. Together these uniform laws set forth a significant departure from prior law. First, the trustee must now judge the performance of the portfolio as a whole, considering an "overall investment strategy" with reasonable risk and return objectives. Second, the duty to diversify is clearly stated. Third, delegation of investment function is specifically allowed, thus encouraging the retention of professional managers. This shift toward professional management of the portfolio as a whole,

with a view toward increasing returns and lowering risks through meticulous asset allocation, is at the heart of modern portfolio theory. Robert Wolf has summarized this point:

Looking at a particular investment as it relates to an entire portfolio, as it may increase return or decrease risk to the portfolio, is a function of what is called modern portfolio theory, developed in part as a result of significant mathematical analysis and academic research. Fiduciary law, on the other hand, has focused historically on each investment being judged by itself, rather than within the context of a portfolio. Was it of sufficient quality for use in a fiduciary portfolio? Has specific research been done on the fundamentals of the company? Could it stand the test of prudence? In the investment world today, each investment is judged in the context of how it affects the risk and return of the portfolio as a whole.

Because individually risky investments may in combination actually lower the overall risk of a portfolio, one can increase return or decrease risk without having to "pay" for it in overall portfolio performance. This is so because many investments show a negative covariance, that is, when one goes down, the other goes up, or at least does not go down. Combining assets that perform differently over time, such as bonds and stocks, or diversified individual stocks within a portfolio, actually eliminates much of the company specific risk associated with security selection.<sup>10</sup>

#### **C. Kentucky's Prudent Investor Rule – KRS 287.277**

In 1996, the General Assembly passed KRS 287.277 and adopted the Prudent Investor Rule for *banks only* as follows:

##### **KRS 287.277 Standards for Bank or Trust Company acting as Fiduciary.**

- (1) Notwithstanding the provisions of any other law, a bank empowered to act as a fiduciary or trust company, when investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing property held in a fiduciary capacity, shall act as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the fiduciary account.
- (2) The standard described in subsection (1) of this section requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the account portfolio and as part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the account.

- (3) In making and implementing investment decisions, the bank or trust company has a duty to diversify the investments of the account unless, under the circumstances, it is prudent not to do so.
- (4) In addition, the bank or trust company shall:
  - (a) Conform to fundamental fiduciary duties of loyalty and impartiality;
  - (b) Act with prudence in deciding whether and how to delegate authority and in the selection and supervision of agents; and
  - (c) Incur only costs that are reasonable in amount and appropriate to the investment responsibilities of the account.
- (5) The duties of the bank or trust company under this section are subject to the rule that in investing the funds of the account, the bank or trust company:
  - (a) Has a duty to the beneficiaries of the account to conform to any applicable statutory provisions governing investment by fiduciaries; and
  - (b) Has the power expressly or impliedly granted by the terms of the account or applicable instrument and has a duty to the beneficiaries of the account to conform to the terms of the account directing or restricting investments by the bank or trust company.

Thus now Kentucky finds itself in the odd dilemma of imposing different standards on the corporate trustee and the individual trustee. This fact must be carefully considered by the trusts and estates practitioner. The trust grantor must be informed about these varying standards so that he or she may opt in or out of the Prudent Investor Rule as dictated by the circumstances of the trust and the grantor's own views toward fiduciary investing.

#### **D. Kentucky's Revised Uniform Principal and Income Act (1962)**

Kentucky adopted the 1962 Revised Uniform Principal and Income Act in 1992. This Act requires a trust to be administered with due regard to the interests of income beneficiaries

and remaindermen and reinforces the Prudent Man Rule in KRS 386.195. More importantly, the Act establishes a clear distinction between principal and income:

KRS 386.205 Definition of Income and Principal.

- (1) Income shall mean the return in money or property derived from the use of principal, including return received as:
  - (a) Rent of real or personal property, . . .
  - (b) Interest on money lent, . . .
  - (d) Corporate [cash dividends],
  - (e) Accrued increment on bonds or other obligations issued at discount, . . .
  - (f) Receipts from business and farming operations, . . .
- (2) Principal shall mean the property which has been set aside by the owner or the person legally empowered so that it is held in trust eventually to be delivered to a remainderman while the return or use of the principal is in the meantime taken or received by or held for accumulation for an income beneficiary. Principal shall include:
  - (a) Consideration received by the trustee on the sale or other transfer of principal or on repayment of a loan or as a refund or replacement or change in the form of principal;

A Kentucky trustee is thus bound by this statutory definition of “income” as meaning “return from the use of principal,” not realization of the appreciation of principal. The statute specifically categorizes capital gain as principal. Absent trust terms to the contrary, the Kentucky trustee cannot allocate realized gains to the income beneficiary or retain in principal the interest and dividend yields, regardless of the desires of the respective beneficiaries or the trustee’s perceptions of fairness and impartiality. Note that this is true for the individual trustee and the corporate trustee. Notwithstanding the corporate trustee’s statutory duty to invest as a prudent investor, viewing investments not in isolation but in the context of the portfolio as a

whole, the corporate trustee must by necessity view each investment in isolation to determine accounting income – and thus the distribution to the income beneficiary – under current Kentucky law.

**E. The Revised Uniform Principal and Income Act (1997)**

The Revised Uniform Principal and Income Act as promulgated by the Commissioners of Uniform State Laws was adopted on August 1, 1997. This new uniform Act softens the distinction between principal and income and gives the trustee new flexibility. Section 104(a) provides this unprecedented power:

A trustee may adjust between principal and income to the extent the trustee considers necessary if the trustee invests and manages the trust assets as a prudent investor, the terms of the trust describe the amount that may or must be distributed to a beneficiary by referring to the trust's income, and the trustee determines, after applying the rules in Section 103(a), that the trustee is unable to comply with Section 103(b).

Section 103(b) in essence requires the trustee to act impartially based on what is fair and reasonable to all beneficiaries, unless the trust terms clearly manifest an intention that the fiduciary shall favor one or more beneficiaries.

This new uniform law is a clear response to the demands of modern investment theory and the Prudent Investor Rule. In the comments to Section 104, this statement is found:

Section 104 does not empower a trustee to increase or decrease the degree of beneficial enjoyment to which a beneficiary is entitled under the terms of the trust; rather, it authorizes the trustee to make adjustments between principal and income that may be necessary if the income component of a portfolio's total return is too small or too large because of investment decisions made by the trustee under the prudent investor rule.” (Emphasis added.)

## **F. KBA Probate Section Proposed Legislation (2002)**

### **(1) The Kentucky Uniform Prudent Investor Act**

The Legislative Committee of the Kentucky Bar Association's Probate Section proposed legislation in the 2002 General Assembly to adopt the Prudent Investor Rule for all Kentucky fiduciaries and clarify numerous pertinent and related issues. The legislation was not introduced to committee.

### **(2) The Kentucky Uniform Principal and Income Act**

The Legislative Committee also proposed legislation in 2002 to adopt the 1997 Uniform Principal and Income Act. Among the many provisions of this legislation, "income" would have been redefined as follows: "Income means money or property that a fiduciary receives as current return from a principal asset. The term includes a portion of receipts from a sale, exchange, or liquidation of a principal asset, . . ." The Section 104 "power to adjust" would have been granted to all trustees acting as prudent investors. This legislation also was not introduced to committee.

## **4. Guidance from the Nonprofit Sector**

The long-term character of nonprofit endowment funds led charitable institutions to embrace total return investing decades ago.<sup>11</sup> Long abandoned are the artificial income and principal distinctions that endowment managers once espoused. Unlike the private trust where the expectations of separate beneficiaries promote competing allegiances, the endowment fund is committed to the success of only one charity. Competition is found merely with the internal management of cash flow expectations of the institution. Although not insignificant, such competition is intramural, i.e., the risk of private litigation – although not absent – is very low. Therefore, endowment managers are more likely to look to the total return of the fund, not merely to the interest or dividend yield of any given investment, for the reasonable cash flow

needs of the charity. Realizing capital gains in the tax-exempt arena to fund current operations, within the parameters of a carefully formulated and monitored investment policy giving high regard to reasonable risks, has become the standard for endowment management.

In 1972, the Uniform Management of Institutional Funds Act was promulgated by the Commission of Uniform State Laws. Kentucky adopted the Act in 1976 at KRS 273.510 – 273.590. The Act provides for use of net appreciation of endowed funds as long as a plan is established based on certain standards:

**KRS 273.520 Appropriation of Net Appreciation.**

The governing board may appropriate for expenditure for the uses and purposes for which an endowment fund is established so much of the net appreciation, realized and unrealized, in the fair value of the assets of an endowment fund over the historic dollar value of the fund as is prudent under the standard established by KRS 273.560. This section does not limit the authority of the governing board to expend funds as permitted under other law, the terms of the applicable gift instrument, or the charter of the institution.

Broad investment authority is granted in KRS 273.540. Current return is not required. Specific authority is given to delegate investment decisionmaking. Because endowments have similar goals with most private trusts (stable flow of real income, no erosion of purchasing power and growth of underlying assets)<sup>12</sup> the policies of total return investing in endowment funds – and the success thereof – provide an attractive model for the trusts and estates practitioner.

**5. Alternatives to the Income Rule Trust**

The “net income” or “income rule” trust, although commonly employed, often fails the expectations of all parties involved. Without deliberate drafting to grant an individual trustee the power to invest for total return, the trustee is compelled to analyze the income yield of each investment in an attempt to provide the life beneficiary with a reasonable return. This approach will certainly not appeal to most remaindermen. Furthermore, even if the trustee is authorized to

invest for total return, a “net income” directive in the trust agreement locks the trustee out of a large segment of the investment markets. Kentucky’s statutory definition of “income” does not allow allocation of capital gains to the income beneficiary. Therefore, pending legislative initiatives, drafting alternatives are needed that take into account changing economic conditions and the needs of all parties involved – income beneficiary, remaindermen and trustee.

#### **A. Discretionary Trusts**

The fully discretionary trust gives broad and complete discretion to the trustee in order to provide distributions of both income and principal. Distribution standards may be employed to guide the trustee, and such standards may be very broad (third party trustees) or ascertainable standards (interested party trustees). A fully discretionary trust, in this context, would allow the trustee to invest for a total return and then exercise discretion in distributing a fair and reasonable return to the current beneficiary. However, the fully discretionary trust has two significant drawbacks. First, the trustee is expected to exercise significant power with little or no direction. Second, the beneficiaries have no framework within which to build expectations.<sup>13</sup> Any trustee action to distribute corpus may be subject to scrutiny, or at best, to ongoing suspicions of all beneficiaries. While these concerns may be lessened if the parties are related, the independent corporate trustee usually finds the fully discretionary trust less than desirable.

#### **B. Inflation Adjustment Trusts**

Some propose the use of an “Indexed Payment Trust,” applying external variables such as the Consumer Price Index to account for inflation and keep real economic substance behind the income beneficiary’s distributions. However, these trusts have been criticized because the variable (inflation) is not necessarily correlated with the return and may even be inversely correlated to return.<sup>14</sup> In times of high inflation, which may cause significant increases to the



income distribution, the stock and bond markets are often adversely effected. This may require liquidation of assets at low prices with a poor dollar-cost averaging affect, which may have a negative effect on the long-term success of the trust, not to mention the relationship between the trustee and the remaindermen. This result would be avoided only by requiring that the income distribution be set at a low initial level to be safe. This would likely frustrate the income beneficiary.

### **C. Total Return Unitrust**

The use of the term “total return trust” often implies the use of a private unitrust with total return investment powers. This variation of the charitable unitrust is popular for the same reason the CRUT is popular: certainty of distributions. By setting a specific percentage to be paid to the life beneficiary each year, the grantor creates in effect a trust partnership between the current beneficiary, the remaindermen and the trustee.<sup>15</sup> All parties know exactly what the first year’s distribution will be, thus the relationship with the trustee starts off on a good foot. The mere existence of clear and attainable expectations removes the suspicion and tension often facing trustees, especially in the long-term trust relationship with a beneficiary having no prior trust experience.

The total return unitrust allows the trustee to invest freely in any asset and pay the required distribution amount from any source. Artificial distinctions between income and principal are discarded, and all parties benefit from increases in the value of the total trust portfolio. The trustee’s duty to treat all beneficiaries impartially is thus met, and negative tensions are reduced. No balancing of interests – which in reality can disappoint all beneficiaries – is required.

The key point in drafting the total return trust is the distribution payment clause. It is at this point that the analogy with the CRUT stops. To qualify as a CRUT, the trust agreement must establish a fixed unitrust payment that allows computation of the present value of the charitable remainder interest to determine the grantor's income and gift tax charitable deduction. However, the establishment of a fixed, inflexible pay-out rule in the total return trust is inappropriate. The problem is evident in two areas:

(1) Adjustments for Market Swings. As recently demonstrated, the stock market does not always track on a graph to the right and higher. On a historical basis, the implementation of a single pay-out rate would result in significant and numerous declines in annual payments to the current beneficiary. As noted by Mr. Wolf, a 5% payout on an S&P 500 portfolio over a 71-year period starting in 1926 would have resulted in decreased distributions in 23 of those 71 years, with 14 years of decreases exceeding 10%. Although the trust corpus would have increased to an impressive \$4,800,464, such volatility in current beneficiary distributions would undoubtedly put a strain on the "trust partnership" aspects of the total return trust.<sup>16</sup> Therefore, "smoothing rules" have been developed as a direct derivation of the "spending rules" that are common in nonprofit endowment funds. The "smoothing rule" provides for distributions to be calculated on a rolling quarterly average – usually no less than twelve quarters. The results are significant. Again citing Wolf's example of a 71-year S&P 500 portfolio starting in 1926, the employment of a three-year rolling average in calculating distributions results in a higher corpus value (\$5,217,253) and a reduction of decreases in annual distributions (13 rather than 23), with only a few of those exceeding 10% (7 rather than 14).<sup>17</sup> Certainly the down markets of 2000-2002 would result in decreases, but the three-year rolling

average would incorporate the significant upswings of the late 1990's, again illustrating the necessity of carefully computing the payout rate.

(2) Alteration of Distribution Formula. Even more critical than the averaging of returns is the incorporation of a mechanism for the distribution formula to be altered. Although attractive in many ways, total return trusts do not have the "safety net" of the income rule trust: conservative, forced preservation of capital.<sup>18</sup> Without careful consideration of the economic circumstances and the resulting investment portfolio decisions that must be made, along with careful consideration of costs,<sup>19</sup> the total return philosophy can be dangerous. A detailed investment strategy must be developed and followed. As stated by one recent commentator:

Recently published research indicates that designing and implementing an automatic-pilot distribution formula that works irrevocably and unchangingly over the broad range of possible future economic conditions is an invitation to a financial catastrophe. The settlor, through the drafting attorney, can (should!) give the trustee clear guidelines to follow. These guidelines, however, should not be set in stone. . . . As the inflation-adjusted dollar value of the portfolio changes from year to year, the trustee needs the flexibility to adjust distribution policy so that it remains suitable for the economic conditions of the trust. This requires the estate and trust attorney to draft guidelines rather than irrevocable distribution formulae.<sup>20</sup>

Note the "adjustment" language of the 1997 Revised Uniform Principal and Income Act cited above. The trustee may, in effect, alter the distribution scheme as needed to accomplish the terms of the trust and be fair and reasonable to all beneficiaries. Absent is any hint of a specific percentage or formula. Such discretion puts significant pressure on the trustee to monitor not only the assets of the trust but the distribution scheme as well. Highly advanced statistical support may become the standard. Again quoting Collins:

With respect to trustee administration, the real focus in a total return trust shifts from asset allocation to distribution policy and, ultimately, to portfolio sufficiency monitoring. . . . The promise of the total return trust is that, if designed,

implemented and administered correctly, it significantly increases the chances of a successful outcome for all interested parties. The pitfall of a total return trust is that, absent adequate information technologies, fiduciaries may unwittingly put the portfolio on a path towards oblivion.<sup>21</sup>

Query: Considering these ominous warnings, is the total return trust with a distribution alteration provision anything more than a glorified fully discretionary trust?

To bring more certainty to the trustee, many states are considering a statutory unitrust concept alternative.<sup>22</sup> In 2001, New York adopted its version of the Revised Uniform Principal and Income Act, which sets forth both a trustee adjustment power and an alternative 4% unitrust scheme.<sup>23</sup> Although attractive for its certainty, a trustee power to alter the unitrust amount – a prudent part of any total return trust – still burdens the trustee with significant discretionary responsibility in the face of changing economic conditions. As noted above, the trustee must possess adequate skill and technology to make such decisions. Collins and Stampfli, statisticians who provide support services to trustees, sum up the problem this way:

Commercial fiduciaries should not provide investment services to total return trusts if they do not possess adequate technology. . . . The viability of these trusts depends on interactions of multiple variables within an interactively complex system. Decisions of seemingly small significance may, in fact, generate both extreme and unexpected future results of affects compound over time.<sup>24</sup>

The required degree of trustee flexibility and other critical elements of the total return trust are illustrated in the sample trust agreement attached hereto. This sample trust is the work-product of attorney Robert B. Wolf. It was originally published in Real Property, Probate and Trust Journal, Summer 2001, and is reprinted with the express, written permission of Mr. Wolf.

## **6. Tax Implications of Total Return Trusts**

The total return trust has a number of serious tax implications that must be thoroughly considered by the practitioner. Recent proposed regulations to portions of the fiduciary income tax and GST sections of the Code have a substantial impact on this analysis and must be studied

carefully. Three important concepts will be mentioned here briefly to highlight the nature of these tax concerns; however, it is essential for the practitioner to digest the most current tax materials and their ramifications prior to embarking on any preparation of total return trusts.

