An Essential Estate Planning Checklist

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AN ESSENTIAL ESTATE PLANNING CHECKLIST

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I. Understand the Process

A. The Objectives of Estate Planning

- ☐ Complete disposition of the clients property at death
- ☐ Reduce the cost of dying
- ☐ Address "Living Probate"
- ☐ Reduce or eliminate family conflict
- ☐ Facilitate the administration of the client's estate
- ☐ Get Paid!!!

B. The Process

1. *First Phone Call* - The potential client will have several concerns.

- ☐ Are you the right attorney for the job?
- ☐ What are your hours?
- ☐ Where are you located?
- ☐ Is there parking?
- ☐ How much will this cost?

2. *First Meeting*

a. Preliminaries

- ☐ Prep the Client
- ☐ When clients come to your office for the first time make sure you make an effort to make them feel at home.
- ☐ Have your receptionist or secretary be prepared to greet them by name.
- ☐ Make a point not to be late or to keep them waiting.
- ☐ A little thing - update the reading material in your waiting area
- ☐ Dress appropriately.

b. Objectives

- Introduction
- Establish credibility
- Get information
- Determine game plan

c. Meeting follow up

- Draft internal memorandum memorializing the meeting for later reference
- Send planning letter with recommendations and fee statement.

3. Second Meeting

- Execute the documents
- Hypothetical probate

4. Follow Up

- Retitle assets
- Complete designations of beneficiary
- Retention of documents
- Periodic review

5. Getting Paid

a. How do you charge?

- Fee Letter
- Flat fee
- Hourly
- Retainer/ Payment Terms

b. For what do you charge?

- Drafting documents
- Titling assets
- Designation of beneficiary
- Expenses

c. Fee Letter

- Required by Rule 1.5

- State Clearly the Scope and Limitations of Your Representation
- State Clearly How and for What Your Client will be charged
- Include a Clause Waiving Conflicts if They Exist.

II. Getting Complete Information

A. Overview

Good estate planning must begin with Complete Information. Before beginning the estate planning process, you must first obtain

- Complete Background information
- Complete Family Information;
- Complete Family Information;
- Copies of existing Estate Planning Documents.
  - Wills
  - Trust
  - General Power of Attorney
  - Medical Power of Attorney
  - Living Will
  - Designations of Beneficiary
    - Life Insurance
    - Retirement Plans
    - Annuities

B. Complete Background Information

- Names
- Address
- Employment
- Contact Information
- Personal Telephone Number
- Employment Telephone Number
- Personal e-mail
- Employment – e-mail

- ☐ How do you wish to be contacted?
- ☐ Prior Marriages
- ☐ Property Settlement Agreement
- ☐ Pre- or Post Nuptial Agreement
- ☐ Prior Residences
- ☐ Citizenship
- ☐ In what state do you vote?
- ☐ In which state is your car registered?
- ☐ Do you own real estate outside Pennsylvania?
- ☐ In which state(s) do you pay income tax?
- ☐ In which state do you plan to retire?
- ☐ Prior residence in a community property state
- ☐ Military Service

C. Complete Family Information

- ☐ Heir's Names
- ☐ Address
- ☐ Ages
- ☐ Relationship
- ☐ Marital status
- ☐ Children
- ☐ Employment
- ☐ Special Concerns

D. Complete Financial Information

1. *Overview*

You must obtain a complete disclosure of the assets and liabilities of the client.

2. *Assets*

a. Categories

The general asset categories should include the following:

- ☐ Cash and Bank Accounts

- ☐ Notes and accounts receivable
- ☐ Bonds
- ☐ Listed stocks
- ☐ Closely-held business interests
- ☐ Real estate (including where the property is located)
- ☐ Life insurance and annuities
- ☐ Employee benefits
- ☐ Miscellaneous property (e.g., personal effects, collections, patents, trademarks, copy- rights, etc.)

b. Additional Information

Also obtain the following information:

- ☐ Value
- ☐ Adjusted cost basis
- ☐ Form of ownership

3. Liabilities

The information gathered should also include a list of the client's liabilities, such as the following:

- ☐ Real estate mortgages
- ☐ Notes to financial institutions
- ☐ Loans on life insurance policies
- ☐ Other obligations, such as charitable pledges, and tax liabilities.

4. Trusts/Powers of Appointment

In addition determine:

- ☐ If the client the beneficiary under any trust established by another
- ☐ If the client holds a power of appointment over any trust?

E. Other Facts that could impact the Dispositional Plan

- ☐ Property settlement agreements
- ☐ Pre- or post-nuptial agreements
- ☐ Issues with potential heirs

- ☐ Disabilities
- ☐ SSDI
- ☐ Troubled marriage
- ☐ Financial distress

F. Identify the People in Charge

- ☐ Executor
- ☐ Successor Executor
- ☐ Trustee
- ☐ Successor Trustee
- ☐ Guardian
- ☐ Successor Guardian

G. Powers of Attorney/Living Will

- ☐ Agent
- ☐ Successor
- ☐ Guardian to be named in the Power
- ☐ Successor Guardian
- ☐ HIPAA Disclosure
- ☐ Living Will

H. Determine if Federal Estate Tax is an Issue

- ☐ Is the estate in excess of the current federal estate tax exemption amount ($5,450,000; $10,900,000 for a married couple)

1. Step One.

Determine assets includible in the "gross estate" and their fair market value.

The "gross estate" includes all property in which the decedents had an interest at the time of death; including personal effects, investments, real property, life insurance at face value, annuities and the value in retirement plans. Joint property with the right of survivorship is taxed one-half in the estate of the first of the joint tenants to die. Also included is the value of certain property interests transferred by the decedent during lifetime in which the decedent retained an interest in or control over until death.

