Heckerling Highlights
Montgomery County Estates & Trusts Study Group
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Overview:

Heckerling 2019 did not, as in some past years, have an overarching theme where one topic took precedence over all others (such as in 2018, when developments under the new tax act were the primary concern). Additionally, the increased federal estate and gift tax credit amount (now $11.4 million for an individual and $22.8 million for a married couple) has, for many practitioners, lessened the emphasis on traditional estate and gift tax planning.

Partially as a consequence of the increased estate and gift tax credit, income and state tax planning has taken on increasing importance. One prominent topic was state taxation of trusts. There have been important recent developments in state and federal cases relating to the constitutional authority to levy taxes. This topic is significant from the planning and administration perspective, as many trust documents contain liberal "change of situs" provisions. Furthermore, in a mobile society, beneficiaries and trustees should be aware of the (possibly inadvertent) tax exposure consequences of relocation. This topic is also heavily related to the litigation arena, as the ability to obtain personal jurisdiction over a fiduciary can be a fundamental strategic concern.

Additionally, trust modification, construction, and reformation remains a prominent topic. With many existing documents geared towards the older, lower unified credit levels, there is arguably an increased demand for court intervention and modification in the administration of trusts to meet the needs of current beneficiaries. Court modification of irrevocable trusts, and the extent to which the IRS will recognize state court orders, are increasingly important. The Maryland Trust Act contains very liberal modification and reformation provisions, but the degree to which a state court modification will be recognized as valid by the IRS (or, in all likelihood, other federal agencies—for example, the SSA) is largely a matter of federal law.

Finally, the topic of trust protectors remains of great interest to both planners and litigators. The powers and standing of a trust protector to intervene in the administration of a trust have been the subject of litigation in recent years.

I. State law issues - *Quill*, *Wayfair*, Commerce Clause and Due Process

Setting the Stage: *South Dakota v. Wayfair, Inc.*, 138 S.Ct. 2080 (2018)

- South Dakota required retailers to collect and remit sales tax, but if not, then consumers were responsible for payment at the same rate. Under existing Commerce Clause precedent (*Quill Corp v. North Dakota*, 504 U.S. 298 (1992)) South Dakota could not require a business with no physical presence in the State to collect sales tax. However, consumer compliance rates are very low causing $50 million/year in lost revenue. Because of this, South Dakota enacted law requiring out of state sellers to collect and remit sales tax "as if the seller had a physical presence in the State." The law applied to sellers who annually delivered more than $100,000 of goods/services in the state or engaged in 200 or more separate transactions for the delivery of goods or services in to the state. Retailers who opposed the law relied on *Quill* and prevailed at the state court level, and the Supreme Court granted certiorari.
- The Supreme Court sided with South Dakota and expressly overruled *Quill*'s "physical presence" requirement. *Quill* had distinguished between Due Process "minimum contacts" analysis (which does not require a physical presence) and the Commerce Clause's requirement that a "substantial nexus" exist between the taxed economic activities and the state (which *Quill* said required a physical presence). The *Wayfair* Court eliminated *Quill*'s "physical presence" requirement, characterizing it as economically inefficient and essentially obsolete in the era of e-commerce. Notably, the Court observed that Due Process and Commerce Clause standards are not identical but they are "parallel."

Kimberley Rice Kaestner 1992 Family Trust v. North Carolina Department of Revenue, 814 S.E. 2d 43 (N.C. 2018)

- North Carolina attempted to tax the income of a trust based solely on the residence of the beneficiaries (who lived in North Carolina through tax years 2005 through 2008). The North Carolina statute said that the income tax on an estate or trust is computed on the amount of the taxable income of the estate or trust that is for the benefit of a resident in North Carolina. The issue was whether the Due Process "minimum contacts" test was satisfied.
- The trust at issue was created in New York with a New York settlor and (individual) Trustee. The initial Trustee was later replaced by an individual Trustee residing in Connecticut. The Connecticut Trustee remained in Connecticut throughout entire relevant period relating to the case, and trust was governed by New York law. One of the beneficiaries of the trust moved to North Carolina in 1997. In 2006, trust was divided into 3 separate for settlor's children, including the North Carolina beneficiary. The North Carolina beneficiary's separate trust was for her and her children, all of whom were North Carolina residents during years at issue.
- During the relevant years, assets were investments, custodians of assets were in Boston, Massachusetts. Documents relevant to trust kept in New York and all of tax returns and

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accountings were prepared in New York. The trust was fully discretionary. No distributions were made to the beneficiaries in North Carolina during tax years at issue, but the trust did make a loan to North Carolina beneficiary. The Trustee did send accountings of trust assets to beneficiary and she received legal advice from Trustee and his firm, and also met with him in New York.