#### **A. Marital Deduction Trusts**

The practitioner will note that one of the keys of the total return trust is the fundamental alteration of the traditional concept of income. Whether such change is stated in terms of a unitrust scheme or a trustee's "power to adjust," the essence of the total return trust is to shift the focus from return on principal to a return of principal if necessary for the reasonable treatment of all beneficiaries. Realization of capital gain for distribution to the income beneficiary raises a substantial and pertinent question in the context of the marital trust: Will the unitrust interest or an income interest subject to the power to adjust qualify for the marital deduction?<sup>25</sup>

Early proponents of the total return trust cautioned that the careful practitioner must provide for a payout of a unitrust amount or the traditional net income of the trust, whichever is greater, at least annually, in order to secure the marital deduction.<sup>26</sup> However, the Proposed Regulations to Section 643(b) would change the definition of "income" with an obvious view toward accommodating the total return trust:

Trust provisions that depart fundamentally from traditional principles of income and principal, that is, allocating ordinary income to income and capital gains to principal, would generally not be recognized. However, amounts allocated between income and principal pursuant to applicable local law will be respected if local law provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust for the year including ordinary income, capital gains, and appreciation. For example, state law that provides for the income beneficiary to receive each year a unitrust amount of between three percent and five percent of the annual fair market value of the trust assets is a reasonable apportionment of the total return of the trust. Similarly, a state law that permits the trustee to make equitable adjustments between income and principal to fulfill the trustee's duty of impartiality between the income and remainder beneficiaries is generally a reasonable apportionment of the total return of the trust. These adjustments are permitted when the trustee invests and

manages the trust assets under the state's prudent investor standard, the trust describes the amount that shall or must be distributed to a beneficiary by referring to the trust's income; and the trustee after applying the state statutory rules regarding allocation of income and principal is unable to administer the trust impartially.<sup>27</sup>

The Proposed Regulations thus authorize a QTIP trust with a unitrust scheme or a power to adjust provision and clarify that such a provision will not constitute the appointment of trust property to any person other than a surviving spouse.<sup>28</sup> However, it is critical for the Kentucky practitioner to note that this change is allowed in the Proposed Regulations only if state law has been adopted to alter the traditional meaning of income. In other words, the adoption of a total return unitrust scheme or power to adjust in the trust agreement alone is not sufficient at this time to qualify for the marital deduction. State law must provide the "requisite support."<sup>29</sup> Therefore, the Kentucky practitioner must at this time continue to include the "greater of" a unitrust amount or traditional net accounting income payable to the surviving spouse. The independent trustee may be given a power to reform the trust to eliminate the "greater of" language if Kentucky were to adopt a statute that authorizes a reasonable apportionment of the total return of the trust to the income beneficiary. See the sample trust agreement below for further language about the QTIP trust and a power to reform.

#### **B. Taxation of Capital Gains**

The Proposed Regulations also address the important question of whether capital gains allocated to the income beneficiary are carried out in DNI. This important concept has a direct impact on the ultimate return of the trust: If capital gains are taxed to the trust itself, the remaindermen are bearing the tax burdens of the income beneficiary, a result that may hinder the partnership aspect of the total return trust. The supplementary information accompanying the Proposed Regulations states as follows:

The provisions of Section 643(b) and 643(a)(3) are further intertwined when consideration is given to the new state statutory provisions defining income. If, under the terms of the governing instrument or applicable local law, realized capital gains are treated as income to the extent the unitrust amount or the equitable adjustment amount exceeds ordinary income, capital gains so treated are included in distributable net income. A similar result is achieved for capital gains consistently allocated to income by the fiduciary pursuant to a discretionary power. In any other situation, the capital gains will be excluded from distributable net income and will be taxed to the trust.<sup>30</sup>

The Proposed Regulations set forth a number of examples to illustrate the application of this rule. It is clear that an ordering rule similar to that used by the charitable remainder trust is approved under the Proposed Regulations.<sup>31</sup>

### **C. GST Trusts**

A point of great concern is whether a grandfathered GST Trust may be modified from an income rule trust to a total return trust without losing GST exempt status. In the past, private letter rulings were the norm to address this critical question. However, final regulations were issued in December 2000 to address a number of critical GST questions including reformation to a total return trust. The final regulations contain an example illustrating the consequences of a judicial modification of a grandfathered trust allowing allocation of capital gains to the income beneficiary. The modification is approved in the example.<sup>32</sup> However, the new Proposed Regulations on the definition of net income raise additional concerns about the shifting of beneficial interest as follows:

[A]dministration of a trust in conformance with applicable state law that defines the term income as a unitrust amount, or permits the trustee to adjust between principal and income to fulfill the trustee's duty of impartiality between income and principal beneficiaries, will not be considered to shift a beneficial interest in the trust, if the state statute provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust and meets the requirements of §1.643(b)-1 of this chapter.<sup>33</sup>

Mr. Wolf warns that this provision confirms that a reformation of a GST Trust from an income rule trust to a total return trust is allowable for GST grandfathering purposes only if supported by the requisite state statutes. As noted above, Kentucky has not passed the applicable statutes. Therefore, the Kentucky practitioner must retain a “whichever is greater” approach to the payment of a unitrust amount or traditional net accounting income until further legislation is passed.<sup>34</sup>

#### **D. Tax Summary**

The addition of the §643 Proposed Regulations on the definition of income clearly favors those states that are moving forward with the adoption of total return trust statutes. In fact, in an unusual turn of events, the actions of the Treasury have been the driving force in state law changes, providing specific guidance about the income tax ramifications of legislative proposals. However, this progressive trend is not yet found in Kentucky trust law. Therefore, the Kentucky practitioner must exercise particular care in implementing the total return trust and fully analyze current tax law prior to drafting the total return trust.

#### **7. Conclusion**

The total return trust is designed to incorporate modern trust investment theory, focusing on a total portfolio and its total return, both earnings and appreciation, rather than focusing on each individual investment to determine suitability. By so doing, the trustee is emphasizing overall growth to the benefit of all beneficiaries, current and remainderman, thus forging a partnership where the expectations of each party are more clearly determinable. By carefully formulating a distribution scheme with the proper mix of certainty and flexibility, the practitioner may employ the total return trust to maximize the economic power of the trust over long durations to the benefit of all parties involved.



## NOTES

- 
- <sup>1</sup> Wolf, Robert B., "Defeating the Duty to Disappoint Equally – The Total Return Trust," 32 Real Prop. Prob. & Tr. J. 45 (1997) ("Wolf I").
- <sup>2</sup> 11 S.W. 767 (Ky. 1889).
- <sup>3</sup> Id. at 768.
- <sup>4</sup> See Bryan v. Security Trust Co., 176 S.W.2d 104, 110 (Ky. 1943).
- <sup>5</sup> See Fidelity T.&S.V. Co. v. Glover, 14 S.W. 343 (Ky. 1890) (discussion of recently enacted statute).
- <sup>6</sup> See Security Trust Co. v. Appleton, 197 S.W.2d 70 (Ky. 1946) (noting that lack of uniform sentiment about diversification among financial authorities would render a judicial decision in favor of requiring diversification an "ultra-hazardous undertaking").
- <sup>7</sup> Rest. 3<sup>rd</sup>, Trusts (Prudent Investor Rule) Introduction.
- <sup>8</sup> Id.
- <sup>9</sup> Id.
- <sup>10</sup> Wolf I, supra, at 56-57.
- <sup>11</sup> Id. at 60.
- <sup>12</sup> Id. at 61.
- <sup>13</sup> Id. at 72-73.
- <sup>14</sup> Id. at 73.
- <sup>15</sup> Id. at 74.
- <sup>16</sup> Id. at 75.
- <sup>17</sup> Id. at 76.
- <sup>18</sup> Patrick J. Collins and Josh Stampfli, "Promises and Pitfalls of Total Return Trusts," 27 ACTEC J. 208 (2001).
- <sup>19</sup> See generally, Robert B. Wolf, "Total Return Trusts: Can Your Client Afford Anything Less?" 33 Real Prop., Prob. & Tr. J. 131 (1998).
- <sup>20</sup> Collins, supra, at 211.
- <sup>21</sup> Collins, supra, at 211, 218.
- <sup>22</sup> See Lyman W. Welch, "Progress of Total Return Legislation," 139 Tr. & Est. 12, 14 (2001).
- <sup>23</sup> Robert B. Wolf, "Estate Planning with Total Return Trusts: Meeting Human and Investment Goals through Modern Trust Design," 36 Real Prop. Prob. & Tr. J. 169, 178-181 (2001) ("Wolf II").
- <sup>24</sup> Collins, supra, at 218.
- <sup>25</sup> Wolf II, supra, at 189.
- <sup>26</sup> Wolf I, supra, at 83-84.
- <sup>27</sup> Prop. Reg. §1.643(b)-1.
- <sup>28</sup> Howell-Smith, Laura, "How Prop. Regs. on the Definition of Income Affect Total Return Trusts," 28 Est. Pl. 308, 312 (2001).
- <sup>29</sup> Wolf, supra, at 192.
- <sup>30</sup> REG-106513-00, 66 F.R. 10396-10400 (2/15/01).
- <sup>31</sup> Wolf, supra, at 194. See the attached sample trust form for example of the ordering rule language.
- <sup>32</sup> Howell-Smith, supra, at 314.
- <sup>33</sup> Prop. Reg. §26.2601-1(b)(4)(i)(D)(2).
- <sup>34</sup> Wolf, supra, at 197; see also, Howell-Smith, supra, at 315.

## SAMPLE TOTAL RETURN UNITRUST

I give the residue of my estate to my trustee to hold as a Total Return Unitrust under the following provisions:

A. **During** \_\_\_\_\_ **life**. My trustee shall pay the distribution amount set forth below to or for the benefit of my \_\_\_\_\_ during h \_\_\_\_\_ life, in quarter-annual installments.

B. **Distribution amount**. The trustee shall pay to my \_\_\_\_\_ in each tax year of this trust during h \_\_\_\_\_ life an amount equal to \_\_\_\_\_ (\_\_\_\_%) percent of the average of the fair market values of the trust as of the close of the last business day of the trust's three previous tax years (or such lesser number of tax years as are available for the first three tax years of the trust) (the "distribution amount"). In the case of a short tax year, the distribution amount shall be calculated as set forth in subparagraph C below. In the case of contributions to or distributions from the trust, including initial funding, the distribution amount shall be determined as set forth in subparagraph D below. **[Non-accrual alternative: The obligation to pay the distribution amount shall cease with the last regular payment before my \_\_\_\_\_ death.]**

C. **Short year**. For a short tax year, **[including the year of a beneficiary's death]** the distribution amount shall be based upon a prorated portion of the distribution amount set forth above, comparing the number of days in the short tax year to the number of days in the calendar year of which the short tax year is a part. **[Note: This accrual may be helpful in securing "present interest" status for the annual gift tax exclusion, if that is important.]**

D. **Contributions and Distributions**. In a tax year in which assets are added to or distributed from the trust (other than the distribution amount) (hereinafter "adjustment year"), the distribution amount shall be increased (in the case of a contribution) or decreased (in the case of a distribution) by an amount equal to \_\_\_\_\_ (\_\_\_\_%) percent times the fair market value of the assets contributed or distributed (as of the date or dates of the contribution or distribution), multiplied by a fraction, the numerator of which is the number of days from the contribution or distribution to the end of the calendar year, and the denominator of which is the days in the calendar year. Further, the year end values for the two tax years preceding the adjustment year shall be increased by the amount of such addition, or decreased by the amount of such distribution, for purposes of determining the distribution amount for years following the adjustment year. **[This complicated language is needed to accommodate multi-year funding of trusts from estates and discretionary distributions in light of the three-year smoothing rule.]**

E. **[Insert for QTIP, if your state does not have a statutory unitrust option so as to validate a unitrust payout for marital deduction purposes under the Proposed Regulations. If your state is a unitrust state, you may delete and re-letter subparagraphs once the regulations are final and in effect.]** If in any trust the net income of the trust exceeds the unitrust amount, such excess net income shall be distributed to my \_\_\_\_\_ at least annually.

F. **Computing Fair Market Value.** All computations of the trust's fair market value, or the value of any contributions or distributions as set forth above, shall include accounting income and principal, but no accruals shall be required. If the trust includes assets for which there is not a ready market, the trustee shall adopt such method of valuation as the trustee deems reasonable in its discretion under the circumstances. **[This allows a closely-held business interest or real estate to be placed in the trust, but the total return trust is cumbersome for this type of asset.]**

G. **Income earned in estate prior to trust funding.** In addition to the distribution amount as determined above, the net accounting income earned in my estate and allocable to the residue shall be paid to the trust, and distributed to my \_\_\_\_\_.

H. **Source of distribution amounts.** The distribution amounts from the trust shall be paid from net accounting income. If the net accounting income is insufficient to satisfy the distribution amount, the trustees shall allocate to income such net realized short-term capital gains as are needed to satisfy the distribution amount, and if still insufficient, the trustees shall allocate to income such net realized long-term capital gains as are needed to satisfy the distribution amount. If, after allocating said short-term and long-term capital gains to income, the income is still insufficient to pay the distribution amount, the balance needed shall be paid from the principal of the trust.

**[If your state has a statutory unitrust with the foregoing ordering rule, it is clear under Prop. Reg. § 1.643(e), Example 9, that the ordering rule will be respected once the Regulations are final. It is likely that if the foregoing ordering rule is in the governing instrument, rather than being a default provision in your state law, it will also be respected, provided that the ordering rule is not inconsistent with your state law. If this were not the case, computer modeling suggests that the payout rate should be lowered .25% to .35% to have a roughly equivalent possibility of preserving the value of the trust after the effect of taxes, expenses and inflation, assuming the trust has a portfolio with a current or stepped up cost basis, and perhaps twice that amount, or .50% to .70% for a trust with an extremely low cost basis portfolio.]**

I. **Discretionary distributions of additional amounts.** In addition to the distribution amounts as set forth above, my trustee shall distribute such additional amounts, if any, of accounting income, capital gain or principal to my said \_\_\_\_\_ as the trustee deems advisable for my \_\_\_\_\_'s health, maintenance and support in h\_\_\_\_\_ accustomed standard of living, taking into account other income or assets which are available to h\_\_\_\_\_. **[Comment: Discretionary distributions may be advisable for the same reasons as they are in any trust. Consider giving an independent trustee broader powers to enable beneficiary "to make estate planning gifts," "for \_\_\_\_\_ welfare" or "for any purpose in which money is needed."]**

J. **Death of \_\_\_\_\_.** On the death of my \_\_\_\_\_, the trustee shall **[pay any accrued distribution amount to my \_\_\_\_\_'s personal representative, and]** distribute

the balance in said trust to my then living issue, per stirpes, subject to the Trust Continuation Provisions hereinafter.

K. **Goal of trust [Optional: and Corporate Trustee's Power to Alter Distribution Rate.]** The goal of this trust is to provide an adequate and a relatively smooth flow of distributions, which distributions over the anticipated term of the trust may to the extent possible maintain or increase their real spending power after inflation. A second and related goal is to maintain or increase the real spending power of the trust both for the long term benefit of my \_\_\_\_\_ and also for the benefit of the remaindermen. It is my intent by using a Total Return Unitrust, which is designed to invest for total return, whether produced by accounting income, short-term or long-term capital gains, to eliminate any conflict the trustee might otherwise experience between attaining the two goals set forth above. The distribution rate has been set at \_\_\_\_\_ (\_\_\_\_%) percent based upon an expectation that over long periods of time, this distribution rate can be maintained and still have the distributions increase to **[partially] offset [or more than offset] inflation. [Optional: If 3% or less. If a higher rate is used, use "to offset inflation as much as possible."]** If this goal is achieved, the trust estate will also have maintained **[or increased] [Optional: If 3% or less]** its real value after inflation. **[Make sure the goals are practical given the rate you insert. It is not a fair goal to expect a real increase after inflation if you insert a rate of 5% or more.]** These goals will not be attainable every year, but will hopefully be attained over the long term. I understand that to the extent discretionary distributions are made in addition to the distribution amount that these economic goals will be compromised. Nevertheless, the corporate trustee shall not be liable for its good faith exercise of judgment in distributing such funds.

**[Optional: In making a determination concerning discretionary distributions in addition to the distribution amount, my corporate trustee/trustee\_\_\_\_ may wish to take into account that the welfare and support of my \_\_\_\_\_ is the most important goal of these trusts, with the preservation and building of wealth for the next generation of secondary importance.]**

**[Optional: If, as a result of permanent, substantial, and fundamental changes in the investment marketplace, the corporate trustee, acting alone, becomes convinced that the goals of the trust as set forth above cannot be attained because of the specific percentage distribution rates used for the distribution amount, the corporate trustee shall have the discretion to change such rates. The foregoing is intended to provide flexibility to the corporate trustee only in the event of extraordinary and unforeseen change in the investment marketplace from those markets experienced during the 20th Century. The corporate trustee shall not be held liable for the good faith exercise or non-exercise of this power.]**

**[Comment: Because the modeling of these trusts demonstrates that they work well and predictably for the periods 1926-1998, 1960-1998 and 1973-1998, it is not clear that this discretion is needed, or even wise. It may, however, give clients an added level of comfort – no small thing.]**

2. **Executors' and trustees' powers.** In addition to the powers conferred by law, my execut \_\_\_\_\_ with respect to my estate, and my trustee, with respect to any trust, shall have the following powers, to be exercised in their absolute discretion, without the necessity of application to any Court, in the capacity to which such powers may be applicable: **[Optional: except that they shall have no power as to the Marital Trust which would disqualify it for purposes of the marital deduction]**

**[Customary Provisions Omitted]**

B. **Investments.** To invest in any type of investment that plays an appropriate role in achieving the investment goals of the trust, which investment shall be considered as part of the total portfolio. It is my specific direction that no category or type of investment shall be prohibited. I specifically do not wish to limit the universe of trust investments in any way other than is dictated by the trustee's exercise of reasonable care, skill, and caution. In connection with the trustee's investment and management decisions with respect to this trust, the trustee is specifically entitled to take into account general economic conditions, the possible effect of inflation or deflation, the expected tax consequences of investment decisions or strategies, the role that each investment or course of action may play within the overall trust portfolio that may include financial assets, interests in closely-held enterprises, **[Note – consider valuation problems here]** tangible and intangible personal property, and real property; **[Note – valuation problem]** the expected total return from income and the appreciation of capital; other resources of the beneficiaries, the needs for liquidity, regularity of income and preservation or appreciation of capital, and the asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries. Nor shall my trustee be limited to any one investment strategy or theory, including modern portfolio theory, the efficient markets theory or otherwise, but should be free to consider any appropriate investment strategy or theory under all the circumstances. **[Insert for QTIP if your state does not have a statutory unitrust: Should the trustee invest in property which is unproductive, my spouse shall have the right to require the trustee to convert the same into productive property within a reasonable time.]** **[Consider provisions for personal use property such as residential real estate or tangible personal property. If such property is contemplated, it should not be included in the market value of the trust for determining the distribution.]**

C. **Delegation.** The trustee may delegate investment and management functions that a prudent person of comparable skills would properly delegate under the circumstances. Should the trustee delegate such function, the trustee shall exercise reasonable care, skill, and caution in selecting an agent, establishing the scope and terms of the delegation consistent with the purposes and terms of the trust, and periodically reviewing the agent's actions in order to monitor performance and compliance with the terms of the delegation. Should such delegation occur as set forth above, the trustee that complies with the requirements for delegation shall not be liable to the beneficiaries or to the trusts for the decisions and actions of the agent to which the function was delegated, but by accepting the delegation of a trust function by the trustee of this trust, the agent submits to the jurisdiction of the courts of this state. **[Most of this paragraph is imported from the Uniform Prudent Investor Act.]**

I. **Reformation**. The corporate trustee, acting alone and in its sole discretion, shall have the power to reform this instrument, with or without Order of Court, in order to make any changes necessary so as to preserve and make the best use of the marital deduction for federal estate tax purposes, the exemption from generation-skipping transfer tax, or to carry out my intent regarding the allocation of capital gains to income as prescribed in this will. Any provisions of this will shall be interpreted or reformed so as to preserve these benefits and carry out my intent wherever possible, provided that such interpretation or reformation does not do violence to my primary intent to provide for my spouse and my children.

Copyright 2000 by Robert B. Wolf.

Republished by express, written permission of Mr. Wolf.



## BIBLIOGRAPHY

Bendremer, Fredric J., "Modern Portfolio Theory and International Investments Under the Uniform Prudent Investor Act," Real Property, Probate and Trust Journal, Vol. 35, No. 2, Winter 2001.

Cline, Christopher P., and Marcia L. Jory, "The Uniform Prudent Investor Act: Trust Drafting and Administration," Estate Planning, Vol. 26, No. 10, December 1999.

Collins, Patrick J., and Josh Stampfli, "Promises and Pitfalls of Total Return Trusts," ACTEC Journal, Vol. 27, No. 3, Winter 2001.

Collins, Patrick J., Sam L. Savage and Josh Stampfli, "Financial Consequences of Distribution Elections From Total Return Trusts," Real Property, Probate and Trust Journal, Vol. 35, No. 2, Summer 2000.

Horn, Jerold I., "Prudent Investor Rule, Modern Portfolio Theory, and Private Trusts: Drafting and Administration Including the "Give-Me-Five" Unitrust," Real Property, Probate and Trust Journal, Vol. 33, No. 1, Spring 1998.

Horn, Jerold I., "Drafting Dispositive Provisions under the Prudent Investor Rule," 26<sup>th</sup> Annual Midwest/Midsouth Estate Planning Institute, UK/CLE Publication, July 1999.

Howell-Smith, Laura, "How Prop. Regs. on the Definition of Income Affect Total Return Trusts," Estate Planning, Vol. 28, No. 7, July 2001.

Levy, Jonathan A., "The Total Return Unitrust: Is It Time for High-Fives?" Trusts & Estates, Vol. 139, No. 6, June 2000.

O'Grady, John B., and Jennifer Schooley Stringer, "Final Regs. Approve Certain Changes in Grandfathered GST Trusts," Estate Planning, Vol. 28, No. 11, November 2001.

Schaengold, David, "The Uniform Principal and Income Act (1997) Has Been Amended," Trusts & Estates, Vol. 139, No. 12, December 2001.

Schaengold, David, "Decade of Change: Revising Trust Investment Law to Coordinate with Modern Portfolio Theory," Tax Management Estates, Gifts and Trusts Journal, Vol. \_\_\_, page 258, (2001).

Welch, Lyman W., "Progress of Total Return Legislation," Trusts & Estates, Vol. 139, No. 12, December 2001.

Wolf, Robert B., and Stephen R. Leimberg, "The Latest State Legislation Governing Total Return Unitrusts," Estate Planning, Vol. 28, No. 10, October 2001.



Wolf, Robert B., "Estate Planning with Total Return Trusts: Meeting Human and Investment Goals through Modern Trust Design," Real Property, Probate and Trust Journal, Vol. 36, No. 2, Summer 2001.

Wolf, Robert B., "Total Return Trusts: Can Your Client Afford Anything Less?" ACTEC Notes, Vol. 24, No. 1, Summer 1998; also in Real Property, Probate and Trust Journal, Vol. 33, No. 1, Spring 1998.

Wolf, Robert B., "Defeating the Duty to Disappoint Equally – The Total Return Trust," ACTEC Notes, Vol. 23, No. 1, Summer 1997; also in Real Property, Probate and Trust Journal, Vol. 32, No. 1, Spring 1997.

**THOSE FUNNY LITTLE LAWS THAT YOU  
DIDN'T KNOW EXISTED AND THAT WILL  
EFFECT YOUR ESTATE AND TRUST PRACTICE**

*Turney P. Berry  
Ogden Newell & Welch PLLC  
Louisville, Kentucky*

Copyright 2002. Turney P. Berry. All Rights Reserved.

**SECTION F**



# **THOSE FUNNY LITTLE LAWS THAT YOU DIDN'T KNOW EXISTED AND THAT WILL EFFECT YOUR ESTATE AND TRUST PRACTICE**

311.175	Persons Who May Execute An Anatomical Gift .....	F-1
311.623	Living Will Directive - Eligible Persons - Scope - Effect - Recognition of Person's Desire Not To Be Resuscitated .....	F-3
311.629	Powers of Health Care Surrogate .....	F-5
311.631	Responsible Parties Authorized To Make Health Care Decisions .....	F-7
381.135	Court-Appointed Commissioners to Determine Division of Land Jointly Held and Allotment of Dower or Curtesy - Survey Requirement .....	F-9
389A.030	Action in Circuit Court for Sale or Division of Property .....	F-13
381.136	Life Tenants and Their Descendants - Partition .....	F-15
381.180	Estates in Trust Subject to Debts of Beneficiary - Spendthrift Trusts Excepted - Other Exceptions .....	F-17
386.093	Effect of Disability, Incapacity, or Death on Power of Attorney, Durable or Otherwise .....	F-19
386.095	Execution and Delivery of Releases of Powers Exercisable by Deed, Will or Otherwise .....	F-21
	Charitable Provisions - Trust Savings Provisions .....	F-23
386.350	Definitions for KRS 386.355 and 386.360	
386.355	Acts Prohibited - Policy of State Regarding Private Foundations- Split-Interest Trusts - Charitable Trusts	
386.360	Trust Instruments - How Amended	
386.365	Distribution of Assets Upon Dissolution - Process for Selection of Receiving Trust - Assets Available for Distribution Defined	
381.260	Grants-in-aid of Charity Valid	
381.270	Gift to Charity Not Defeated for Want of Trustee	

## **SECTION F**

386.715	Duty to Inform and Account to Beneficiaries .....	F-31
386.825	Powers Exercisable By Joint Trustees - Liability .....	F-33
391.130	Descendants May Recover Annuity Not Fully Earned At Annuitant's Death .....	F-35
391.160	Authority of Life Tenant to Invade Corpus .....	F-37
391.210 - 391.260	Community Property Rights .....	F-39
391.210	Application	
391.215	Rebuttable Presumptions	
391.220	Disposition Upon Death	
391.225	Perfection of Title of Surviving Spouse	
391.230	Perfection of Title of Personal Representative, Heir, or Devisee	
391.235	Purchaser for Value or Lender	
391.240	Creditor's Rights	
391.245	Acts of Married Persons	
391.250	Limitations on Testamentary Disposition	
391.255	Uniformity of Application and Construction	
391.260	Title	
392.090	All Property Claims or Curtesy Barred by Divorce or Adultery .....	F-51
394.065	Validity of Trust, Devise or Legacy Not Affected By Specified Provisions .....	F-53
394.076	Uniform Testamentary Additions to Trust Act .....	F-55
394.070	Appointment by Will in Exercise of a Power - When Valid .....	F-57
394.310	Original Will May Be Withdrawn From Court, When .....	F-59
	Interpretation of Wills .....	F-61
394.400	Issue of Dead Devisee or Legatee Take Parent's Share	
394.410	Death of Part of Group of Devisees Before Testator-Children Includes Grandchildren	
394.520	Specific Legacy - When Payable	
397.1002	Requirement of Survival by One Hundred Twenty (120) Hours	
395.020	Executor Not to Act Until Will Probated - Exception .....	F-67
446.060	Writings - Signature Must Be At End - to Be in English .....	F-69

## SECTION F

287.380	Deposits by Minors .....	F-71
287.385	Education Loans to Minors – Validity .....	F-73
381.280	Forfeiture of Right to Property for Killing Decedent .....	F-75
Provisions Dealing with Aliens .....		F-77
381.300	Realty of Nonresident Alien Liable to Escheat After Eight Years Unless He Becomes Citizen	
381.310	Spouses and Children of Citizens - Property Rights	
381.320	Aliens Right as to Personalty - as to Realty if Resident	
381.330	Nonresident Alien - Rights as to Real Property Inherited	
Trustee Investments .....		F-83
386.020	Authorized Investments of Trust Funds - Fiduciary to Account for Profits	
386.800	Definitions	
386.810	Powers of Trustees Conferred by this Chapter	
386.820	Power of Court to Permit Deviation and to Approve Transactions Involving Conflict of Interest	
287.110	Investment of Funds Held in Fiduciary Capacity - Capital Stock Liable for Fiduciary Obligations	
287.277	Standards for Bank or Trust Company Acting as Fiduciary	
287.272	Investment of Fiduciary Assets in Company or Trust Associated with Investing Institution - Fee	
287.275	Limits on Liability of Bank or Trust Company Acting as Fiduciary .....	F-95
287.220	Corporate Fiduciaries Subject to Laws Governing Individuals- Security on Bonds - Ability to Serve as Trustee of Multiple Trusts with Common or Nonidentical Beneficiaries .....	F-95

## SECTION F



**311.175**

**Persons Who May Execute an Anatomical Gift**

Note (2) which allows others to make such gifts. Consider what "actual notice" might mean in a practical sense. What does a client do who definitely does not want gifts made? (3) would allow a client to notify likely donees, but not all.



**311.175 Persons who may execute an anatomical gift.**

- (1) Any individual of sound mind and eighteen (18) years of age or more may give all or any part of his body for any purpose specified in KRS 311.185, the gift to take effect upon death.
- (2) Any of the following persons, in order of priority stated, when persons in prior classes are not available at the time of death, and in the absence of actual notice of contrary indications by the decedent or actual notice of opposition by a member of the same or a prior class, may give all or any part of the decedent's body for any purpose specified in KRS 311.185:
  - (a) The spouse,
  - (b) An adult son or daughter,
  - (c) Either parent,
  - (d) An adult brother or sister,
  - (e) A guardian of the person of the decedent at the time of his death,
  - (f) Any other person authorized or under obligation to dispose of the body.
- (3) If the donee has actual notice of contrary indications by the decedent or that a gift by a member of a class is opposed by a member of the same or a prior class, the donee shall not accept the gift. The persons authorized by subsection (2) of this section may make the gift after or immediately before death.
- (4) A gift of all or part of a body authorizes any examination necessary to assure medical acceptability of the gift for the purposes intended.
- (5) The rights of the donee created by the gift are paramount to the rights of others except as provided by subsection (4) of KRS 311.225.

**Effective:** June 18, 1970

**History:** 1970 Ky. Acts ch. 68, sec. 2, effective June 18, 1970.

**311.623      Living Will Directive – Eligible Persons – Scope – Effect – Recognition of  
Person's Desire Not To Be Resuscitated**

Note (3). EMS requires its own form.

**311.623 Living will directive -- Eligible persons -- Scope -- Effect -- Recognition of person's desire not to be resuscitated.**

- (1) An adult with decisional capacity may make a written living will directive that does any or all of the following:
  - (a) Directs the withholding or withdrawal of life-prolonging treatment; or
  - (b) Directs the withholding or withdrawal of artificially provided nutrition or hydration; or
  - (c) Designates one (1) or more adults as a surrogate or successor surrogate to make health care decisions on behalf of the grantor. During any period in which two (2) or more surrogates are serving, all decisions shall be by unanimous consent of all the acting surrogates unless the advance directive provides otherwise; or
  - (d) Directs the giving of all or any part of the adult's body upon death for any purpose specified in KRS 311.185.
- (2) Except as provided in KRS 311.633, a living will directive made pursuant to this section shall be honored by a grantor's family, regular family physician or attending physician, and any health care facility of or in which the grantor is a patient.
- (3) For purposes of KRS 311.621 to 311.643, notification to any emergency medical responder as defined by KRS Chapter 211 or any paramedic as defined by KRS Chapter 311, of a person's authentic wish not to be resuscitated shall be recognized only if on a standard form or identification approved by the Kentucky Board of Medical Licensure, in consultation with the Cabinet for Health Services.

**Effective:** July 15, 1998

**History:** Amended 1998 Ky. Acts ch. 392, sec. 1, effective July 15, 1998; and. ch. 426, sec. 538, effective July 15, 1998. -- Created 1994 Ky. Acts ch. 235, sec. 2, effective July 15, 1994.

**Legislative Research Commission Note (7/15/98).** This section was amended by 1998 Ky. Acts chs. 392 and 426 which do not appear to be in conflict and have been codified together.

**311.629 Powers of Health Care Surrogate**

In view of (2), if the "attending physician" says grantor has decisional capacity, can anyone remove the attending physician?

Note the issues that obviously arise under (3)(c) and (3)(d).

Is (1) subservient to (3)? That is, can a client authorize treatment to be withheld in circumstances other than (3)?

**311.629 Powers of health care surrogate.**

- (1) A surrogate designated pursuant to an advance directive may make health care decisions for the grantor which the grantor could make individually if he or she had decisional capacity, provided all the decisions shall be made in accordance with the desires of the grantor as indicated in the advance directive. When making any health care decision for the grantor, the surrogate shall consider the recommendation of the attending physician and honor the decision made by the grantor as expressed in the advance directive.
- (2) The surrogate may not make a health care decision in any situation in which the grantor's attending physician has determined in good faith that the grantor has decisional capacity. The attending physician shall proceed as if there were no designation if the surrogate is unavailable or refuses to make a health care decision.
- (3) A health care surrogate may authorize the withdrawal or withholding of artificially-provided nutrition and hydration in the following circumstances:
  - (a) When inevitable death is imminent, which for the purposes of this provision shall mean when death is expected, by reasonable medical judgment, within a few days; or
  - (b) When a patient is in a permanently unconscious state if the grantor has executed an advance directive authorizing the withholding or withdrawal of artificially-provided nutrition and hydration; or
  - (c) When the provision of artificial nutrition cannot be physically assimilated by the person; or
  - (d) When the burden of the provision of artificial nutrition and hydration itself shall outweigh its benefit. Even in the exceptions listed in paragraphs (a), (b), and (c) of this subsection, artificially-provided nutrition and hydration shall not be withheld or withdrawn if it is needed for comfort or the relief of pain.
- (4) Notwithstanding the execution of an advance directive, life sustaining treatment and artificially-provided nutrition and hydration shall be provided to a pregnant woman unless, to a reasonable degree of medical certainty, as certified on the woman's medical chart by the attending physician and one (1) other physician who has examined the woman, the procedures will not maintain the woman in a way to permit the continuing development and live birth of the unborn child, will be physically harmful to the woman or prolong severe pain which cannot be alleviated by medication.

**Effective:** July 15, 1994

**History:** Created 1994 Ky. Acts ch. 235, sec. 5, effective July 15, 1994.

**311.631      Responsible Parties Authorized To Make Health Care Decisions**

Note the line-up of surrogates and the powers in 311.629 as given by (4).

Suppose the patient executed the statutory prescribed form designating spouse, and leaving decisions up to spouse. Spouse predeceases, and per (1)(c) the children are acting. What effect does (3) have? What if patient directed there be no treatment but let spouse override; may the children override?

**311.631 Responsible parties authorized to make health care decisions.**

- (1) If an adult patient, who does not have decisional capacity, has not executed an advance directive or to the extent the advance directive does not address a decision that must be made, any one (1) of the following responsible parties, in the following order of priority if no individual in a prior class is reasonably available, willing, and competent to act, shall be authorized to make health care decisions on behalf of the patient:
  - (a) The judicially-appointed guardian of the patient, if the guardian has been appointed and if medical decisions are within the scope of the guardianship;
  - (b) The spouse of the patient;
  - (c) An adult child of the patient, or if the patient has more than one (1) child, the majority of the adult children who are reasonably available for consultation;
  - (d) The parents of the patient;
  - (e) The nearest living relative of the patient, or if more than one (1) relative of the same relation is reasonably available for consultation, a majority of the nearest living relatives.
- (2) In any case in which a health care decision is made under this section, the decision shall be noted in writing in the patient's medical records.
- (3) An individual authorized to consent for another under this section shall act in good faith, in accordance with any advance directive executed by the individual who lacks decisional capacity, and in the best interest of the individual who does not have decisional capacity.
- (4) An individual authorized to make a health care decision under this section may authorize the withdrawal or withholding of artificially-provided nutrition and hydration only in the circumstances as set forth in KRS 311.629(3).

**Effective:** July 15, 1994

**History:** Created 1994 Ky. Acts ch. 235, sec. 6, effective July 15, 1994.

**381.135 Court-Appointed Commissioners to Determine Division of land jointly held and allotment of dower or curtesy – Survey requirement**

Note 1(b). What is the effect on discounts? Can a partnership agreement trump this right? That is, can a 20% owner give up the statutory right, and, if so, does that bind the owner's heirs?



**381.135 Court-appointed commissioners to determine division of land jointly held and allotment of dower or curtesy -- Survey requirement.**

- (1) (a) As used in this subsection:
  1. "Ownership interest in a closely held farm corporation or partnership" means any interest in a farm with one (1) or more of the shareholders or partners owning twenty percent (20%) or more of the corporation or partnership.
  2. "Farm" means a tract of at least five (5) contiguous acres used for the production of agricultural or horticultural crops including, but not limited to, livestock, livestock products, poultry, poultry products, grain, hay, pastures, soybeans, tobacco, timber, orchard fruits, vegetables, flowers, or ornamental plants, including provision for dwellings for persons and their families who are engaged in the above agricultural use on the tract, but not including residential building development for sale or lease to the public.
- (b) A person desiring a division of land held jointly with others, a person desiring an allotment of dower or curtesy, or a person with an ownership interest of twenty percent (20%) or more in a closely held farm corporation or partnership may file in the Circuit Court of the county in which the land or the greater part thereof lies a petition containing a description of the land, a statement of the names of those having an interest in it, and the amount of such interest, with a prayer for the division or allotment; and, thereupon, all persons interested in the property who have not united in the petition shall be summoned to answer not more than twenty (20) days after service of the summons. The written evidences of the title to the land, or copies thereof, if there be any, must be filed with the petition.
- (2) The statutory guardian of an infant or guardian or conservator of a person adjudged mentally disabled may file or unite in the petition, in the names of, and in conjunction with such infant or mentally disabled person; and, if the petition be against an infant or mentally disabled person the guardian or conservator may appear and defend for them; if they fail to do so, the court shall appoint a discreet person for that purpose.
- (3) Upon such a petition by all interested in the property, or upon the expiration of twenty (20) days after the service of a summons on all who have an interest in the property and have not united in the petition, the court may order the division, or allotment of dower or curtesy, according to the rights of the parties.
- (4) The court shall appoint three (3) competent persons as commissioners to determine the division or allotment of land, having a due regard for the rights of all parties interested. Before proceeding to act, the commissioners shall take an oath to discharge their duty impartially.
- (5) The order of appointment shall fix a time and place for the meeting of the commissioners who shall meet accordingly; but, if prevented from meeting at the time and place so fixed, they may meet as soon thereafter as convenient, and may

adjourn to such other time and place as they may agree upon, until their duty shall be performed.