- The North Carolina Supreme Court stated that, in reference to taxation power, the Due Process Clause requires some minimum connection and the person, property, or transaction it seeks to tax (citing *Quill*). It also requires that the income attributed to the State for tax purposes must be rationally related to values connected with the taxing state (citing *Quill* again). Minimum connection (or "minimum contacts") exists when the taxed entity "purposefully avails itself of the benefits of an economic market" in the taxing state even if it has no physical presence in the state. It is "essential in each case that there be some act by which the party purposefully avails itself the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws."
- The Trustee had taken no action directed towards North Carolina and unilateral action by beneficiary in moving to North Carolina was insufficient to give rise to the minimum connection for Due Process purposes. Contacts between Trustee and beneficiary (e.g., the meeting in New York) were not the same as contacts between Trustee and North Carolina and were fairly infrequent/irregular. Consequently, the trust's income was not subject to North Carolina taxation. The Court's holding was based on Due Process principles, not a Commerce Clause analysis.
- The U.S. Supreme Court granted North Carolina certiorari on January 11, 2019. The oral argument transcript can be found online at:

https://www.supremecourt.gov/oral_arguments/argument_transcripts/2018/18-457_4d46.pdf

Fielding v. Commissioner of Revenue, 916 N.W. 2d 323 (Minn. 2018)

- Four irrevocable inter vivos trusts were classified as "resident trusts" under Minnesota law. As a consequence, the worldwide income of the trusts were subject to Minnesota taxation.
- The four trusts were created by Minnesota domiciliary, were prepared by a Minnesota law firm, and were funded with nonvoting common stock of a Minnesota S-Corp. The original trustee was California domiciliary. The trusts were grantor trusts for first 30 months of their existence, and the grantor filed Minnesota tax returns during this period. On December 31, 2011, the grantor relinquished power to substitute assets in trusts, and the trusts ceased to be grantor trusts for income tax purposes.
- When the trusts switched to non-grantor status, the grantor was still domiciled in Minnesota. Because of this, the trusts became classified as "resident trusts" under the Minnesota statute. A Colorado domiciliary (an individual) became Trustee on January 1, 2012. The trusts continued to file Minnesota income tax returns in 2012 and 2013 without protest.

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- In 2014, a Texas domiciliary (an individual) became Trustee. The Minnesota S-Corp stock held by the trusts was sold. Three of the four trust beneficiaries did not live in Minnesota, and some of the trusts' income had no direct connection to Minnesota. The trust records were not kept in Minnesota (other than the documents prepared by the Minnesota law firm). The Trustee never traveled to Minnesota for trust business, and the trusts did not own any "physical property" in Minnesota.
- Minnesota taxes were imposed on the gain from the stock sale because of "resident trust" statute. If the trusts had not been deemed residents of Minnesota, those income items would have been assigned to the trusts' domicile and not subject to Minnesota income tax. The trusts filed 2014 Minnesota returns under protests and sought tax refunds for difference.
- In reviewing the "resident trust" statute, the Minnesota Supreme Court analyzed whether the domicile of grantor (the basis for the "resident trust" classification) was a sufficient connection with Minnesota to classify the trusts as "residents" and therefore tax all of their income. (It was undisputed that Minnesota could tax Minnesota sources of income.) The imposition of a tax will not violate Due Process if there is 1) minimum connection between state and the thing subject to tax and 2) income subject to tax is rationally related to benefits conferred on taxpayer by the state. Here, the contacts between Minnesota and the trusts were insufficient to satisfy Due Process and therefore the trusts could not be classified as Minnesota residents for tax purposes.
- As with *Kaestner*, the case was decided on Due Process grounds, and the Court did not reach the Commerce Clause issue. A petition for certiorari by Minnesota is pending with the U.S. Supreme Court.

Comptroller of the Treasury v. Taylor, 238 Md. App. 139 (2018)

- Testator died with a valid will creating a residuary marital trust, valued at about $2.3 million. At time of death, he and his wife were residents of Wayne County, Michigan. The Marital Trust gave a lifetime income interest to the wife. His estate filed a 706 claiming making a federal QTIP election over the amounts funding the marital trust.
- The wife lived in Michigan until 1993, then moved to Maryland and died in 2013. Her Personal Representative filed a 706 including the QTIP trust as part of her gross estate (which was $5.5 million). On the MET-1, the Personal Representative excluded the value of the Marital Trust, decreasing estate to $4.1 million. The Personal Representative explained this on the MET-1 saying that no MET-1 had been filed in Maryland for the husband on his death, and thus no Maryland QTIP election was made for the assets in the Marital Trust. The Maryland Comptroller disallowed exclusion of the Marital Trust from the wife's gross estate, and the tax court affirmed. The Circuit Court reversed the tax court.
- Md. Code, Tax-Gen § 7-301 is definition of Maryland taxable estate. It says that the "estate" includes the federal gross estate of the decedent, as augmented by § 7-309(b)(6)

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(Maryland QTIP property from first spouse's death, which would not necessarily be includible in the federal gross estate). Under § 7-301(d), the "Maryland estate" is the portion of the "estate" which Maryland has the power to tax. Under § 7-302, the Maryland estate tax applies to the transfer of the "Maryland estate."

- The Comptroller argued it was entitled to tax the "transfer" of the wife's income interest at her death, as she had been living in Maryland and enjoying the interest in the trust during life. The taxpayer argued that Maryland lacks authority to tax the QTIP because there was no transfer of assets at the wife's death. The transfer of assets occurred at the husband's death (when equitable and legal title changed) in Michigan.
- The Court of Special Appeals looked at distinction in § 7-301 between the "estate" and the "Maryland estate," which recognizes that there will be assets in the "estate" that Maryland has no power to tax. While 7-309(b)(6)(i) augments the "estate" with property for which a Maryland QTIP election is made, no Maryland QTIP election was made in this case. The Court of Special Appeals further agreed with taxpayer that the Marital Trust vested at the time of the testator's death, and therefore there was no "transfer" that Maryland had the power to tax, as the transfer had occurred at the husband's death.
- The Court of Special Appeals did not (explicitly) reach the issue of Due Process. The Court of Appeals granted certiorari in this matter in December 2018.

Observations:

1. Per *Wayfair*, there is no longer a need for a "physical connection" to form a "substantial nexus" for taxation under Commerce Clause. There already was no physical presence requirement for Due Process, per *Quill*.
2. *Fielding* and *Kaestner* cases actually did not address Commerce Clause issue. They relied solely on due process. *Taylor* indirectly addressed both Commerce Clause and Due Process issues in holding that the transfer at issue (into the Marital Trust) did not have a sufficient connection to Maryland to be subject to transfer tax.
3. The Due Process analysis for tax purposes focuses on whether the trusts, as separate taxable entities, had sufficient contacts with the state to have enjoyed services and protections from its laws (that are paid for by taxes). It is not enough for a beneficiary to live in a state (at least when the trust is fully discretionary) or for the trustee to send accountings and documents into the state. The analysis is still a little "analog" with the focus on the location of the Trustee.

Questions:

1. Mandatory distribution standard vs. discretionary distribution standard – would this make a difference if the beneficiary's distributions were mandatory? *Kaestner* implies this is a

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factor, as state law protects a state resident's property rights. Much of the Supreme Court oral argument concentrated on this point.

2. Due Process for litigation purposes vs. tax purposes – the tax Due Process test is a variation on the *International Shoe*/*Shaffer* analysis of minimum contacts and reasonableness, but it focuses largely on the extent to which the trust, as its own distinct "entity," has utilized state services. What about a trustee who has committed misconduct or otherwise harmed the interest of the beneficiary in the trust? There are non-tax cases involving trusts where Court has found sufficient minimum contacts with beneficiary's state even though trustee is not living there. E.g. *Lobato v. Herndon* 2017 W.L. 1185202 (D. Md. 2017). *Regnery v. Wallerich*, 626 F. Supp. 2d 872 (N.D. Ill. 2009); *Steen Seijo v. Miller*, 425 F. Supp. 2d 194 (D.P.R. 2006). This is in line with the *Calder v. Jones* "effects" test for intentional torts. (There is also contrary authority.) In addition to the constitutional analysis, the Maryland long-arm statute (Md. Code, Courts & Judicial Proceedings § § 6-103) must be satisfied.
3. Corporate trustee vs. individual trustee—in the above trust cases, the trustees were individuals. Under the *International Shoe*/*Shaffer* analysis, "continuous and systematic" contacts with the forum state can give rise to "general" personal jurisdiction, even when the contacts are not specifically related to the transaction or occurrence at issue. For a large corporate trustee with multiple trust-based contacts in the forum state—would analysis be different for tax or for litigation Due Process?