- (6) The commissioners shall equitably determine the allotment to the parties of their respective interests in the land. A registered land surveyor shall perform the actual survey of the land in accordance with the determination made by the commissioners, and prepare the descriptions of the land, including all related maps, plats, and documents, and he shall affix thereto his personal seal and signature, unless such actual survey and the resultant description, maps, plats, and documents pertaining to this land are already in existence. The commissioners shall make report thereof to the court, which may either confirm, set aside, or remand the report to the commissioners for correction.
- (7) If the report be confirmed, a commissioner to be appointed for the purpose shall, by deed, convey to each party the land allotted to him.
- (8) If the report be confirmed by the Circuit Court, it, together with said surveyor's descriptions, survey and all related documents, and the applicable deeds shall be certified by the clerk of that court to the county clerk, for record.
- (9) Two (2) of the commissioners may act, if one (1) refuses or fails to do so.
- (10) A party summoned may, by answer, controvert the allegations of the petition or contest the rights claimed therein; and, thereupon, the case shall be tried and decided as an ordinary action, but without the intervention of a jury.
- (11) The costs of the action shall be apportioned among the parties in the ratio of their interests, except that the costs arising from a contest of fact or law shall be adjudged against the unsuccessful party.
- (12) No verification of the pleadings shall be required.
- (13) The commissioners and the land surveyor shall be paid a reasonable compensation, to be taxed as costs.
- (14) This section shall not affect the jurisdiction of courts of equity to make partition or allot dower or curtesy.

**Effective:** July 15, 1998

**History:** Amended 1998 Ky. Acts ch. 316, sec. 1, effective July 15, 1998. -- Amended 1988 Ky. Acts ch. 227, sec. 1, effective July 15, 1988. -- Amended 1982 Ky. Acts ch. 141, sec. 96, effective July 1, 1982. -- Amended 1978 Ky. Acts ch. 384, sec. 508, effective June 17, 1978. -- Amended 1976 (1st Extra. Sess.) Ky. Acts ch. 14, sec. 302, effective January 2, 1978. -- Amended 1974 Ky. Acts ch. 386, sec. 68. -- Transferred 1952 Ky. Acts ch. 84, sec. 1, effective July 1, 1953, from C.C. sec. 499.



**389A.030      Action in Circuit Court For Sale or Division of Property**

This is the more general statute. Note that deals with the rights of a life tenant upon sale or division of the entire property.

**389A.030 Action in Circuit Court for sale or division of property.**

- (1) When two (2) or more persons other than tenants by the entirety in residential property actually occupied by them as a principal residence share title to real estate in such manner that a conveyance by them jointly would pass a fee simple title, any one (1) or more of them may bring an action for the sale or division thereof in the Circuit Court of the county in which the land, or the greater part thereof, lies, making parties defendant those owners who have not joined as plaintiffs. A fiduciary possessing a power of sale may institute such an action against owners of interests not represented by him. Defendant owners shall be brought before the court in the manner provided by the civil rules whether or not a fiduciary possesses a power of sale of the defendant's interest, but any fiduciary possessing such a power shall also be made a defendant. The case shall be tried without a jury.
- (2) A defendant who is under disability and for whom no fiduciary is acting shall be represented in the action by a guardian ad litem, but in the event of sale of such defendant's interest the court shall retain control of the proceeds of such interest until a duly appointed and adequately bonded fiduciary or custodian pursuant to a court order makes claim to the funds.
- (3) In all such actions indivisibility of the real estate shall be presumed unless an issue in respect thereto is raised by the pleading of any party, and if the court is satisfied from the evidence that the property is divisible, without materially impairing the value of any interest therein, division thereof pursuant to KRS 381.135 shall be ordered.
- (4) If a sale of all or any part of the real estate shall be ordered, the court shall refer the matter to the master commissioner or appoint a commissioner to conduct a public sale and convey the property upon terms of sale and disposition of the net proceeds as may have been determined by the court.
- (5) The death of any party pending the action and prior to distribution of the proceeds of sale or setting apart a divisible share shall not affect the action but the court may direct distribution or apportionment to the successors in interest of the decedent upon application therefor.
- (6) If the interest of any party be one for life, or other term, in any portion of the real estate, the court shall determine the value of such interest and direct that such party receive a portion of the net sale proceeds or portion of the property if divisible, in fee in satisfaction of such interest, but if any party to the action objects to such procedure, and if the court finds that such procedure would defeat the objects and purpose of a person not a party to the action, such as a testator, grantor or settlor, but that sale or division is nevertheless desirable, the court shall order that the interest of the life or term tenant shall continue as to his portion of the real estate or the net proceeds of the sale thereof, in the latter case by directing that the funds derived from the sale of that portion of the real estate in which the life or term interest existed be paid to a trustee, appointed by and accountable to the District Court, for reinvestment and distribution of income and principal in a manner consistent with the instrument under which the life or term estate was created.

Effective: July 15, 1982

**381.136      Life Tenants and Their Descendants – Partition**

Note that in (1) “all persons” with an interest must be parties.

This a very useful statute.

**381.136 Life tenants and their descendants – Partition.**

- (1) Where the land is held under a deed or will vesting a life estate in two or more persons or in trust for their benefit, with remainder as to the share of each to his or her children or descendants, it shall be lawful for a court of equity, on the petition of one of such life tenants and his or her children or descendants who would then be entitled to such remainder, all persons having interests in such lands being made parties, to partition such land so as to set apart to such life tenants and children or descendants so much of said land to which they shall be entitled in severalty; and to that alone shall attach the title or interest of after-born children or descendants in whom, by the terms of said deed or will, such a remainder would vest.
- (2) Where part of the land so held shall be situated in this state and part in another state, the court may, in making partition, take into consideration the value of all of said land, and set apart to those resident in this state land in this state equal to their full share of all said land, securing, by proper deeds and orders to the nonresidents, release of the interest of such residents in the lands in the other state or territory.

**Effective:** July 1, 1953

**History:** Transferred 1952 Ky. Acts ch. 84, sec. 1, effective July 1, 1953, from C.C. sec. 499a. -- Created 1886 Ky. Acts ch. 1171, secs. 1 and 2.

**381.180      Estates in Trust Subject to Debts of Beneficiary – Spendthrift Trusts Excepted  
– Other Exceptions**

I know you know we have a spendthrift statute but it is worth reading.

Note in 6(a) that spendthrift trusts may be reached for child support and spousal maintenance.

Note 7(a) on self-settled trusts. The meaning of “for his own benefit” is not obvious. For instance, does it mean that if the creator is not a current beneficiary but can become one upon the action of another that the trust is for the creator’s own benefit. The Restatement (2d) of Trusts §156 sets forth the common law rule.



**381.180 Estates in trust subject to debts of beneficiary – Spendthrift trusts excepted – Other exceptions.**

- (1) Estates of every kind held or possessed in trust shall be subject to the debts and charges of the beneficiaries thereof the same as if the beneficiaries also owned the similar legal interest in the property, unless the trust is a spendthrift trust.
- (2) As used herein, unless the context otherwise requires, "spendthrift trust" means a trust in which by the terms of the instrument creating it a valid restraint on the voluntary and involuntary alienation of the interest of a beneficiary is imposed.
- (3) Specific language shall not be necessary to create a spendthrift trust and it shall be sufficient if the instrument creating the trust manifests an intention to create a spendthrift trust.
- (4) If an instrument creating a trust provides that a beneficiary is entitled to receive income of the trust and that his interest shall not be alienable by him and shall not be subject to alienation by operation of law or legal process, the restraint on the voluntary and involuntary alienation of his right to income due and to accrue shall be valid.
- (5) If an instrument creating a trust provides that a beneficiary is entitled to receive principal of the trust at a future time and that his interest shall not be alienable by him and shall not be subject to alienation by operation of law or legal process, the restraint on the voluntary and involuntary alienation of his right to principal shall be valid.
- (6) Although a trust is a spendthrift trust, the interest of the beneficiary shall be subject to the satisfaction of an enforceable claim against the beneficiary:
  - (a) By the spouse or child of the beneficiary for support, or by the spouse for maintenance;
  - (b) If the trust is not a trust described in subsection (7)(b) of this section by providers of necessary services rendered to the beneficiary or necessary supplies furnished to him; and
  - (c) By the United States or the Commonwealth of Kentucky for taxes due from him on account of his interest in the trust or the income therefrom.
- (7)
  - (a) If a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary alienation of his interest, his interest nevertheless shall be subject to alienation by operation of law or legal process.
  - (b) This subsection shall not be construed to subject to alienation any interest in an individual retirement account or annuity, tax sheltered annuity, simplified employee pension, pension, profit-sharing, stock bonus, or other retirement plan described in the Internal Revenue Code of 1986, as amended, which qualifies for the deferral of current income tax until the date benefits are distributed.

**Effective:** July 13, 1990

**History:** Amended 1990 Ky. Acts ch. 220, sec. 1, effective July 13, 1990. -- Amended 1974 Ky. Acts ch. 386, sec. 69. -- Amended 1966 Ky. Acts ch. 61, sec. 1. --

**386.093      Effect of Disability, Incapacity, or Death on Power of Attorney, Durable or Otherwise**

Note (3). Consider: should a client have a “death-bed” attorney-in-fact, with only the powers to form partnerships and make gifts, so that upon premature death the attorney-in-fact can do “death-bed” planning? Apparently it would be effective if the attorney-in-fact didn’t know about the death.

Note 386.093(6) on the power to make gifts. Presumably, giving the power to the attorney-in-fact satisfies the statute. The statute should limit IRS challenges.

**386.093 Effect of disability, incapacity, or death on power of attorney, durable or otherwise.**

- (1) As used in this section, "durable power of attorney" means a power of attorney by which a principal designates another as the principal's attorney in fact in writing and the writing contains the words, "This power of attorney shall not be affected by subsequent disability or incapacity of the principal, or lapse of time", or "This power of attorney shall become effective upon the disability or incapacity of the principal", or similar words showing the intent of the principal that the authority conferred shall be exercisable notwithstanding the principal's subsequent disability or incapacity, and, unless it states a time of termination, notwithstanding the lapse of time since the execution of the instrument.
- (2) All acts done by an attorney in fact under a durable power of attorney during any period of disability or incapacity of the principal have the same effect and inure to the benefit of and bind the principal and the principal's successors in interest as if the principal were competent and not disabled. Unless the instrument states a time of termination, the power is exercisable notwithstanding the lapse of time since the execution of the instrument.
- (3) The death of a principal who has executed a written power of attorney, durable or otherwise, does not revoke or terminate the agency as to the attorney in fact or other person, who, without actual knowledge of the death of the principal, acts in good faith under the power. Any action so taken, unless otherwise invalid or unenforceable, binds successors in interest of the principal.
- (4) The disability or incapacity of the principal who has previously executed a written power of attorney that is not a durable power does not revoke or terminate the agency as to the attorney in fact or other person, who, without actual knowledge of the disability or incapacity of the principal, acts in good faith under the power. Any action so taken, unless otherwise invalid or unenforceable, binds the principal and the principal's successors in interest.
- (5) If the power of attorney is to become effective upon the disability or incapacity of the principal, the principal may specify the conditions under which the power is to become effective and may designate the person, persons, or institution responsible for making the determination of disability or incapacity. If the principal fails to so specify, the power shall become effective upon a written determination by two (2) physicians that the principal is unable, by reason of physical or mental disability, to prudently manage or care for the principal's person or property, which written determination shall be conclusive proof of the attorney in fact's power to act pursuant to the power of attorney. The two (2) physicians making the determination shall be licensed to practice medicine.
- (6) Notwithstanding any provision of law to the contrary, a durable power of attorney may authorize an attorney in fact to make a gift of the principal's real or personal property to the attorney in fact or to others if the intent of the principal to do so is unambiguously stated on the face of the instrument.

Effective: July 14, 2000

**386.095      Execution and Delivery of Releases of Powers Exercisable by Deed, Will or Otherwise**

It would appear that (1) would allow an inter vivos or testamentary power to be "cut-down" to one or more persons. The statute is helpful if remaindermen need to consent to some action and a beneficiary has a power of appointment. The beneficiary can execute a partial release, thus fixing the class which must consent.

**386.095 Execution and delivery of releases of powers exercisable by deed, will or otherwise.**

- (1) Any power which is exercisable by deed, by will, by deed or will, or otherwise, whether general or special, other than a power in trust which is imperative, is releasable by written instrument signed by the donee of the power and delivered as hereinafter provided. A power which is releasable may be released with respect to the whole or any part of the property subject to such power and may also be released in such manner as to reduce or limit the persons or objects, or classes of persons or objects, in whose favor such power would otherwise be exercisable. No release of a power shall be deemed to make imperative a power which was not imperative prior to such release, unless the instrument of release expressly so provides.
- (2) Such release may be delivered to any of the following:
  - (a) Any person specified for such purpose in the instrument creating the power;
  - (b) Any trustee of the property to which the power relates;
  - (c) Any person, other than the donee of the power, who could be adversely affected by an exercise of the power; or
  - (d) The recorder of deeds of the county in which the donee of the power resides or has a place of business, or in which the deed, will or other instrument creating the power is recorded.

**Effective:** July 13, 1984

**History:** Amended 1984 Ky. Acts ch. 111, sec. 196, effective July 13, 1984. — Created 1944 Ky. Acts ch. 14, sec. 1.

## **Charitable Provisions – Trust Savings Provisions**

<b>386.350</b>	<b>Definitions for KRS 386.355 and 386.360</b>
<b>386.355</b>	<b>Acts Prohibited – Policy of State Regarding Private Foundations – Split-Interest Trusts – Charitable Trusts</b>
<b>386.360</b>	<b>Trust Instruments – How Amended</b>
<b>386.365</b>	<b>Distribution of Assets Upon Dissolution – Process for Selection of Receiving Trust – Assets Available for Distribution Defined</b>
<b>381.260</b>	<b>Grants-in-aid of Charity Valid</b>
<b>381.270</b>	<b>Gift to Charity Not Defeated for Want of Trustee</b>

These statutes assist in various ways with charitable trusts. The provisions of 386.355 should be included in any charitable trust that is or might be a private foundation, and those of 386.365 in all charitable trusts.

386.360 is useful but read literally only allows amendments to conform to the requirements of the Internal Revenue Code in effect on January 1, 1970, not thereafter. Amendments to cure charitable remainder trust problems may not be covered, for instance.

381.260 requires a charitable bequest only to identify with reasonable certainty the charitable beneficiary or beneficiaries.

**386.350 Definitions for KRS 386.355 and 386.360.**

As used in KRS 386.355 and 386.360, unless the context requires otherwise:

- (1) "Internal Revenue Code" means the Internal Revenue Code of 1954, in effect on January 1, 1970, including all appropriate provisions of the Tax Reform Act of 1969 at the dates specified in that law, exclusive of any amendments made subsequent to December 31, 1969.
- (2) "Trust" includes a trust or any other entity (other than a corporation) which has, in whole or in part, a charitable purpose.
- (3) "Trustee" includes any member of the governing body of any trust, as defined in this section.

**History:** Amended 1974 Ky. Acts ch. 56, sec. 1. -- Created 1972 Ky. Acts ch. 344, sec. 1.

**386.355 Acts prohibited -- Policy of state regarding private foundations -- Split-interest trusts -- Charitable trusts.**

- (1) In the administration of any trust which is a "private foundation" as defined in Section 509 of the Internal Revenue Code, a trust for charitable purposes described in Section 4947(a)(1) of the Internal Revenue Code to the extent that it is treated for federal tax purposes as such a private foundation, or a "split-interest trust" as described in Section 4947(a)(2) of the Internal Revenue Code, the following acts are prohibited:
  - (a) Engaging in any act of "self-dealing" (as defined in Section 4941(d) of the Internal Revenue Code) which would give rise to any liability for any tax imposed by Section 4941 of the Internal Revenue Code;
  - (b) Retaining any "excess business holdings" (as defined in Section 4943(c) of the Internal Revenue Code) which would give rise to any liability for any tax imposed by Section 4943 of the Internal Revenue Code;
  - (c) Making any investments which would jeopardize the carrying out of any of the exempt purposes of the trust, within the meaning of Section 4944 of the Internal Revenue Code, so as to give rise to any liability for any tax imposed by Section 4944 of the Internal Revenue Code; and
  - (d) Making any "taxable expenditures" (as defined in Section 4945(d) of the Internal Revenue Code) which would give rise to any liability for any tax imposed by Section 4945 of the Internal Revenue Code; provided, however, that the prohibitions of this subsection shall not apply to split-interest trusts or to amounts thereof, to the extent that such prohibitions are made inapplicable thereto by Section 4947 of the Internal Revenue Code.
- (2) In the administration of any trust which is a "private foundation" as defined in Section 509 of the Internal Revenue Code, or a trust for charitable purposes described in Section 4947(a)(1) of the Internal Revenue Code to the extent that it is treated for federal tax purposes as such a private foundation, there shall, for the purposes specified in the governing instrument, be distributed at such time and in such manner, for each taxable year, amounts of income and principal at least sufficient to avoid liability for any tax imposed by Section 4942 of the Internal Revenue Code.
- (3) Subsections (1) and (2) of this section express the continuing policy of this state with respect to charitable trust interests and are enacted to assist such trusts in maintaining various tax benefits extended to them, and shall apply to all trusts described therein; provided, however, that subsections (1) and (2) of this section shall not apply to a trust in existence on July 1, 1972, to the extent that the Attorney General of this state, the trustor, or any beneficiary of such trust, on or before November 30, 1972, files with the trustee of such trust a written objection to the application to such trust of one (1) or more provisions of subsections (1) and (2) of this section and the trustee receiving such written objection commences an action on or before December 31, 1972, in the court having jurisdiction over such trust to reform its governing instrument or any other instrument in order to meet, or to excuse such trust from compliance with the requirements of subsections (1) and (2)



of this section. If a trustee receiving such written objection shall commence such an action, the one (1) or more provisions of subsections (1) and (2) of this section specified in such written objection shall not apply to such trust unless and until such court determines that their application to such trust is in the best interests of all parties in interest.