II. Trust Construction, Modification, and Reformation in light of *Bosch's Estate*

Commissioner v. Bosch's Estate, 387 U.S. 456 (1967)

- The question was whether IRS is bound by state court determination of property rights when it is not made a party to a proceeding. This case resolved two estate tax cases with arguably conflicting rulings.
  - Case 1 (*Commissioner v. Bosch's Estate*) - 1930 Revocable Trust, left decedent's wife a life estate and general power of appointment over principal of corpus. If the power was not exercised, ½ would go to husband's heirs and ½ to wife's. In 1951, wife executed instrument purporting to release general power and replace it with special power. When decedent died in 1957, the estate attempted to claim marital deduction over portion passing to wife's trust. IRS said that it did not qualify for the § 2056 deduction. The ultimate issue was whether the 1951 instrument was valid--if not (as wife claimed) then she retained the general power of appointment and the estate could take the marital deduction. A New York state court ruled that the release was a "nullity," and the US Court of Appeals held that the state court's determination controlled.

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- Case 2 (*Second National Bank v. United States*) - Testator died in 1958. The will directed payment from his residuary estate of any and all death taxes, contrary to any statute that directed apportionment. The residue was left in trust, ⅓ income to surviving spouse, other ⅔ to his grandchildren then living. In 1958 (before death), testator executed codicil giving wife general power of appointment over the widow's (portion of the) trust, to qualify it for marital deduction under IRC § 2056. In 1959, the estate claimed deduction over ⅓ of estate (widow's share) before any death taxes paid. IRS denied the deduction and reduced it by requiring that taxes be charged to the full estate prior to the claimed marital deduction. The taxpayer petitioned the state probate court to determine proration of estate taxes paid, the grandchildren consented, and notice was given to IRS. No objections were filed and the probate court found, despite the statement in will, that there was no direction against apportionment and thus the state apportionment statute applied, and ordered entire federal tax to be charged against grandchildren's trusts. The IRS brought suit. On appeal, US Court of Appeals said that the probate court was incorrect with respect to the state law and its determination was not binding on IRS.

- The Supreme Court first said that Court of Appeals' interpretation of the state law on apportionment in Case 2 would be upheld, as it deferred to the Court of Appeals on this matter of state law. The only issue remaining in both cases is whether a state court's determination of legal rights is binding on the IRS. The IRS argued that only an adversary proceeding in the state court should be binding.
- In neither proceeding was IRS a party and neither *res judicata* nor collateral estoppel applied. The legislative history of the federal marital deduction statute, which indicated that state court proceeding on interpretation of a will should be given "proper regard" if the proceeding was an "adversary proceeding"
- The Supreme Court said that where state's highest court has not spoken on point, lower court decisions are given weight (in case of intermediate appellate court, are presumptively correct) but are not controlling. Where the state's highest court has spoken on point, its decision is controlling. If there is no such decision, then the IRS should give "proper regard" to state's courts but is not required to follow them, and the IRS should effectively sit as its own "state court" to determine state law. The Supreme Court used this standard instead of one that relies on "adversarial" vs. "non-adversarial" because it would avoid confusion. Case 2 was reversed and Case 1 was remanded for proceedings with this opinion.

Maryland Modification and Reformation

Md. Code, Est. & Trusts 14.5-410

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(a) (1) A noncharitable irrevocable trust may be terminated on consent of the trustee and all beneficiaries if the court concludes that continuance of the trust is not necessary to achieve any material purpose of the trust.

(2) A noncharitable irrevocable trust may be modified on consent of the trustee and all beneficiaries if the court concludes that modification is not inconsistent with a material purpose of the trust.

(b) The existence of a spendthrift provision or similar protective language in the terms of the trust does not prevent a termination of a trust under subsection (a)(1) of this section.

(c) On termination of a trust under subsection (a)(1) of this section, the trustee shall distribute the trust property as agreed by the beneficiaries.

(d) If not all beneficiaries consent to a proposed modification or termination of the trust under subsection (a) of this section, the modification or termination may be approved by the court if the court is satisfied that:

(1) If all beneficiaries had consented, the trust could have been modified or terminated under this section; and

(2) The interests of a beneficiary that does not consent will be adequately protected.

NOTE: The concept of a trust's "material purpose" is difficult to define and not discussed extensively in Maryland case law. The "material purpose" requirement originates from the so-called *Claflin* rule, taken from *Claflin v. Claflin*, 20 N.E. 454 (Mass. 1889). See Unif. Trust Code § 411 Cmt. (explaining that the "material purpose" rule is derived from the *Claflin* doctrine). Under the *Claflin* doctrine, the following types of trust provisions generally demonstrate a "material purpose:" 1) spendthrift provisions; 2) a specified age at which the beneficiary is to receive his or her disbursement; 3) a distribution standard giving the trustee total discretion; or 4) provisions demonstrating that the trust is created for the sole purpose of supporting the beneficiary. Chester, Ronald, Modification and Termination of Trusts in the 21st Century: The Uniform Trust Code Leads A Quiet Revolution, 35 Real Prop. Prob. & Tr. J. 697 (Winter 2001) (quoting Dukeminier, Jesse & Stanley M. Johnson, Wills, Trusts, and Estates 854 (6th Ed. 2000))

Md. Code, Est. & Trusts 14.5-411:

(a) (1) The court may modify the administrative or dispositive terms of a trust or terminate the trust if, because of circumstances not anticipated by the settlor, modification or termination will further the purposes of the trust.