- (4) No trustee of a trust to which subsection (1) or (2) of this section is applicable shall be surcharged for a violation of a prohibition or requirement of said subsections unless he participated in such violation knowing that it was a violation, nor shall such a trustee be surcharged if such violation was not willful and was due to reasonable cause; provided, however, that this subsection does not exonerate a trustee from any responsibility or liability to which he is subject under any other rule of law, whether or not duplicated in subsections (1) and (2) of this section.
- (5) Except as provided in subsection (4) of this section, nothing in this section shall impair the rights and powers of the courts or the Attorney General with respect to any trust.
- (6) In furtherance of the continuing policy of this state to assist charitable trust interests in maintaining various tax benefits extended to them, the provisions of subsections (1) and (2) of this section shall be deemed to have been in force and effect on January 1, 1970; provided, however, the provisions of said subsections shall affect a trust organized before January 1, 1970, only on and after the first day of its first taxable year (for federal tax purposes) beginning on or after January 1, 1972.

**History:** Created 1972 Ky. Acts ch. 344, sec. 2.

**386.360 Trust instruments – How amended.**

- (1) In order to assist charitable trust interests in maintaining various tax benefits extended to them, the governing instrument of a trust may be amended to permit the trust to conform to the requirements of, or to obtain benefits available under, applicable provisions of the Internal Revenue Code. Such amendment may be made by the trustee with the approval of the Attorney General of this state, of the trustor and, if one (1) or more beneficiaries are named in the governing instrument of such trust, of each named beneficiary. If the trustor is not then living or is not then competent to give such approval, such amendment may be made by the trustee with the approval of the Attorney General and, if one (1) or more beneficiaries are named in the governing instrument of such trust, of each named beneficiary. If one (1) or more of said required approvals is not obtained, the trustee may apply to the court having jurisdiction over such trust for approval of such amendment. Said governing instrument may also be amended in any respect and by any method set forth in such instrument or as otherwise provided by law.
- (2) Nothing in this section shall impair the rights and powers of the courts or the Attorney General with respect to any trust.

**History:** Created 1972 Ky. Acts ch. 344, sec. 3.

**386.365 Distribution of assets upon dissolution -- Process for selection of receiving trust -- Assets available for distribution defined.**

- (1) Upon termination or dissolution of any trust or other entity (other than a corporation) which is or may become an exempt organization as described in Section 501(c)(3) of the Internal Revenue Code of 1954, as amended, or a charitable trust described in Section 4947(a)(1) of the Internal Revenue Code of 1954, as amended, any assets lawfully available for distribution shall be distributed to one (1) or more qualifying organizations described in Section 501(c)(3) of said Internal Revenue Code (or described in any corresponding provision of any successor statute) which organization or organizations have a charitable purpose which, at least generally, includes a purpose similar to the terminating or dissolving organization. The organization to receive the assets of the dissolving organization hereunder shall be selected in the discretion of a majority of the managing body of the dissolving organization, and if its members cannot so agree, then the recipient organization shall be selected pursuant to a verified petition in equity filed in a court of proper jurisdiction against the terminating or dissolving organization by one (1) or more of its managing body which verified petition shall contain such statements as reasonably indicate the applicability of this section. The court upon a finding that this section is applicable shall select the qualifying organization or organizations to receive the assets to be distributed, giving preference if practicable to organizations located within the Commonwealth of Kentucky. In the event that the court shall find that this section is applicable but that there is no qualifying organization known to it which has a charitable purpose, which, at least generally, includes a purpose similar to the terminating or dissolving organization, then the court shall direct the distribution of its assets lawfully available for distribution to the Treasurer of the Commonwealth of Kentucky to be added to the general fund.
- (2) For purposes of this section "assets lawfully available for distribution" shall include the assets of a terminating or dissolving organization remaining after:
  - (a) Payment, or provision for payment, of all liabilities and obligations of the organization; and
  - (b) Return, transfer or conveyance of any assets held by the organization (the terms of creating instrument of which require such return, transfer or conveyance upon termination or dissolution or otherwise) in accordance with the terms of the creating instrument; and
  - (c) In the event legal action is filed pursuant hereto, payment or provision for payment of all costs, including a reasonable attorney's fee for the parties, fixed by the court.
- (3) This section shall not be construed to deprive any person of any vested property interest which he may have on June 21, 1974.

**History:** Created 1974 Ky. Acts ch. 155, sec. 1.

**381.260 Grants-in-aid of charity valid.**

- (1) Every grant, conveyance, legacy, bequest, devise, gift, appointment, assignment and transfer of property, whenever made and in whatever form, shall be valid (a) if made to any corporation, association, trust, foundation, or similar organization or entity, created or formed for and devoted solely to charitable, religious, scientific, literary, educational, humane, benevolent or like purposes or, (b) except as otherwise provided by statute, if it is made for any charitable or humane purpose and if it points out with reasonable certainty the purposes of the charity and the beneficiaries thereof.
- (2) A grant, conveyance, legacy, bequest, devise, gift, appointment, assignment and transfer of property, whenever made and in whatever form, is deemed to point out with reasonable certainty the purposes of the charity and beneficiaries thereof if and so long as the same is to or for the use of any corporation, trust, community chest, fund, foundation, or other entity organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, including the encouragement of art and the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private stockholder or individual (except as reasonable compensation for services rendered), and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office, even though such corporation, trust, fund, foundation or other entity is authorized to apply the trust income or property to any class or classes of charitable purposes mentioned above and the trustee or other managing individual or body is able and willing to make the selection.

**Effective:** July 15, 1980

**History:** Amended 1980 Ky. Acts ch. 123, sec. 1, effective July 15, 1980. -- Amended 1966 Ky. Acts ch. 211, sec. 1(1). -- Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 317.

**381.270 Gift to charity not defeated for want of trustee.**

No charity shall be defeated for want of a trustee or other person in whom the title may vest; but courts of equity may uphold the charity by appointing trustees, if there be none, or by taking control of the fund or property, and directing its management and settling who is the beneficiary thereof.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 318.

**386.715      Duty to Inform and Account to Beneficiaries**

Breach of notification provisions can lead to surcharge of a trustee.

**386.715 Duty to inform and account to beneficiaries.**

The trustee shall keep the beneficiaries of the trust reasonably informed of the trust and its administration. In addition:

- (1) Within thirty (30) days after his acceptance of the trust, the trustee shall inform in writing the current beneficiaries and if possible, one (1) or more persons who may represent beneficiaries with future interests, of the court in which the trust is registered and of his name and address.
- (2) Upon reasonable request, the trustee shall provide the beneficiary with a copy of the terms of the trust which describe or affect his interest and with relevant information about the assets of the trust and the particulars relating to the administration.
- (3) Upon reasonable request, a beneficiary is entitled to a statement of the accounts of the trust annually and on termination of the trust or change of the trustee.

**History:** Created 1976 Ky. Acts ch. 218, sec. 14.

**386.825 Powers Exercisable By Joint Trustees – Liability**

This statute initially appears helpful to limit the liability of an out-voted trustee. However, consider which (1) would limit a dissenting trustee's liability without (3) requiring a co-trustee to attempt to prevent a breach.



**386.825 Powers exercisable by joint trustees – Liability.**

- (1) Any power vested in three (3) or more trustees may be exercised by a majority, but a trustee who has not joined in exercising a power is not liable to the beneficiaries or to others for the consequences of the exercise; and a dissenting trustee is not liable for the consequences of an act in which he joins at the direction of the majority of the trustees, if he expressed his dissent in writing to any of his cotrustees at or before the time of the joinder.
- (2) If two (2) or more trustees are appointed to perform a trust, and if any of them is unable or refuses to accept the appointment, or, having accepted, ceases to be a trustee, the surviving or remaining trustees shall perform the trust and succeed to all the powers, duties, and discretionary authority given to the trustees jointly.
- (3) This section does not excuse a cotrustee from liability for failure either to participate in the administration of the trust or to attempt to prevent a breach of trust.

**History:** Created 1976 Ky. Acts ch. 218, sec. 49.

**391.130      Descendants May Recover Annuity Not Fully Earned at Annuitant's Death**

The drafting point is to provide that an annuity cuts off with the last payment received if you do not want to prorate.

**391.130 Descendants may recover annuity not fully earned at annuitant's death.**

Whenever any person entitled to an annuity dies within the year, and before the annuity is fully earned, the heirs or personal representative of that person may recover such proportion of the entire amount of the annuity as the time of the year already elapsed at the date of the death of the annuitant bears to the entire year.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 2070.

**391.160      Authority of Life Tenant to Invade Corpus**

Note (3) applies to trusts. In an otherwise hopeless situation where a beneficiary is trustee and the standards are not ascertainable, if an argument can be made that in fact the trust does not "expressly state the purpose for or the extent to which" the trustee can distribute principal then 3(c) and (4) may save the situation.

**391.160 Authority of life tenant to invade corpus.**

- (1) If
  - (a) A devise, bequest, or conveyance of real or personal property is made by written instrument free of any trust; and
  - (b) By the express terms of the instrument or by rule of law the devise, bequest or conveyance is made to a life tenant with power to consume principal or invade corpus, with the remainder to another upon the death of the life tenant; and
  - (c) The instrument does not expressly state the purpose for or the extent to which the life tenant may consume principal or invade corpus, then the provisions of subsection (2) shall apply.
- (2) The life tenant's power to consume principal or invade corpus shall be limited to such consumption or invasion as shall be necessary for his health, education (including college and professional education), and support in his accustomed manner of living.
- (3) If
  - (a) A devise, bequest, or conveyance of real or personal property is made in trust by written instrument; and
  - (b) By the express terms of the trust instrument or by rule of law the devise, bequest or conveyance is made for the benefit of a tenant for life with power in the trustee to consume principal or invade corpus for the benefit of the life tenant, with remainder to another upon the death of the life tenant; and
  - (c) The instrument does not expressly state the purpose for or the extent to which the trustee may consume principal or invade corpus for the benefit of the life tenant, then the provisions of subsection (4) shall apply.
- (4) The trustee's power to consume principal or invade corpus for the benefit of the life tenant shall be limited to such consumption or invasion as shall be necessary for his health, education (including college and professional education), and support in his accustomed manner of living.

**History:** Created 1974 Ky. Acts ch. 299, sec. 12.

**391.210 - 391.260    Community Property Rights**

<b>391.210</b>	<b>Application</b>
<b>391.215</b>	<b>Rebuttable Presumptions</b>
<b>391.220</b>	<b>Disposition Upon Death</b>
<b>391.225</b>	<b>Perfection of Title of Surviving Spouse</b>
<b>391.230</b>	<b>Perfection of Title of Personal Representative, heir, or devisee</b>
<b>391.235</b>	<b>Purchaser for Value or Lender</b>
<b>391.240</b>	<b>Creditors' Rights</b>
<b>391.245</b>	<b>Acts of Married Persons</b>
<b>391.250</b>	<b>Limitations on Testamentary Disposition</b>
<b>391.255</b>	<b>Uniformity of Application and Construction</b>
<b>391.260</b>	<b>Title</b>

**391.210 Application.**

KRS 391.210 to 391.260 applies to the disposition at death of the following property acquired by a married person:

- (1) All personal property, wherever situated:
  - (a) Which was acquired as or became, and remained, community property under the laws of another jurisdiction; or
  - (b) All or the proportionate part of that property acquired with the rents, issues, or income of, or the proceeds from, or in exchange for, that community property; or
  - (c) Traceable to that community property;
- (2) All or the proportionate part of any real property situated in this state which was acquired with the rents, issues or income of, the proceeds from, or in exchange for, property acquired as or which became, and remained, community property under the laws of another jurisdiction, or property traceable to that community property.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(1).

**391.215 Rebuttable presumptions.**

In determining whether KRS 391.210 to 391.260 applies to specific property the following rebuttable presumptions apply:

- (1) Property acquired during marriage by a spouse of that marriage while domiciled in a jurisdiction under whose laws property could then be acquired as community property is presumed to have been acquired as or to have become, and remained, property to which KRS 391.210 to 391.260 applies; and
- (2) Real property situated in this Commonwealth and personal property wherever situated acquired by a married person while domiciled in a jurisdiction under whose laws property could not then be acquired as community property, title to which was taken in a form which created rights of survivorship, is presumed not to be property to which KRS 391.210 to 391.260 applies.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(2).



**391.220 Disposition upon death.**

Upon death of a married person, one-half (1/2) of the property to which KRS 391.210 to 391.260 applies is the property of the surviving spouse and is not subject to testamentary disposition by the decedent or distribution under the laws of succession of this Commonwealth. One-half (1/2) of that property is the property of the decedent and is subject to testamentary disposition or distribution under the laws of succession of this Commonwealth. With respect to property to which KRS 391.210 to 391.260 applies, the one-half (1/2) of the property which is the property of the decedent is not subject to the surviving spouse's right to elect against the will.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(3).

**391.225 Perfection of title of surviving spouse.**

If the title to any property to which KRS 391.210 to 391.260 applies was held by the decedent at the time of death, title of the surviving spouse may be perfected by an order of the probate court or by execution of an instrument by the personal representative or the heirs or devisees of the decedent with the approval of the probate court. Neither the personal representative nor the court in which the decedent's estate is being administered has a duty to discover or attempt to discover whether property held by the decedent is property to which KRS 391.210 to 391.260 applies, unless a written demand is made by the surviving spouse or the spouse's successor in interest.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(4).

**391.230 Perfection of title of personal representative, heir, or devisee.**

If the title to any property to which KRS 391.210 to 391.260 applies is held by the surviving spouse at the time of the decedent's death, the personal representative or an heir or devisee of the decedent may institute an action to perfect title to the property. The personal representative has no fiduciary duty to discover or attempt to discover whether any property held by the surviving spouse is property to which KRS 391.210 to 391.260 applies, unless a written demand is made by an heir, devisee, or creditor of the decedent.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(5).

**391.235 Purchaser for value or lender.**

If a surviving spouse has apparent title to property to which KRS 391.210 to 391.260 applies, a purchaser for value or a lender taking a security interest in the property takes his interest in the property free of any rights of the personal representative or an heir or devisee of the decedent. If a personal representative or an heir or devisee of the decedent has apparent title to property to which KRS 391.210 to 391.260 applies, a purchaser for value or a lender taking a security interest in the property takes his interest in the property free of any rights of the surviving spouse. A purchaser for value or a lender need not inquire whether a vendor or borrower acted properly. The proceeds of a sale or creation of a security interest shall be treated in the same manner as the property transferred to the purchaser for value or a lender.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(6).

**391.240 Creditors' rights.**

KRS 391.210 to 391.260 does not affect rights of creditors with respect to property to which KRS 391.210 to 391.260 applies.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(7).

**391.245 Acts of married persons.**

KRS 391.210 to 391.260 does not prevent married persons from severing or altering their interests in property to which KRS 391.210 to 391.260 applies.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(8).

**391.250 Limitations on testamentary disposition.**

KRS 391.210 to 391.260 does not authorize a person to dispose of property by will if it is held under limitations imposed by law preventing testamentary disposition by that person.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(9).

**391.255 Uniformity of application and construction.**

KRS 391.210 to 391.260 shall be so applied and construed as to effectuate the general purpose to make uniform the law with respect to the subject of KRS 391.210 to 391.260 among those states which enact it.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(10).



**391.260 Title.**

KRS 391.210 to 391.260 may be cited as the Uniform Disposition of Community Property Rights at Death Act.

**History:** Created 1974 Ky. Acts ch. 328, sec. 1(11).

**392.090 All Property Claims or Curtesy Barred by Divorce or Adultery**

Note the limits in (2).

**392.090 All property claims or curtesy barred by divorce or adultery.**

- (1) Absolute divorce bars all claim of either husband or wife to the property, real and personal, of the other after his or her decease.
- (2) If either spouse voluntarily leaves the other and lives in adultery, the offending party forfeits all right and interest in and to the property and estate of the other, unless they afterward become reconciled and live together as husband and wife.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. secs. 2133, 2144.

**394.065      Validity of Trust, Devise or Legacy Not Affected By Specified Provisions**

There is no need to fund a revocable trust, or to have multiple beneficiaries, for it to be valid

**394.065 Validity of trust, devise or legacy not affected by specified provisions.**

- (1) No writing declaring and creating a trust, including a life insurance trust, when otherwise valid, shall be an invalid trust or a testamentary disposition of property because the grantor of the trust reserves to himself: (a) the income of the trust estate for his life, or any other period, or the right to receive the income of the trust estate or have it used for his benefit for his life, or any other period, whether at the grantor's direction or in the trustee's discretion; and/or (b) the right to receive amounts of the trust principal or have such amounts used for his benefit whether at the grantor's direction or in the discretion of the trustee; and/or (c) the right, at any time during his lifetime, to modify, alter, amend or revoke the trust instrument, in whole or in part; and/or (d) the right, at any time during his lifetime, to make recommendations to or direct the trustee as to any or all investments of the trustee and any or all administrative or other functions of the trustee.
- (2) Subsection (1) above shall be applicable to all writings executed after its enactment and to all writings previously executed if the grantor is living at the time of its enactment.

**History:** Created 1964 Ky. Acts ch. 128, sec. 1(2) and (3).

**394.076      Uniform Testamentary Additions to Trust Act**

1(a) allows a pour-over to an unfunded trust.

**394.076 Uniform testamentary additions to trust act.**

- (1) A will may validly transfer property to the trustee of a trust:
  - (a) Established during the testator's lifetime by the testator, by the testator and one (1) or more other persons, or by one (1) or more other persons, including a funded or unfunded life insurance trust, although one (1) or more persons other than the trustee have reserved any or all rights of ownership of the insurance contracts; or
  - (b) Established at the testator's death by the testator's transfer to the trustee, if the trust is identified in the testator's will and its terms are set forth in a written instrument, other than a will, executed before, concurrently with, or after the execution of the testator's will or in another individual's will if that other individual has predeceased the testator, regardless of the existence, size, or character of the corpus of the trust.
- (2) A transfer referred to in subsection (1) of this section shall not be invalid because the trust is amendable or revocable, or because the trust was amended after the execution of the will or the testator's death.
- (3) Unless the testator's will provides otherwise, property transferred to a trust in accordance with subsection (1) of this section shall not be held under a testamentary trust of the testator but shall become a part of the trust to which it is transferred. The property shall be administered and disposed of in accordance with the provisions of the governing instrument setting forth the terms of the trust, including any amendments to it made before or after the testator's death.
- (4) Unless the testator's will provides otherwise, a revocation or termination of the trust before the testator's death shall cause the devise or bequest to lapse.
- (5) This section shall be effective for any devise or bequest made by wills of decedents dying on or after July 15, 1998.
- (6) This section shall be construed to effectuate its general purpose to make uniform the law of those states that enact it.
- (7) This section may be cited as the Uniform Testamentary Additions to Trusts Act.