(2) To the extent practicable, the modification described in paragraph (1) of this subsection shall be made in accordance with the probable intention of the settlor.

(b) The court may modify the administrative terms of a trust if continuation of the trust on its existing terms would be impracticable or wasteful or impair the administration of the trust.

(c) On termination of a trust under subsection (a) of this section, the trustee shall distribute the trust property in a manner consistent with the purposes of the trust as ordered by the court.

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Md. Code, Est. & Trusts 14.5-413
The court may reform the terms of a trust, even if unambiguous, to conform the terms to the intention of the settlor if it is proved by clear and convincing evidence that both the intent of the settlor and the terms of the trust were affected by a mistake of fact or law, whether in expression or inducement.

Md. Code, Est. & Trusts 14.5-414
(a) To achieve the tax objectives of the settlor, the court may modify the terms of a trust in a manner that is not contrary to the probable intention of the settlor.
(b) The court may provide that the modification described in subsection (a) of this section has retroactive effect.

2018 Private Letter Rulings Relating to Modification, Reformation, and Construction

PLRs 201837005-201837009 & 201845029 (2018)

- Irrevocable trust for grandchildren and descendants. No generation skipping transfers had been made from trust.
- There were two "scrivener's errors" - 1) beneficiaries' withdrawal rights were not limited to gift tax exclusion amount, causing beneficiary to have a general power of appointment over the full contribution; and 2) there was no "hanging" Crummey power, but rather the withdrawal power lapsed in full on an annual basis.
- Lawyer wanted to reform trust to limit withdrawal rights to annual exclusion and to create a hanging Crummey power only causing the withdrawal right to lapse up to the greater of 5%/$5,000/year. Lawyer did a reformation in state court that was retroactive to date of trust's creation.
- The IRS said that 1) grandchildren do not have a general power of appointment except to the extent they have it under reformed instrument 2) reformation does not constitute exercise or release of the grandchildren's general power of appointment 3) lapse of grandchildren's withdrawal rights over contributions to trust did not result in gifts, and 4) the trust is not includible in grandchildren's estate other than the extent they can withdraw funds under the reformed trust instrument.
- The IRS relied on *Bosch's Estate* but said that the reformation was to correct scrivener's error, not change the underlying trust instrument.

PLRs 201814001 & 201814002

- Irrevocable pre-1985 trust grandfathered in as GST-exempt. Trust was f/b/o lineal descendants. Terms of trust were ambiguous, but settlor was still alive and attested at the time the trust was created, he only intended for it to benefit blood descendants.

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- The settlor sought declaratory judgments consistent with this intent, and the state court entered an order contingent on obtaining a private letter ruling stating that the judgments would not cause adverse tax consequences.
- The IRS said that there was a bona fide issue over whether adopted descendant qualified under the trust under state law, and the Court's order construing the trust was consistent with applicable state law that would be applied by highest law of the state.
- The IRS followed Reg. §26.2601-1(b)(4)(i)(C), which provides that a judicial construction of a governing instrument to resolve an ambiguity in the terms of the instrument or to correct a scrivener's error will not cause an exempt trust to be subject to the GST tax if the judicial action involves a bona fide issue and the construction is consistent with the applicable state law that would be applied by the highest court of the state (pursuant to Commissioner v. Estate of Bosch, 387 U.S. 456 (1967)).
- Here the declaratory judgment met the requirements of the regulations and the construction of the trusts would not affect the exempt status. The PLR also clarified that no transfer occurred for gift tax purposes, and there was no disposition of interest in the trust to trigger gain or loss.

PLR 201807001

- Between September 19, 1995 and August 20, 1996, Donor created an irrevocable trust which he intended to qualify as a grantor trust. Trust permitted distributions to Donor and Donor's issue during life. Donor, Donor's issue, Donor's spouse were not and never have been US citizens. Trust had provision that allowed independent trustee, with court approval, to reform any provision of the trust so that burdensome income tax consequences may be eliminated or modified.
- Before August 20, 1996, the trust was treated as a grantor trust. After that date, there was a change in federal law said that the grantor had to be a US citizen or US corporation for grantor trust rules to apply. IRC 671(f)(1). There was an exception, however, for trusts where the distributions were limited to the grantor or the grantor's spouse.
- The new law became effective on enactment, August 20, 1996, but had certain grandfather rules for trusts in existence on September 19, 1995 where additions or transfers to the trust before that date were grandfathered in. However, since the Donor had established the trust after the grandfather date, he was not allowed to be treated as "owner" of any portion of it since his descendants were beneficiaries and he was not US citizen.
- Donor sought a modification of the trust agreement to remove his descendants as beneficiaries. Both the Donor and his drafting attorney testified about the intent to qualify as a grantor trust when the trust was drafted. The state court concluded that the trust, as originally drafted, was based on a mistake of fact and law, and it modified the trust, deleting the descendants as beneficiaries. In the private letter ruling, the IRS said that the reformation of the trust was consistent with applicable state law and therefore the trust's