**Effective:** July 15, 1998

**History:** Created 1998 Ky. Acts ch. 415, sec. 10, effective July 15, 1998.

**394.070      Appointment by Will in Exercise of a Power – When Valid**

This appears to say that if a power of appointment by its terms is exercisable by a Will executed a certain way, the special requirements for execution do not have to be complied with.



**394.070 Appointment by will in exercise of a power — When valid.**

No appointment made by will in the exercise of any power shall be valid, unless the same is so executed that it would be valid for the disposition of the property to which the power applies if it belonged to the testator; and every will so executed shall be a valid execution of a power of appointment by will, even if the instrument creating the power expressly requires that a will made in execution of such power be executed with some additional or other form of execution or solemnity.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 4829.

**394.310      Original Will May Be Withdrawn From Court, When**

**You can take the Will with you!**

**394.310 Original will may be withdrawn from court, when.**

The District Court before which a will has been probated may permit any person interested to withdraw the will temporarily upon proper terms, if it is shown that the original will is necessary as evidence in any proceeding pending in a foreign government, or in any state of the United States. A copy of the will shall always be retained and entered upon the records of the court permitting the withdrawal.

**Effective:** January 2, 1978

**History:** Amended 1976 (1st Extra. Sess.) Ky. Acts ch. 14, sec. 365, effective January 2, 1978. -- Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 4866.

## **Interpretation of Wills**

- 394.400      Issue of Dead Devisee or Legatee Take Parent's Share**
- 394.410      Death of Part of Group of Devisees Before Testator – Children Includes Grandchildren**

Note (2).

- 394.520      Specific Legacy - When Payable**
- 397.1002      Requirement of Survival by One Hundred Twenty (120) Hours**

Obviously, many cases interpret these statutes and similar issues.

394.400 points out the need to condition bequests on survivorship if that is intended and, generally, to provide default takers. Note (2) in 394.410.

394.520 applies to Wills. If a specific bequest of a pecuniary amount is moved from the Will to the revocable trust, what duties does trustee have to distribute?

**394.400 Issue of dead devisee or legatee take parent's share.**

If a devisee or legatee dies before the testator, or is dead at the making of the will, leaving issue who survive the testator, such issue shall take the estate devised or bequeathed, as the devisee or legatee would have done if he had survived the testator, unless a different disposition thereof is made or required by the will.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 4841.

**394.410 Death of part of group of devisees before testator – Children includes grandchildren.**

- (1) When a devise is made to several as a class or as tenants in common, and one (1) or more of the devisees die before the testator, and another or others survive the testator, the share or shares of such as so die shall go to his or their descendants, if any; if none, to the surviving devisees, unless a different disposition is made by the devisor.
- (2) A devise to children embraces grandchildren when there are no children, and no other construction will give effect to the devise.
- (3) If a devise is made to several as joint tenants with right of survivorship and one (1) or more of the devisees dies before the testator and another or others survive the testator, the share or shares of such as so die shall go to such as so survive. Provided, however, in the event of the death of all the joint tenants before the death of the testator, the order of death of the joint tenants shall not affect the devolution of the property and, in this case, devolution shall be governed by subsection (1) hereof, as if the devise had been made to the deceased devisees as tenants in common.

**Effective:** October 1, 1942

**History:** Amended 1972 Ky. Acts ch. 168, sec. 14. – Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 2064.

**394.520 Specific legacy — When payable.**

If no time is fixed for the payment of a specific pecuniary legacy, it shall be payable one (1) year after the probate of the will, and carry interest after due.

**Effective:** July 15, 1980

**History:** Amended 1980 Ky. Acts ch. 259, sec. 16, effective July 15, 1980. --  
Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat.  
sec. 2065.

**397.1002 Requirement of survival by one hundred twenty (120) hours.**

Except as provided in KRS 397.1006, if the title to property, the devolution of property, the right to elect an interest in property, or the right to exempt property, homestead, or family allowance depends upon an individual's survivorship of the death of another individual, an individual who is not established by clear and convincing evidence to have survived the other individual by one hundred twenty (120) hours is deemed to have predeceased the other individual. This section shall not apply if its application would result in a taking of intestate estate by the state.

**Effective:** July 15, 1998

**History:** Created 1998 Ky. Acts ch. 415, sec. 2, effective July 15, 1998.





**395.020      Executor Not to Act Until Will Probated – Exception**

What does “take care of and preserve” mean in the last sentence?

**395.020 Executor not to act until will probated – Exception.**

The person named in a will as executor shall not act as executor to any extent until the will or an authenticated copy of the will is admitted to record, and he has executed bond and taken oath in the court in which the record is made. He may, however, provide for the burial of the testator, pay the reasonable funeral expenses, and take care of and preserve the estate.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 3886.

**446.060**

**Writings – Signature must Be at End – to Be in English**

With respect to (1), if a holographic Will is signed in the middle, is the first half valid because the signature is at the end of the first half?

With respect to (2), is a non-English holographic Will not valid?

**446.060 Writings – Signature must be at end – To be in English.**

- (1) When the law requires any writing to be signed by a party thereto, it shall not be deemed to be signed unless the signature is subscribed at the end or close of the writing.
- (2) Every writing contemplated by the laws of this state shall be in the English language.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 468.

**287.380      Deposits by Minors**

Ok, so you don't need to know but I've always wondered.

Similarly, **287.385, Education Loans to Minors -- Validity.**

**287.380 Deposits by minors.**

When any deposit is made by a minor, in his name, the bank may pay to him the amount deposited.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 591.

**287.385 Educational loans to minors – Validity.**

For the purpose of borrowing money from a state or national bank for their own higher educational purposes, the disabilities of nonage of minors are removed for all purposes, whether male or female. Any minor is authorized to make and execute any and all promissory notes, contracts, or other instruments necessary to be executed by him in order to borrow money for his own higher educational purposes, and such promissory notes, contracts, or other instruments shall have the same force and effect as though they were the obligations of persons over the age of their majority. Any promissory note, contract, or other instrument entered into by any such person pursuant to the provisions of this section shall have the approval of the parent or guardian of such minor and of the financial officer of the institution of higher learning.

**Effective:** July 15, 1998

**History:** Amended 1998 Ky. Acts ch. 196, sec. 14, effective July 15, 1998. -- Created 1964 Ky. Acts ch. 185, sec. 1.





By its terms the statute does not apply to retirement plans or IRAs. However, federal common law may reach the same result. See Egelhoff v. Egelhoff, 532 U.S. 141, 121 S.Ct. 1322 (2001); Addison v. Metropolitan Life Insurance Company, 5 F.Supp.2d 392 (W.D.Va. 1998).

What does “unless otherwise disposed of” mean? If the bequest is “to A if living, if not to B” and A killed the decedent? Does the bequest go to B?

**381.280 Forfeiture of right to property for killing decedent.**

If the husband, wife, heir-at-law, beneficiary under a will, joint tenant with the right of survivorship or the beneficiary under any insurance policy takes the life of the decedent and is convicted therefor of a felony, the person so convicted forfeits all interest in and to the property of the decedent, including any interest he would receive as surviving joint tenant, and the property interest so forfeited descends to the decedent's other heirs-at-law, unless otherwise disposed of by the decedent.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 1406a.

## **Provisions Dealing With Aliens**

- 381.300      Realty of Nonresident Alien Liable to Escheat After Eight Years Unless He Becomes Citizen**
- 381.310      Spouses and Children of Citizens – Property Rights**
- 381.320      Aliens Right as to Personalty – as to Realty if Resident**
- 381.330      Nonresident Alien – Rights as to Real Property Inherited**

**381.300 Realty of nonresident alien liable to escheat after eight years unless he becomes citizen.**

- (1) Except as otherwise provided in this chapter, the real estate of a nonresident alien may be escheated to the state at any time after the expiration of eight (8) years after the time he acquires title thereto.
- (2) Any alien who has purchased, or contracted to purchase, any real estate, or who holds or has title thereto, and who becomes a citizen of the United States before the property is escheated, and any purchaser, lessee, heir, or devisee, from him, if a citizen of the United States, who becomes the owner thereof by purchase or inheritance before the property is escheated, shall take and hold the property free and released from any right or claim of the state by reason of such person's having been an alien.

**Effective:** July 13, 1984

**History:** Amended 1984 Ky. Acts ch. 275, sec. 1, effective July 13, 1984. — Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 335.

**381.310 Spouses and children of citizens -- Property rights.**

Any person whose spouse is a citizen of the United States, and any person whose father or mother, at the time of his birth, was a citizen thereof, although born out of the United States, may take and hold real or personal estate by devise, purchase, descent, or distribution.

**Effective:** October 1, 1942

**History:** Amended 1974 Ky. Acts ch. 386, sec. 70. -- Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 336.

**381.320 Alien's right as to personalty — As to realty if resident.**

Any alien, not an enemy, may take and hold any personal property except chattels real. If such alien resides within this state he may take and hold any lands for the purposes of residence, or of occupation by him or his servants, or for the purpose of any business, trade, or manufacture, for as long as he remains a resident of the state. An alien so taking and holding shall have like rights, remedies and exemptions concerning such property as if he were a citizen of the United States.

**Effective:** July 13, 1984

**History:** Amended 1984 Ky. Acts ch. 275, sec. 2, effective July 13, 1984. -- Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 337.

**381.330 Nonresident alien – Rights as to real property inherited.**

If real estate passes to a nonresident alien by descent or devise, such property may be held and alienated by such nonresident alien for eight (8) years after the final settlement of the decedent's estate from which it was acquired. If such heir or devisee is a minor, the real estate may be held for his benefit by a guardian or curator, and may be sold by proper proceeding had in conformity with the laws regulating sales of infant's real estate, if commenced within such eight (8) years.

**Effective:** October 1, 1942

**History:** Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 338.





## **Trustee Investments**

### **386.020      Authorized Investments of Trust Funds – Fiduciary to Account for Profits**

The “legal list.” Note 1(g) in particular: dividend paying securities only.

### **386.800      Definitions**

### **386.810      Powers of Trustees Conferred By This Chapter**

### **386.820      Power of Court to Permit Deviation and to Approve Transactions Involving Conflict of Interest**

The prudent man rule, including the power of deviation under 386.820(1). This is a security by security approach.

### **287.110      Investment of Funds Held in Fiduciary Capacity – Capital Stock Liable for Fiduciary Obligations**

Corporate trustees must invest as provided by law for “other trust funds.”

### **287.277      Standards for Bank or Trust Company Acting as Fiduciary**

Prudent Investor Rule. Applies to corporate Trustees only. This is a portfolio approach.

### **287.272      Investment of Fiduciary Assets in Company or Trust Associated with Investing Institution – Fee**

Can invest in affiliates.

**386.020 Authorized investments of trust funds -- Fiduciary to account for profits.**

- (1) Any fiduciary holding funds for loan or investment may invest them in:
  - (a) Bonds or other interest-bearing obligations of the federal government;
  - (b) Bonds, state warrants and other interest-bearing obligations of this state;
  - (c) Obligations issued separately or collectively by or for federal land banks, federal intermediate credit banks and banks for cooperatives under the Act of Congress known as the Farm Credit Act of 1971, 85 Stat. 583, 12 U.S.C. Sec. 2001 and amendments thereto;
  - (d) Notes and bonds secured by mortgage or trust deed insured by the federal housing administrator, obligations issued or insured by the federal housing administrator, and securities issued by national mortgage associations;
  - (e) Obligations representing loans and advances of credit that are eligible for credit insurance by the federal housing administrator, and the fiduciary may obtain such insurance;
  - (f) Loans secured by real property or leasehold, that the federal housing administrator insures or makes a commitment to insure, and the fiduciary may obtain such insurance;
  - (g) Real estate mortgage notes, bonds and other interest-bearing or dividend-paying securities, including securities of any open-end or closed-end management type investment company or investment trust registered under the Federal Investment Company Act of 1940 or units of common trust funds managed by the fiduciary, which would be regarded by prudent businessmen as a safe investment. The fact that the fiduciary is providing services to the foregoing investment company or trust as investment advisor, custodian, transfer agent, registrar or otherwise shall not preclude the fiduciary from investing in the securities of such investment or trust;
  - (h) Real estate, after obtaining the approval of the District Court for such investment;
  - (i) Life insurance, endowment and annuity contracts issued by legal reserve companies authorized to do business in this state, after obtaining the approval of the District Court for such investment. Said fiduciary may select any optional settlement provided in a policy maturing by death or as an endowment;
  - (j) Notes, other interest-bearing obligations, and purchases of participations in such instruments, that are guaranteed in whole or in part by the United States of America or by any agency or instrumentality thereof;
  - (k) Certificates of deposit and savings accounts of any state or national bank whose deposits are insured by the Federal Deposit Insurance Corporation and whose main office is in this state, including itself, if such fiduciary is a bank. Such investments shall be insured by the Federal Deposit Insurance Corporation and the amount of the investments shall not exceed the limits of insurance of the Federal Deposit Insurance Corporation; and

- (1) United States government securities or United States government agency securities, the payment of the principal and interest on which the full faith and credit of the United States is pledged, said investments being made under the terms of a repurchase agreement between the fiduciary and any state or national bank whose main office is in this state, including itself, if such fiduciary is a bank.
- (2) Fiduciaries holding funds for loan or investment may make loans with the securities named in subsection (1) as collateral.
- (3) The fiduciary shall account for all interest or profit received.

**Effective:** July 13, 1990

**History:** Amended 1990 Ky. Acts ch. 450, sec. 1, effective July 13, 1990. -- Amended 1986 Ky. Acts ch. 391, sec. 1, effective July 15, 1986. -- Amended 1980 Ky. Acts ch. 134, sec. 1, effective July 15, 1980. -- Amended 1976 (1st Extra. Sess.) Ky. Acts ch. 14, sec. 325, effective January 1, 1978. -- Amended 1976 Ky. Acts ch. 107, sec. 3. -- Amended 1970 Ky. Acts ch. 267, sec. 1. -- Amended 1962 Ky. Acts ch. 133, sec. 1. -- Amended 1960 Ky. Acts ch. 155, sec. 1. -- Amended 1954 Ky. Acts ch. 52, sec. 1. -- Amended 1950 Ky. Acts ch. 171, sec. 1. -- Amended 1944 Ky. Acts ch. 111, sec. 1. -- Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. secs. 4706, 4706a, 4706-6, 4706-7.

### **386.800 Definitions.**

As used in KRS 386.805 to 386.840:

- (1) "Trust" means an express trust created by a trust instrument, including a will, whereby a trustee has the duty to administer a trust asset for the benefit of a named or otherwise described income or principal beneficiary, or both; "trust" does not include a resulting or constructive trust, a business trust which provides for certificates to be issued to the beneficiary, an investment trust, a voting trust, a security instrument, a trust created by the judgment or decree of a court, a liquidation trust, or a trust for the primary purpose of paying dividends, interests, interest coupons, salaries, wages, pensions or profits, or employee benefits of any kind, an instrument wherein a person is nominee or escrowee for another, a trust created in deposits in any financial institution, or other trust the nature of which does not admit of general trust administration;
- (2) "Trustee" means an original, added, or successor trustee;
- (3) "Prudent man" means a trustee whose exercise of trust powers is reasonable and equitable in view of the interests of income or principal beneficiaries or both, and in view of the manner in which men of ordinary prudence, diligence, discretion, and judgment would act in the management of their own affairs.

**History:** Created 1976 Ky. Acts ch. 218, sec. 44.

**386.810 Powers of trustees conferred by this chapter.**

- (1) From time of creation of the trust until final distribution of the assets of the trust, a trustee has the power to perform, without court authorization, every act which a prudent man would perform for the purposes of the trust including but not limited to the powers specified in subsection (3).
- (2) In the exercise of his powers including the powers granted by this chapter, a trustee has a duty to act with due regard to his obligation as a fiduciary, including a duty to give consideration to available tax exemptions, deductions, or credits for tax purposes. "Tax" includes, but is not limited to, any federal, state, or local income, gift, estate, or inheritance tax.
- (3) A trustee has the power, subject to subsections (1) and (2) of this section:
  - (a) To collect, hold, and retain trust assets received from a trustor until, in the judgment of the trustee, disposition of the assets should be made; and the assets may be retained even though they include an asset in which the trustee is personally interested;
  - (b) To receive additions to the assets of the trust;
  - (c) To continue or participate in the operation of any business or other enterprise, and to effect incorporation, dissolution, or other change in the form of the organization of the business or enterprise;
  - (d) To acquire an undivided interest in a trust asset in which the trustee, in any trust capacity, holds an undivided interest;
  - (e) To invest and reinvest trust assets in accordance with the provisions of the trust or as provided by law;
  - (f) To deposit trust funds in a bank, including a bank operated by the trustee;
  - (g) To acquire or dispose of an asset, for cash or on credit, at public or private sale; and to manage, develop, improve, exchange, partition, change the character of, or abandon a trust asset or any interest therein; and to encumber, mortgage, or pledge a trust asset for a term within or extending beyond the term of the trust, in connection with the exercise of any power vested in the trustee;
  - (h) To make ordinary or extraordinary repairs or alterations in buildings or other structures, to demolish any improvements, to raze existing or erect new party walls or buildings;
  - (i) To subdivide, develop, or dedicate land to public use; or to make or obtain the vacation of plats and adjust boundaries; or to adjust differences in valuation on exchange or partition by giving or receiving consideration; or to dedicate easements to public use without consideration;
  - (j) To enter for any purpose into a lease as lessor or lessee with or without option to purchase or renew for a term within or extending beyond the term of the trust;
  - (k) To enter into a lease or arrangement for exploration and removal of minerals or other natural resources or enter into a pooling or unitization agreement;

- (l) To grant an option involving disposition of a trust asset, or to take an option for the acquisition of any asset;
- (m) To vote a security, in person or by general or limited proxy;
- (n) To pay calls, assessments, and any other sums chargeable or accruing against or on account of securities;
- (o) To sell or exercise stock subscription or conversion rights; to consent, directly or through a committee or other agent, to the reorganization, consolidation, merger, dissolution, or liquidation of a corporation or other business enterprise;
- (p) To hold a security in the name of a nominee or in other form without disclosure of the trust, so that title to the security may pass by delivery, but the trustee is liable for any act of the nominee in connection with the stock so held;
- (q) To insure the assets of the trust against damage or loss, and the trustee against liability with respect to third persons;
- (r) To borrow money to be repaid from trust assets or otherwise; to advance money for the protection of the trust, and for all expenses, losses, and liability sustained in the administration of the trust or because of the holding or ownership of any trust assets, for which advances with any interest the trustee has a lien on the trust assets as against the beneficiary;
- (s) To pay or contest any claim; to settle a claim by or against the trust by compromise, arbitration, or otherwise; and to release, in whole or in part, any claim belonging to the trust to the extent that the claim is uncollectible;
- (t) To pay taxes, assessments, compensation of the trustee, and other expenses incurred in the collection, care, administration, and protection of the trust;
- (u) To allocate items of income or expense to either trust income or principal, as provided by law, including creation of reserves out of income for depreciation, obsolescence, or amortization, or for depletion in mineral or timber properties;
- (v) To pay any sum distributable to a beneficiary under legal disability, without liability to the trustee, by paying the sum to the beneficiary or by paying the sum for the use of the beneficiary either to a legal representative appointed by the court, or if none, to a relative;
- (w) To effect distribution of property and money in divided or undivided interests and to adjust resulting differences in valuation;
- (x) To employ persons, including attorneys, auditors, investment advisors, or agents to advise or assist the trustee in the performance of his administrative duties; to act without independent investigation upon their recommendations; and instead of acting personally, to employ one (1) or more agents to perform any act of administration, whether or not discretionary;
- (y) To prosecute or defend actions, claims, or proceedings for the protection of trust assets and of the trustee in the performance of his duties;

- (z) To execute and deliver all instruments which will accomplish or facilitate the exercise of the powers vested in the trustee.

**History:** Created 1976 Ky. Acts ch. 218, sec. 46.



**386.820 Power of court to permit deviation and to approve transactions involving conflict of interest.**

- (1) KRS 386.805 to 386.840 do not affect the power of a court of competent jurisdiction for cause shown and upon petition of the trustee or affected beneficiary and upon appropriate notice to the affected parties to relieve a trustee from any restrictions on his power that would otherwise be placed upon him by the trust or by this chapter.
- (2) If the duty of the trustee and his individual interest or his interest as trustee of another trust, conflict in the exercise of a trust power, the power may be exercised only by court authorization (except as provided in KRS 386.810, subsections (3)(a), (d), (f), (r), and (x)) upon petition of the trustee. Under this section, personal profit or advantage to an affiliated or subsidiary company or association is personal profit to any corporate trustee.

**History:** Created 1976 Ky. Acts ch. 218, sec. 48.

**287.110 Investment of funds held in fiduciary capacity – Capital stock liable for fiduciary obligations.**

Funds held in a fiduciary capacity shall be invested under the order of the court, or in such manner as may be provided by law for the investment of other trust funds, and the capital stock shall be primarily liable for the obligations of the corporation in its fiduciary capacity.

**Effective:** July 15, 1996

**History:** Amended 1996 Ky. Acts ch. 338, sec. 12, effective July 15, 1996. -- Amended 1984 Ky. Acts ch. 324, sec. 14, effective July 13, 1984. -- Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. sec. 614.

**287.277 Standards for bank or trust company acting as fiduciary.**

- (1) Notwithstanding the provisions of any other law, a bank empowered to act as a fiduciary or trust company, when investing, reinvesting, purchasing, acquiring, exchanging, selling, and managing property held in a fiduciary capacity, shall act as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the fiduciary account.
- (2) The standard described in subsection (1) of this section requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the account portfolio and as part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the account.
- (3) In making and implementing investment decisions, the bank or trust company has a duty to diversify the investments of the account unless, under the circumstances, it is prudent not to do so.
- (4) In addition, the bank or trust company shall:
  - (a) Conform to fundamental fiduciary duties of loyalty and impartiality;
  - (b) Act with prudence in deciding whether and how to delegate authority and in the selection and supervision of agents; and
  - (c) Incur only costs that are reasonable in amount and appropriate to the investment responsibilities of the account.
- (5) The duties of the bank or trust company under this section are subject to the rule that in investing the funds of the account, the bank or trust company:
  - (a) Has a duty to the beneficiaries of the account to conform to any applicable statutory provisions governing investment by fiduciaries; and
  - (b) Has the power expressly or impliedly granted by the terms of the account or applicable instrument and has a duty to the beneficiaries of the account to conform to the terms of the account directing or restricting investments by the bank or trust company.

**Effective:** July 15, 1996

**History:** Created 1996 Ky. Acts ch. 338, sec. 6, effective July 15, 1996.

**287.272 Investment of fiduciary assets in company or trust associated with investing institution – Fee.**

- (1) Notwithstanding any other law, a bank empowered to act as a fiduciary or a trust company, to the extent that it exercises investment discretion as a fiduciary, custodian, managing agent, or otherwise with respect to the investment and reinvestment of assets that it holds in a fiduciary capacity, may invest and reinvest the fiduciary assets in an investment company or investment trust established, owned, or controlled by the bank or trust company or an affiliate of the bank or trust company.
- (2) The fact that the bank or trust company, or any affiliate of the bank or trust company, is providing services to the investment company or trust as investment advisor, sponsor, distributor, custodian, transfer agent, registrar, or otherwise, and receiving reasonable remuneration for the services, does not preclude the bank or trust company from investing in the investment company or trust.
- (3) The bank or trust company making an investment of fiduciary assets in the investment company or investment trust may charge a reasonable fee for investment advisory, brokerage, transfer agency, register, management, or other similar services provided to the investment company. The fee may be in addition to the compensation which the bank or trust company is otherwise entitled to receive from the fiduciary account provided that the fee is disclosed at least annually, by prospectus, account statement, or any other written means to all persons entitled to receive statements of account activity.
- (4) As used in subsection (1) of this section, "affiliate of the bank or trust company" means any bank, trust, or other entity that controls, is controlled by, or is under common control with the bank, trust company, or other entity.

**Effective:** July 15, 1996

**History:** Created 1996 Ky. Acts ch. 338, sec. 4, effective July 15, 1996.



**287.275      Limits on Liability of Bank or Trust Company Acting as Fiduciary**

Corporate trustee is protected if there is an advisory committee. The drafting issue is whether you want to protect the corporate trustee in all circumstances. This is an extraordinarily broad statute.

**287.220      Corporate Fiduciaries Subject to Laws Governing Individuals – Security on Bonds – Ability to Serve as Trustee of Multiple Trusts with Common or Nonidentical Beneficiaries**

Note (3). Overrules one interpretation of 386.820(2).

**287.275 Limits on liability of bank or trust company acting as fiduciary.**

- (1) When an instrument, under which a bank empowered to act as a fiduciary or trust company acts, reserves in the grantor, or vests in an advisory or investment committee or in one (1) or more other persons, any power, including, but not limited to, the authority to direct the acquisition, disposition, or retention of any investment or the power to authorize any act that the bank or trust company may propose, the fiduciary is not liable, either individually or as a fiduciary, for either of the following:
  - (a) Any loss that results from compliance with an authorized direction of the grantor, committee, person, or persons; or
  - (b) Any loss that results from a failure to take any action proposed by the bank or trust company that requires the prior authorization of the grantor, committee, person, or persons if the bank or trust company timely sought but failed to obtain that authorization.
- (2) The bank or trust company referred to in subsection (1) of this section is relieved from any obligation to perform investment reviews and make recommendations with respect to any investments to the extent the grantor, an advisory or investment committee, or one (1) or more other persons have authority to direct the acquisition, disposition, or retention of any investment.
- (3) This section shall not apply to the extent that the instrument, under which the bank or trust company referred to in subsection (1) of this section acts, contains provisions that are inconsistent with this section.

**Effective:** July 15, 1996

**History:** Created 1996 Ky. Acts ch. 338, sec. 5, effective July 15, 1996.

**287.220 Corporate fiduciaries subject to laws governing individuals – Security on bonds – Ability to serve as trustee of multiple trusts with common or nonidentical beneficiaries.**

- (1) When acting as a fiduciary or in any other capacity in which the duties, powers, liabilities, rights, and compensation are regulated by law, or under the control or supervision of the court, banks and trust companies shall, except as provided in subsections (2) and (3) of this section, be subject to the same duties and responsibilities, have the same rights and powers, and receive the same compensation as is allowed the individual holding or exercising similar offices or trusts.
- (2) Upon all bonds required to be executed by such corporation before any court, the capital stock shall be the only security required for the faithful performance of its duties, unless the court or officer before whom the bond is executed, or some party in interest demands additional security.
- (3) A bank or trust company serving as a trustee of multiple trusts having one (1) or more common beneficiaries or remainder beneficiaries, need not obtain court approval for performance or execution of its duties, and it shall not be considered a conflict of interest solely because all beneficiaries or remainder beneficiaries of the trusts are not identical.

**Effective:** July 14, 2000

**History:** Amended 2000 Ky. Acts ch. 440, sec. 3, effective July 14, 2000. – Recodified 1942 Ky. Acts ch. 208, sec. 1, effective October 1, 1942, from Ky. Stat. secs. 598b-4, 611.





# **THE BASICS OF FIDUCIARY LIABILITY**

## **Can You Risk Proof A Fiduciary?**

*Tawana Edwards  
The Glenview Trust Company  
Louisville, Kentucky*

Copyright 2002. Tawana Edwards. All Rights Reserved.

**SECTION G**



## **THE BASICS OF FIDUCIARY LIABILITY**

### **Can You Risk Proof A Fiduciary?**

Why are fiduciaries more vulnerable to risk? .....	G-1
How can fiduciaries minimize risk? .....	G-2
1. Asset Information .....	G-3
2. Co-Fiduciary .....	G-4
3. Asset Control .....	G-4
4. Clear Dispositive Scheme .....	G-4
5. Termination Clause .....	G-4
6. Successor Fiduciary Provisions .....	G-4
7. Investment Provisions .....	G-4
8. Resignation Provisions .....	G-4
9. Tax Provisions .....	G-5

#### **Appendix:**

SR 96-10 (SPE), April 24, 1996: Risk-Focused Fiduciary Examinations .....	G-7
Successor Fiduciary Provisions .....	G-15



## **Risk – the chance of harm or loss.**

Today much is written and discussed regarding fiduciary risk, whether the discussion concerns the activities of a Board of Directors with respect to their company, or an ERISA trustee concerning plan assets and plan participants, or a financial institution acting as trustee or investment manager for an individual. Why so much discussion now? Have the risks involved changed or increased? Are there new risks? What makes fiduciaries more vulnerable to risks than others? Finally, what can fiduciaries do to mitigate risks?

The trust and investment business continues to be a very competitive and increasingly complex business. The competitive environment and rapid growth have enhanced the opportunity for risk as trustees develop new products, additional services with higher service standards or operational efficiencies. The traditional risks associated with serving as a fiduciary probably have not changed significantly in the last decade. Those risks include transactional type risks associated with potential financial losses, such as lost securities or misappropriation of funds. Traditional type risks exposing the fiduciary to loss also include self dealing, conflicts of interest, errors, omissions, fraud, improper use of trust assets, improper or unsuitable investment decisions. All potentially exposing the fiduciary to loss. But, the complexity of the business has increased. Fiduciary investing utilizes more sophisticated investment vehicles. Also, the delivery of fiduciary services is increasingly dependent on new information systems and technologies.

Several years ago, in response to this changing risk situation, various regulatory agencies expanded their examination programs to specifically assess risk management practices in the fiduciary activities of an institution. For a discussion on that topic see the Supervisory Letter issued by the Federal Reserve Board in 1996, attached as Appendix A.

### *Why are fiduciaries more vulnerable to risk?*

I think one of the key reasons that trustees are more vulnerable to risk is simply “time”. Many trusts continue in existence for a very long period of time. Generally, a corporate fiduciary thinks this is a good thing. You collect fees longer, a long-term revenue stream. But in his article “Risk Management: Facing The Consequences” (Trusts & Estates, November 2000) Peter Bernstein reminds us there is a relationship between risk and time. He says, “As the time horizon expands, uncertainty increases because the range of possible outcomes widens as we look further and further into the future.” His comments

related specifically to investment decisions and time but I think it applies equally to all discretionary decisions made by a fiduciary. With many jurisdictions repealing the rule against perpetuities you may see more of these situations

Probably the most common reason for fiduciary vulnerability is the fact that beneficiaries often have diverse interests yet a trustee must serve all beneficiaries' interest. It is the age-old conundrum for a fiduciary. It is very difficult to keep everyone happy. The competing interest of beneficiaries in a split interest trust will continue to create the potential for disagreements and possibly litigation. .

Finally, last but not least, a fiduciary generally is required to be properly capitalized to serve as a fiduciary. This capitalization creates the relatively deep pocket that can be very attractive to an eager litigant.

Certain types of decisions carry greater risk. Obviously discretionary decisions by the fiduciary carry greater risk. This is the very reason why so many corporate fiduciaries do not want to serve if they are required to exercise any discretion other than investment discretion. But, eliminating fiduciary discretion is not the answer to minimizing risk. In fact eliminating discretion may reduce the effectiveness and therefore eventually the use of trusts.

#### *How can fiduciaries minimize risk?*

This may sound exceedingly elementary but the first step to minimizing risk is to read and understand the governing document (i.e. the will or trust). In so many instances I have found the answer just be reviewing the document. Generally if the fiduciary is acting in accordance with the document the risk is minimized. But clearly it is not that simple. Unfortunately the documents cannot possibly anticipate every interpretive situation that might arise during the continuance of the fiduciary relationship. But still, every effort should be made to determine that you are within the scope of authority granted to the fiduciary in the governing document.

A fiduciary can also minimize risk by developing and following written policies and procedures. Any time you have two or more individuals working to deliver fiduciary services having written policies and procedures that are consistently followed, will minimize risk. This is true because there is some protection in consistency, even if the action was not perfect.

The policies and procedures should be thorough and cover every action of the fiduciary from marketing the products to the termination of an account. Obviously, the policies should be based on applicable laws and regulations to provide accurate guidance. There

are many good publications with sample fiduciary policy and procedure manuals. I have used Trust Department Administration and Operations (Matthew Bender) and Trust Department Policies and Procedures Manual, Sheshunoff Information Services, Inc. 2002. I found both to be very useful.

The written operational procedures should be specific and include directions and guidelines for completing all transactions. The procedure should require complete records of the administration of each account and provide which documentation should be retained and in what file. While it is important that the activities of the fiduciary be documented, it is also important to keep the files clean and businesslike. You should assume that every piece of paper could potentially be printed in the newspaper or appear as evidence in litigation. Once the policies and procedures are in place and have been disseminated and explained you should also implement a schedule for updating and reviewing the policies and procedures.

Once the policies and procedures are developed they should be followed. Kentucky law provides that it is negligent if performance fails to follow the written policy. In fact, these policies may actually be used against you to substantiate your liability. An example is found in the Kentucky case of Thomas v. Turner, Ky. App. 736 S.W. 2d 343. In Thomas v. Turner, the Court of Appeals was reviewing a decision of the Circuit Court that had authorized the bank as trustee to transfer real estate (an asset of the trust) to a company that was owned by a director of the bank. The appellate court in ultimately deciding against the bank indicated "the bank's own trust policies prohibit selling trust real estate when the potential for appreciation is high even though the current income production is low." (p.344). Then again, at page 345 of the opinion, "the bank's own trust policies rail against self-serving practices and conflicts of interest." Several different attorneys have suggested it would be better to have NO policies than to have out of date (dust covered) policies that no one knows or follows. However, all regulatory agencies that supervise trust activities for financial institutions will require written policies and procedures.

One of the most obvious ways for a fiduciary to manage risk is to control the type of business that is accepted. The initial step in a risk management process is the review of prospective business. Whether an individual or a committee performs the review, the function of reviewing potential business is a vital step in managing risks. In today's competitive market there is a tendency to close the sale, then ask questions. But, this can be very dangerous since liability attaches upon acceptance. Conversely, in an attempt to control risk some corporate fiduciaries have determined certain accounts will never be accepted. Both are extremes and adequate review process that is consistently utilized is a better solution for the fiduciary and the client. Some of the major points to be considered in this initial review include the following:

1. Asset Information. Current financial statements should accompany the discussion drafts of the documents to permit a risk investment review before the account is accepted. Obviously, in this step the fiduciary should look for "risky"



assets such as property environmentally at risk, assets or liabilities that may create conflicts of interest with the fiduciary (example loans with the commercial side of the bank).

2. Co- Fiduciary. If it is a co fiduciary situation determine whether the duties of each are delineated. Does the document specify which fiduciary controls in the event there is a disagreement? Is a dissenting fiduciary exonerated?
3. Asset Control. If the fiduciary will be responsible for assets in the control of another does the document protect the fiduciary accordingly? If not, can adequate protections be arranged or control changed.
4. Clear Dispositive Scheme. Determine whether all the beneficiaries are identified clearly and unambiguously in the document. Try to avoid from the beginning any potential involvement in litigation to “interpret” dispositive provisions.
5. Termination Clause. Is the language clear? Will the fiduciary understand at what point in time their responsibility ends?
6. Successor Fiduciary Provisions. When considering a successor fiduciary appointment ask yourself “if the current fiduciary can not handle this trust properly, will I be able to do so, what will I need to do differently and can I do that?” If the decision is made to accept this appointment as successor, the document should have language relieving the successor fiduciary of the obligation to review and correct the actions of the prior fiduciary and to protect the successor from liability for the actions of the prior fiduciary. Sample language is included in Appendix B.
7. Investment Provisions. Are the investment powers clear? The document should not only include standards by which the fiduciary’s actions will be measured but also include additional provisions that are necessary to adequately address any special circumstances such as stock restrictions or an ongoing business, etc. with which the fiduciary feels comfortable and clearly understands. Are the authorized investments broad enough to cover the type of assets you will likely purchase for the trust. If not, does the governing law give the needed authority?
8. Resignation Provisions. Can you bail out if need be? The greater the specificity as to all matters pertaining to resignation, the better. Is the language clear on how the successor trustee will be appointed in the event the present trustee resigns? Without appropriate authority or reason, the act of resigning can expose the fiduciary to liability for breach of fiduciary duty.