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"reformation" would be taken into account as of the date of formation for the purpose of determining whether it fell in the exception under 671(f) (i.e. whether deleting "the issue of Donor" made it again qualify as grantor trust).

PLRs 201803003, 201818005, 201820007, 201820008, 201825007 & 201845006

- An irrevocable trust was created prior to October 22, 1942, by parents for the benefit of Daughter. Daughter's only right was to receive distributions of net earnings, but not principal, awarded to her by the trustee with the consent of the advisory board of the trust and to distribution of the trust estate made by the trustee at the termination of the trust. At Daughter's death, her equitable interest was to pass to and vest in her heirs in accordance with the laws of descent and distribution then in force. The trust was to continue for Daughter's life and for a period of 21 years after her death at which time the trust would terminate and the trust corpus would be distributed to the beneficiaries.
- Certain of the children and grandchildren of Daughter sought a declaratory judgment concerning the impact of disclaimers they planned to make. The court ruled that Daughter and the successor beneficiaries all had a testamentary general power of appointment. A pre-October 22, 1942, power of appointment has adverse estate tax consequences only if it is exercised. Upon the death of Daughter or successor beneficiary, the heirs at law of that beneficiary would succeed to the beneficiary's interest in the trust. The court also ruled that after Daughter's death, each successor beneficiary would have three separate beneficial interests: (a) an income interest for 21 years after Daughter's death; (b) the remainder interest, which vested in possession 21 years after Daughter's death; and (c) a pre-1942 general power of appointment. The court ruled that each of those interests could be disclaimed independently of others.
- Several years later, Daughter proposed to partially release her general power of appointment to restrict the power in two respects. First, the power was to be exercisable only in favor of the Daughter's estate. Second, the power could only be appointed to take effect after her death. The intention of Daughter was to allow her power of appointment over the trust to lapse at her death.
- Subsequently, the trustee petitioned the supervising court, with the consent of Daughter and other beneficiaries, to provide that when the trust terminated 21 years after the death of Daughter, any share distributed to a beneficiary under a specified age was to be held in a continuing trust until that beneficiary reached the specified age. If that beneficiary survived Daughter but died before reaching the specified age, the beneficiary would have a general testamentary power of appointment causing the property to be included in the beneficiary's estate. The later petition also requested the court to modify the trust to allow for the administration of the separate trusts created after Daughter's death.
- The taxpayer requested the following rulings: 1) The power of appointment granted to the great-grandchildren who succeeded to Daughter's interest in the trust would be considered

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a pre-October 22, 1942, power of appointment, and the complete release or lapse of that power of appointment would not have any adverse estate, gift, or GST tax consequences; 2) The proposed disclaimer by any one or more of the great-grandchildren would be a qualified disclaimer under Section 2518 and would not have any adverse gift tax or estate tax consequences to the disclaimants and would not result in the loss of the GST exempt status of the trust; 3) The assets of a continuing trust created pursuant to proposed modification after Daughter's death would be included in the estate of the beneficiary if the beneficiary died before the termination of the continuing trust; 4) The proposed construction of the trust would not cause the trust to be subject to GST tax; 5) The proposed construction of the trust would not result in a taxable gift by any of the beneficiaries of the trust.