9. Tax Provisions. To discuss all the appropriate tax provisions necessary in fiduciary documents is beyond the scope of this outline. However, documents should specifically exonerate the fiduciary from liability for making tax decisions that may (or will definitely) adversely affect one or more classes of beneficiaries in favor of another class of beneficiaries.

Once the initial acceptance review is completed and you have decided it is safe, in fact good business, to accept the trust is there a need for any further review? It is sound fiduciary practice to establish some form of periodic review. . This review would include periodically check to determine whether policies and procedures are being followed, and whether duties are being performed within the guidelines or standards established in the policies. In this manner you are self-auditing and can locate and correct errors or omissions before others find them. At the risk of stating the obvious, it is far less expensive to find and correct your own mistakes than to have those mistakes discovered by a disgruntled beneficiary.

Another key component of managing risk is product analysis. Review the fiduciary services being provided to clients. Include an evaluation of the risks involved in delivering those services. Re-examine what is involved in delivering the service (i.e. the number of people involved, the costs associated with the service, the expertise required, any losses or charge offs sustained on the service). Is this service being delivered profitably? Before you decide to deliver an additional product or service go through the same analysis.

Client communication is another key to minimizing risk. Obviously if you are able to keep all your clients happy you have a reduced risk of litigation. Generally, satisfied clients do not sue you for breach of fiduciary duty, etc. Of course that does not mean a fiduciary can or should always to whatever a beneficiary desires in order to keep the beneficiary happy. There are times when the beneficiary's request is beyond the trustee's authority in the document. However, even in those instances face to face communication with all the beneficiaries on a regular basis to keep them informed of developments and decisions will often avoid most of the potential controversies that typically arise. This is especially true of investment actions. Whether or not a fiduciary has full discretion, communication of investment decisions and actions, before implementing them will often avoid future controversy. I am not suggesting the fiduciary request beneficiary approval (unless it is required by the document or the particular circumstance). However, a beneficiary/client who might otherwise resent the entire trust being invested in a family of mutual funds may fully appreciate the wisdom of the decision if it is effectively communicated in advance. When communicating with the client avoid "institutional arrogance". Remember to whom the \$\$\$\$\$\$ belongs.

**In addition to frequency of communication, also consider the method of communication and let your client drive that choice. Does the client understand the statements? Are charts and graphs a better choice for a particular client and words for another?**

**In conclusion, you may not be able to “risk proof” the fiduciary but you can minimize risk. Do so by utilizing written policies and procedures, performing initial reviews prior to accepting the fiduciary appointment, understanding whether the service can be delivered effectively and profitably through product analysis and increase communication with your client/beneficiaries. Not only will the risk be minimized but you will likely have better satisfied clients also**

# EXHIBIT A



**BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM**

WASHINGTON, D. C. 20551

**DIVISION OF BANKING  
SUPERVISION AND REGULATION**

**SR 96-10 (SPE)  
April 24, 1996**

**TO THE OFFICER IN CHARGE OF SUPERVISION  
AT EACH FEDERAL RESERVE BANK**

**SUBJECT: Risk-Focused Fiduciary Examinations**

Recent changes in the nature and complexity of fiduciary activities, both in the United States and abroad, have underscored the need to revise the focus and emphasis of fiduciary examinations in order to assess better a banking organization's ability to manage effectively the risks associated with fiduciary activities and ensure the prudent conduct of those activities. The changes include rapid growth in fee-based products and service globalization, the increasing dependence on new information systems and communications technologies, whether developed in-house or outsourced, and the heightened demand in the fiduciary area for more sophisticated investment products. These changes have, to some extent, diminished the line separating commercial banking and fiduciary activities.

The Federal Reserve's fiduciary examinations have traditionally focused on risks associated with compliance, financial management and operations, and the fiduciary's duty of undivided loyalty to the trust beneficiaries. Much of the examination was oriented to specific transactions and their compliance with statutory or regulatory requirements where noncompliance could result in defined penalties such as those authorized by ERISA and the Internal Revenue Code. The financial management and operations review focused on activities associated with possible financial losses that occur due to error, omission, fraud or accident that result from lost securities, misappropriation of funds, and mispostings, for example. Some fiduciary risk arises from the potential that a fiduciary could violate its duty of loyalty to the trust's principals or beneficiaries resulting in possible losses to the fiduciary from settlements and litigation. For example, the improper use of trust assets, possibly for personal gain, and improper or unsuitable investment decisions can expose the fiduciary to material loss or litigation.

Given the changes in the industry noted above, the Federal Reserve's fiduciary examination current focus is being expanded to look more intensively at risk management practices and related aspects of a banking organization's trust activities. This will result in, among other things, (1) greater use of a more diversified examiner population including those with capital markets, information systems, and safety and soundness experience<sup>1</sup>, (2) a stronger emphasis on an assessment of the individual organization's unique risk profile, and (3) a thorough review of risk identification, measurement, monitoring and control. This enhanced focus is consistent with the guidance provided to examiners and distributed to state

member banks and bank holding companies in SR 95-51, issued November 14, 1995, "Rating the Adequacy of Risk Management Processes and Internal Controls at State Member Banks and Bank Holding Companies." The letter calls for the rating of a bank's risk management practices taking into consideration credit, market, liquidity, operational, legal and reputational risks, all of which are pertinent to fiduciary activities as well. The attachment to that letter indicates that a bank's "...risk management systems should also encompass the organization's trust and fiduciary activities..."<sup>2</sup>.

Based on the need to enhance the examination process in order to adapt to these changes, a System Task Force on Reengineering Trust Supervision has developed a fiduciary examination approach that is more intensively focused on evaluating risk, assessing management's internal controls to limit risk, and integrating both the pre-planning, assessment stage and the on-site findings into the overall safety and soundness evaluation of a banking organization. In designing this approach, particular attention was directed to ensuring that examiners continue to emphasize the unique nature of the risks inherent in fiduciary activities as they relate to the fiduciary's "duty of undivided loyalty" to the trust customer which requires placing the interests of the customer above those of the institution.

### **Risk Profile of Fiduciary Activities**

The risk-focused fiduciary examination and supervision process centers around the preparation and upkeep of individualized risk profiles by the Reserve Bank for organizations that engage in a significant volume of fiduciary activities<sup>3</sup>. The appropriate scope of the fiduciary examination, particularly for the largest banking organizations, would be influenced by an assessment of the information contained in the risk profiles<sup>4</sup>. Where appropriate, coordinated interdistrict examiner pooling arrangements or other System initiatives would be used to provide the most effective resources to address the particular fiduciary risks and safety and soundness risks within the banking organization. Examinations would focus resources on the activities that pose the most substantive risk as detailed in each institution's profile and would be influenced by prior examination findings as well. In this way, it is expected that a more thorough understanding of each institution's unique risks and risk controls will develop.

The banking organization's efforts to identify, measure, monitor and control risk through implementation of specific policies, procedures, internal controls and management information systems will then be assessed and tested during the examination. Conclusions should be discussed with bank management, and, in the case of the more complex institutions at a minimum, should be incorporated into the safety and soundness report of examination.

As indicated in SR 95-51, and consistent with the greater emphasis given to risk management in Federal Reserve examination and supervisory policy statements, System examiners have been asked to assign a rating for risk management practices and assign that rating significant weight when evaluating the banking organization's management. Similarly, effective with the commencement of new examinations, trust examiners are instructed to assign a formal supervisory rating to an institution's risk management processes including its internal controls pertaining to fiduciary activities<sup>5</sup>. The specific rating of risk management and internal controls should be given significant weight when evaluating the "Supervision and Organization" component as part of the overall trust rating<sup>6</sup>.

## **Risk Focus**

With the adoption of the System's risk-focused examination approach for fiduciary activities, it is anticipated that in a complex institution, fiduciary examiners will direct more of their attention to assessing the organization's functions and its ability to identify, measure, monitor and control fiduciary, market, credit and operational risks. In particular, examiners should assess risks that result from the fiduciary's investment management, investment advisory, mutual funds, global custody, and securities lending and processing activities, and any other activities that are subject to adverse movements in market rates or prices, or to operating problems associated with processing a large volume of securities. These fiduciary activities could result in material losses to trust customers and, in turn, expose the institution to financial losses and litigation if not conducted in a manner consistent with the fiduciary's duty of loyalty and the investor's stated objectives. Recently, some of these fiduciary activities conducted at several large banking organizations have led to actual or potential customer losses and, rather than risking litigation or potentially exposing the organization to business reputation impairment, these banking organizations elected to absorb the losses directly.

A review of internal controls and policies and procedures will continue to be an integral part of the examination program. Greater attention to management competence and accountability, to management's review of risks associated with the introduction of new products and services and to its overall risk awareness will constitute other significant facets of the examination.

This emphasis on risk assessment and control parallels the guidelines and procedures pertaining to state member bank examinations and bank holding company inspections that are contained in SR 95-51, and recognizes the efforts of many progressive institutions in establishing fiduciary risk assessment and control initiatives of their own. Along these lines, when rating the quality of risk management of fiduciary activities, examiners should place primary consideration on findings relating to the following elements of a sound risk management system: (1) active board and senior management oversight, (2) adequate policies, procedures, and limits, (3) adequate risk measurement, monitoring and management information systems, and (4) comprehensive internal controls. Each of these elements is described further below, along with a list of considerations relevant to assessing the adequacy of each element.

▲ [Return to top](#)

### **Active Board and Management Oversight**

Given that boards of directors have ultimate responsibility for all of the activities of their institutions, they should approve overall fiduciary business strategies and policies including those related to identifying, measuring, monitoring and controlling fiduciary risks. The boards of directors must understand the nature of the risks significant to their organization and ensure that management is taking the steps necessary to manage these risks.

Senior management has the responsibility for implementing approved strategies in a way that will limit fiduciary risks and ensure compliance with laws and regulations. Senior management should, therefore, be fully involved in the fiduciary activities

of their institution and have sufficient knowledge of all fiduciary business lines to ensure that necessary policies, controls and risk monitoring systems are in place and that accountability and lines of authority are clearly set forth.

In assessing the quality of fiduciary oversight by boards of directors and senior management, examiners should consider whether these conditions exist:

The board and senior management have a clear understanding and working knowledge of the types of fiduciary activities performed by the institution and the risks inherent in them. They have approved appropriate policies, procedures, recordkeeping systems and reporting systems to support the fiduciary activities and to help measure and monitor risks. They have established procedures to keep them informed about changes in fiduciary activities and the associated risks.

Management at all levels provides adequate supervision of the daily activities of officers and employees to ensure that its lines of fiduciary business are managed and staffed by persons with knowledge, experience, and expertise consistent with the nature and scope of the organization's fiduciary activities.

Before offering new services or introducing new products, management identifies the fiduciary risks associated with them and ensures that internal controls are in place to manage the service or product and the accompanying risk.

### **Adequate Policies, Procedures and Limits**

An institution's directors and senior management should establish fiduciary and fiduciary risk management policies and procedures commensurate with the types of activities the institution conducts. The policies and procedures should provide enough detailed guidance to ensure that all material areas of fiduciary activity and risk are addressed. They should also be modified when necessary to respond to changes in the organization's activities. A smaller, less complex institution that has effective management which is heavily involved in daily operations generally would be expected to have more basic policies addressing the significant areas of its activities and setting forth a limited but appropriate set of requirements and procedures. In a larger institution, where senior management must rely on a widely-dispersed staff to implement strategies in a wide range of complex situations, far more detailed policies and related procedures would be expected.

In assessing the adequacy of an institution's fiduciary and fiduciary risk management policies and procedures, examiners should consider whether these conditions exist:

The institution's policies and procedures adequately address the fiduciary activities performed and are consistent with management's experience level and the institution's stated goals and objectives.

The institution's policies and procedures provide for adequate identification, measurement, monitoring and control of the risks posed by its fiduciary activities.

Policies clearly establish accountability and set forth lines of authority.

Policies provide for review of new fiduciary services and activities to ensure that they are suitable and consistent with fiduciary customer objectives, and that the systems necessary to identify, measure, monitor and control risks associated with new services and activities are in place before the activity is initiated.

### **Adequate Risk Monitoring and Management Information Systems**

Risk monitoring requires institutions to identify and measure all areas of material fiduciary risk on a continuous basis. To do so effectively, risk monitoring activities must be supported by information systems that provide senior management with timely reports on financial condition, operating performance, marketing efforts, new products and services, pending or threatened litigation and risk exposure arising from fiduciary activities. They also must provide regular and more detailed reports for managers engaged in the daily management of the institution's activities.

The sophistication of risk monitoring and control information systems should be commensurate with the complexity of the institution's fiduciary operations. Less complex institutions may require only a limited number of management reports to support risk monitoring activities. Larger, more complex institutions, however, would be expected to have much more comprehensive reporting and monitoring systems. These systems would allow for more frequent reporting and closer monitoring of complex activities.

In assessing the adequacy of an institution's measurement and monitoring of fiduciary risk, examiners should consider whether these conditions exist:

The institution's fiduciary risk monitoring practices and reports encompass all of its business lines and activities, and are structured to monitor exposures consistent with established goals, limits and objectives.

Key assumptions, data sources, and procedures used in identifying, measuring and monitoring fiduciary risk are appropriate for the activities performed by the institution and are adequately documented and tested for reliability on a continuous basis.

Reports to management are accurate and timely and contain sufficient information for policy and decision makers to identify any adverse trends and any potential or real problems. The reports must be adequate for them to evaluate the level of fiduciary risk faced by the institution.

▲ [Return to top](#)

### **Adequate Internal Controls**

A comprehensive internal control structure is critical to the safe and sound functioning of an institution and its fiduciary risk management system. Establishing and maintaining a system of internal controls that sets forth official lines of authority and appropriate segregation of duties is one of management's most important responsibilities.



A well structured system of internal controls promotes effective fiduciary operations and reliable reporting, safeguards assets, and helps to ensure compliance with laws, regulations, and institutional policies. Controls should be periodically tested by an independent party (preferably the auditor, or at least an individual not involved in the process being reviewed) who reports directly to either the institution's board of directors or one of its designated committees. Given the importance of appropriate internal controls to organizations of all sizes and risk profiles, the results of these reviews should be adequately documented, as should management's responses to them.

In evaluating the adequacy of an institution's internal controls as they relate to fiduciary activities, examiners should consider whether these conditions exist:

The system of internal controls is appropriate to the type and level of fiduciary activities.

The institution's organizational structure establishes clear lines of authority and responsibility.

Reporting lines provide sufficient independence of the control areas from the business lines and adequate separation of duties throughout the institution.

Financial, operational, and regulatory reports are reliable, accurate, and timely.

Adequate procedures exist for ensuring compliance with laws and regulations.

Internal audit or other control review practices provide for independence and objectivity.

Internal controls and information systems are adequately tested and reviewed with findings documented and weaknesses given appropriate and timely attention.

The board of directors and/or the audit committee reviews the effectiveness of internal audits and other control review activities on a regular basis.

The fiduciary risk assessment and control categories and tools listed above are not meant to be all inclusive but are guidelines for use by the fiduciary examiner and the fiduciary activities management in their risk assessment and control efforts. It is expected that adjustments to the list will be made as the risk-oriented examination approach continues to develop and be utilized. It is also expected that the examination of each individual institution may require some modification depending upon its organization and the complexity of the products and services offered.

### **Other Initiatives**

The Task Force is also reviewing fiduciary examination frequency guidelines to see if they need to be modified. In addition, the trust examination handbook will be changed as necessary to reflect the risk-focused examination approach.

Should you have any comments or questions regarding this letter, please contact Howard Amer (ext. 2958) or Don Vinnedge (ext. 2717) at the Board.

James I. Garner  
Deputy Associate Director

**Cross reference:**

SR 95-51, Rating the Adequacy of Risk Management  
SR 95-22, Supervising Foreign Banking Organizations  
SR 95-17, Evaluating Risk Management in Nontrading Activities  
SR 94-53, Investment Adviser Activities  
SR 93-69, Evaluating Risk Management in Trading Activities  
SR 82-28, Trust Rating System

▲ [Return to top](#)

---

**Footnotes**

1. Consistent with the intent of SR 94-31, which provides state member banks the opportunity to have their fiduciary activities examined on a coordinated basis with the safety and soundness examination of the bank, the proposed increased use of a variety of examiners with various specializations during complex fiduciary examinations is meant to enhance the overall examination process. [Return to text](#)
2. This initiative is also consistent with guidance previously provided to examiners that was contained in SR 93-69 (Examining Risk Management and Internal Controls for Trading Activities of Banking Organizations), SR 94-53 (Investment Adviser Activities), SR 95-17 (Evaluating the Risk Management and Internal Controls of Securities and Derivatives Contracts Used in Nontrading Activities) and SR 95-22 dealing with ratings for U.S. offices of foreign banks. [Return to text](#)
3. Significant volume can be measured in relation to the bank's overall size or in relation to the volume of business conducted by the largest banking organizations. [Return to text](#)
4. The Task Force is also developing comparable guidance for use in supervising small banking organizations with noncomplex fiduciary activities. [Return to text](#)
5. Consistent with SR 95-51, the assignment of a specific risk management rating of from 1 to 5 should be included on the Examiner's Comments page of the confidential section when using the trust examination report. Comments, conclusions and criticisms relating to risk management should be brought to the attention of management and should be presented in the open section on the "Supervision and Organization" page and, if warranted, on the open section Examiner's Comments page.

In those cases where the findings pertaining to fiduciary activities are integrated into a safety and soundness examination or inspection report of a state member bank, bank holding company or U.S. branch or agency of a foreign bank, the risk management comments and rating for fiduciary activities should be included on the respective open and closed section

pages that pertain to fiduciary activities and should also be considered and referenced when presenting the comparable subject matter for the overall organization. [Return to text](#)

6. The Uniform Interagency Trust Rating System (UITRS) is contained in SR 82-28 along with the Federal Reserve's Implementing Guidelines. In assigning risk management rating, no new component will be added to UITRS. [Return to text](#)

▲ [Return to top](#)

---

[Home](#) | [SR letters](#) | [1996](#)

[Accessibility](#)

To comment on this site, please fill out our [feedback](#) form.

**Last update: July 26, 2001 10:30 AM**

## **APPENDIX B**

### **SUCCESSOR FIDUCIARY PROVISIONS**

A successor trustee shall not be obligated to examine the accounts, records and acts of the previous trustee or trustees or any allocation of trust assets made by the previous trustee. Any successor trustee shall not be responsible for any act or omission to act on the part of any previous trustee or trustee.