- With respect to the first ruling request, Daughter had a pre-October 22, 1942, general power of appointment to which the grandchildren would succeed when Daughter dies. To the extent that any grandchild disclaimed his or her interest in that power of appointment or died during the 21-year period following Daughter's death, some great-grandchildren might succeed to her power of appointment. Under the Section 2041 regulations, the power of appointment held by the great-grandchildren and more remote beneficiaries would be considered a power created before October 22, 1942, and consequently the release or lapse of such a power would not treated as the exercise of the power and would have no adverse estate or gift tax consequences.
- With respect to the second ruling request, Daughter's heirs cannot succeed to any interest in the trust until Daughter's death pursuant to the terms of the trust. Consequently, Daughter's great-grandchildren could disclaim their interest and there would be no adverse estate or gift tax consequences.
- With respect to the third ruling request, a beneficiary who survives Daughter but dies before reaching a specified age will have a general power of appointment over the continuing trust. If the beneficiary survives the 21-year term following Daughter's death but dies without exercising the power of appointment, the remaining assets in the continuing trust are to be distributed to the beneficiary's estate. Thus, the assets will be included in the gross estate of the continuing beneficiary for federal estate tax purposes if the beneficiary dies before the continuing trust terminates.
- With respect to the fourth ruling request, the proposed modifications would not have any adverse generation-skipping transfer tax consequences. The modification would fall within the scope of Reg. 26.2601-1(b)(4)(i)(D)(1), which provides that a modification of the governing instrument of an exempt trust is valid under applicable state law and will not have adverse GST consequences when the modification does not shift a beneficial interest to any beneficiary who occupies a lower generation than the person or persons who held the beneficial interest prior to the modification and the modification does not extend the time for the vesting of any beneficial interest in the trust beyond the period provided for in the original trust. That was the case here.

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- With respect to the fifth ruling request, because the proposed construction of the trust clarified ambiguous terms of the trust and reflected the rights of the parties under applicable law, the proposed construction of the trust would not result in a taxable gift by any of the beneficiaries of the trust.

III. Trust Protector – Standing

Carberry v. Kaltschmid, 2018 Cal. App. Unpub. LEXIS 3900, 2018 WL 2731898 (2018).

- The Court in this unpublished case ruled that a trust protector does not have standing to compel trustees to account.
- Husband created a trust for his widow and six children that became irrevocable upon his death in 2014. Two of his children were named as trustees. The original trust protector resigned in 2015 and he named a successor trust protector (who was not related to any of the beneficiaries).
- The trust terms provided that: (a) the protector acted in a fiduciary capacity; (b) the protector had the powers to amend or modify the trust (but not to expand its own powers), construe the trust in the event of an ambiguity, the power to sign documents to exercise its powers, the power to appoint a special trustee, the power to appoint successor trustees if there is a vacancy not filled by other trust terms, the power to terminate an uneconomical trust, and the power to change the trust situs and governing law; (c) the trustee had no duty to investigate the trustee's actions or inactions, audit the trust books, or evaluate portfolio performance; and (d) the protector was entitled to compensation.
- In January 2016, the protector wrote the trustee to inquire about a trust loan and the status of an ongoing dispute among the trustees and requested an accounting. Counsel for a trustee advised that the parties were working on a settlement. In February, the protector wrote another letter asking for the settlement agreement and stated that "as Trust Protector, I have a fiduciary duty to keep myself informed of the condition of the administration of the Trust". Counsel for a trustee responded that they were working with the family to resolve the disputes, and that counsel for the trustees and the beneficiaries agreed that the protector would not be accused of not fulfilling his duties if he placed his work on hold while the family worked on resolution.
- In September, the protector sued to compel the trustees to account and provide information (although the only "information" sought other than the accounting was a copy of the settlement agreement). The protector made allegations that the trust was delinquent with tax filings and had incurred high legal fees. He also sought confirmation of his ability to appoint a special trustee. A trustee opposed, arguing that: (a) the protector lacked standing to demand an accounting; (b) the high fees were the fees of the prior protector which were part of the dispute; (c) the parties were in mediation to resolve the trust disputes; and (d) that accountings had been provided to the beneficiaries.

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- The trial court dismissed the protector's claim for lack of standing and the protector appealed. On appeal, the court of appeals affirmed on the following grounds:
  - The probate code provides that a trustee is to provide accountings to beneficiaries and that a trustee or a beneficiary has standing to compel a trustee to account. The protector is not a beneficiary and there is no authority giving a non-beneficiary protector standing to compel an accounting.
  - The trust terms do not entitle the protector to compel an accounting. The trust terms require the trustee to account to the beneficiaries only. None of the powers granted to the protector include the power to compel an accounting.
  - The trial court was not required to grant an amorphous request that the court compel the trustees to communicate generally with the protector when no specific information was identified.
  - A concurring opinion noted that: (1) a law review article concluding that a trustee who has the power to remove a trustee has a duty to stay informed about the trust is irrelevant because this protector did not have the power to remove trustees; and (2) the authority granted the protector does not render the protector the functional equivalent of a trustee.

Drafting Point: Unlike the role of a Trustee, a Trust Protector does not have implied common law powers or duties. The Trust Protector's powers are governed by the instrument (and in some states, by statute). From a drafting perspective, the Trust Protector is more akin to an attorney-in-fact than a traditional fiduciary and the powers of a Trust Protector should be clearly articulated.

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David received his B.A. from Brigham Young University, magna cum laude and University Honors, in 2011 and his J.D. from George Washington University Law School, with honors, in 2014. He was admitted to the Maryland Bar in 2014.

David served on the Public Contract Law Journal at George Washington University Law School. During law school, he participated in the IRS Voluntary Income Tax Assistance Program. He is the Chair of the Estate and Trust Section for the Anne Arundel County Bar Association. He is a member of various local and national bar associations.

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Publications

Lawyers of the firm have published articles on tax and other topics related to their professional interests, including: "*Medicaid Planning for Maryland Family Lawyers,*" MARYLAND BAR JOURNAL, Vol. 49, No. 2 March/April 2016 (Co-Author with Phyllis J. Erlich); "*Self-Settled Asset Protection Trusts for Married Couples in Maryland*," Steve Leimberg's Asset Protection Planning Newsletter (April 2015); "*The Terms of the Trust: Extrinsic Evidence of Settlor Intent"* ACTEC JOURNAL, Spring 2014 (Co-author with Anna Katherine Moody); *"Benevolent Benefactors Be Aware: Changes in Medicaid Policy Result in Fairer Treatment of Gifts,"* MARYLAND BAR JOURNAL, Vol. 47, No. 3, May/June 2014 (Co-author with Laurie S. Frank); *"Is this the Death of Ahlborn? The Self-Defeating Expansion of States, Authority to Seek Reimbursement Under the Medicaid Secondary Payer Act,"* NAELA NEWS, February/March 2014 (Co-author with Jason A. Frank). *Resisting the Contractarian Insurgency: The Uniform Trust Code, Fiduciary Duty, and Good Faith in Contract,"* ACTEC JOURNAL, Winter 2010; *"Asset Protection and Tenancy by the Entirety,"* ACTEC JOURNAL, Spring 2009; *"Perfect Ambiguity: The Role of the Attorney in Maryland Guardianships,"* MARYLAND JOURNAL OF CONTEMPORARY LEGAL ISSUES, 1996.

Lectures/Course Presentations

Lawyers of the firm participated as a lecturers in various continuing education programs for lawyers, including: *"Succession Planning: Not Just for Senior Lawyers"* (MSBA 2018); *"A Survey of the Common Types of Fiduciary Litigation"* (University of Baltimore Law Forum 2018 Symposium); *"Estate Planning for Federal Employees"* (U.S. Census Bureau 2018); *"Deadman Statute and Hearsay Issues and Objections for Orphans' Court Judges"* (Judicial College of Maryland 2018); "*Elder Financial Abuse*: *2018 Update"* (MSBA 2018); "*Pesky and Persistent Evidentiary Issues in Estate & Trust Litigation"* (MSBA 2018); "*Contested Guardianships*" (NAELA Maryland-DC Chapter 2017); *"Transmittal of Issues from Orphans' Court to Circuit Court"* (Judicial College of Maryland 2016); *"ABA Section of Real Property, Trust & Estate Law Domestic Asset Protection Trust Planning: Jurisdiction Selection Series"* (eCLE, ABA 2015); *"Document Drafting for the Elder Law*

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Practitioner" (MSBA 2015); *"Orphans' Court Judges' Orientation,"* (Judicial Institute of Maryland 2015); *"Maryland Trust Act,"* (MSBA 2014); *"Heirs, Legatees and Related Issues,"* (Judicial Institute of Maryland 2013); *"Estate/Tax Implications of DOMA after the Windsor Case"* (MSBA 2013); *"Asset Protection, An Overview for Maryland Estate and Trust Lawyers,"* (MSBA 2013)*; A Beneficiary's Right to Information,"* (MSBA 2012); *"Trust Litigation: The Enforcement of Beneficiary Rights,"* (MSBA 2011); *"Asset Protection: An Overview for Maryland Estate and Trust Lawyers,"* (MSBA 2010); *"Back to the Future, <u>Schoukroun</u> and the Spousal Election,"* Hot Topics in Elder Law, (MICPEL 2009); *"A Match Made In Heaven – Using Tenancy by the Entirety for Creditor Protection Without Sacrificing Estate Planning,"* (MSBA 2009); *"Asset Protection – A Guide for Maryland Estate and Trust Lawyers,"* (MICPEL Advance Estate Planning Institute 2006); *"Revocable Inter Vivos Trusts,"* (MICPEL 2004 and 2006); *"Valuation Discounting,"* (MICPEL 2003; MSBA 2002 and 2003); *"Business Valuation,"* (MICPEL 1998); *"Family Partnerships,"* (MICPEL 1996); *"Avoiding Probate - Will Substitutes,"* 1996; *"Basic Estate Planning,"* (MICPEL 1993).

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