2. Step Two.

Add the amount of the decedent's post - 1976 taxable gifts not included in the gross estate.

Note: The inclusion of the donor's taxable gifts into the calculation is not intended to tax such gifts a second time. This step in the calculation merely serves to ”gross up” the taxable estate into a higher marginal tax bracket.

- Has either spouse been married previously to a now deceased spouse?
- Did the estate of a deceased spouse elect portability?
- What is the level of the Unused Basic Exclusions Amount, available to the estate of the surviving spouse?

III. Determining the Dispositive Plan

A. Determine the “Who”

- Primary heirs
- Contingent heirs
- Wipe Out
- Identify the “Who – NOT!!!”

B. Determine the “What”

- Specific Property
- Amount
- Percentage
- Probate or Non-Probate
- The Residue

C. Determine the “How”

- Outright
- In Trust
  - Minors
  - Special Needs
  - Other
- Conditional Gifts

A decedent may make a testamentary gift conditional upon the recipient’s doing or refraining from doing some clearly specified act. If the legatee or devisee fails to carry out the condition, the property passes to someone else. The condition may also relate

to the occurrence of some event over which the legatee may or may not have any actual control. Conditions imposed by persons in connection with the making of the testamentary instrument may take one of these forms:

- Those dealing with the existence or non-existence of the instrument itself;
- A conditional revocation of earlier instruments;
- A “no contest” or “in terrorem” clause affecting all legatees or devisees; and
- Conditional legacies or devises where conditions effect only the particular beneficiary.

In Pennsylvania, one’s right to dispose of his or her property has always been liberally construed. Accordingly, testators who are not under any obligation to make a gift may attach any conditions to the gift as he or she pleases, provided that the condition does not involve acts that are illegal or contrary to public policy. When the conditions in force are not fulfilled, the conditional gift will pass under the terms of a gift-over. If the condition is enforceable and there is no gift-over upon failure to satisfy the condition, the subject property will pass under residuary clause or by intestacy.

In Pennsylvania the following conditions have been recognized as valid:

- The personal application or appearance of the donee;
- Survival of the donee for a stated period of time;
- Remaining in testator’s employ;
- Continuing to reside with testator or wife after execution of the will;
- Releasing a claim;
- Giving up other property;
- Sobriety;
- Not electing against the will;
- Business capacity;
- Cessation of an illicit relationship;
- So long as he/she remains single;
- So long as he/she does not marry;
- A condition forbidding marriage to a limited segment of the population may be valid;
- A condition not intended to induce divorce but that merely provides protection for the legatee in the event that divorce occurs is valid.

In placing conditions of gifts, make sure they are reasonable and can be practically determined by the executor during the normal term of the administration of the estate. For example, a provision like the following might be better provided in a trust rather than a will:

"I give my library of books to my wife, until she remarries."

IV. Draft the Document

A. Drafting Tips

- *Start with a Form*

  Start with a form from a reliable source. Learn the form and know what it provides in every provision. Make the form your own –again, don't stop with the form; it is just a starting point. Add or change provisions as necessary.

- *Avoid Long Sentences and Use Outline Form*

  Don't use run on sentences and long paragraphs. This can create an unreadable document. This is a matter of style but I would recommend that you format your document in outline format. This helps you breakdown ideas in a logical way and also makes the document easier to read.

- *Number Pages and Paragraphs*

  It sounds fundamental, but numbering paragraphs and pages allows for easy reference in the document when you are reviewing it with the client or perhaps with someone else at a later date.

- *Get the Names Right*

  Again, it sounds fundamental, but getting the names wrong, particularly the name of the client's or the names of immediate family members, is one mistake you never want to make. It makes you look sloppy and inattentive to detail, and it is the one mistake everyone will notice.

- *Eliminate Gender References*

  Eliminate gender biased references. Avoid phrases, like the following:

  " …provided that if a person dies intestate as to all or any part of his estate property which he gave …

  And replace it with the following when appropriate:

  "…provided that if a person dies intestate as to all or any part of his or her estate property which he or she gave…"

- *Make Personal References*

Make personal references in the document. By that I mean instead of *"I give $10,000, to my son", use "I give $10,000, to my son, Frank".* This serves several purposes. First, it personalizes the document and makes it read less like a form. Second, it insures proper identification of the heir.

- *Make Consistent References*

  Use consistent references. If you refer to a testator's issue in one part of the Will, don't shift to testator's descendants in another part. Again, this shows a lack of attention to detail.

- *Check Your Internal References*

  Make sure your internal references are correct, that is the reference to a particular paragraph for example, as in "as defined in paragraph I.A", actually refers to the proper paragraph.

- *Use Simple Language*

  Use simple language which is understandable to the layman. For example, use "I give" rather the more legal "I bequeath", or "I devise". Also the following is preferable:

  "I give the rest of my estate to my daughter, SARAH, if she survives me."

  Instead of the wordier:

  "All the rest, residue and remainder of my estate, both real and personal, of whatsoever nature and where ever so situate, of which I shall die seized or possessed or to which I shall be in any way entitled, or over which I shall possess any power of appointment by Will at the time of my death, including any lapsed legacies, I give, devise and bequeath as follows:…"

- *Use 14Pt Type*

  For older clients think about using 14 point type. They will appreciate the large print simply because it makes the document easier for them to read.

B. Gift Drafting

In drafting gift provisions you must as the scrivener:

- Properly identify the heir or heirs;
- Provide for what happens if the heir doesn't exist.
- Properly identify the subject property;
- Provide for what happens if the property doesn't exist;

C. Identifying the Heirs

- It is important to identify the heirs so that there is no confusion as to who is to receive the gift in question.
- You should always, when able, identify heirs by name and relationship to the testator.
- For someone outside the immediate family, use a first and last name. It doesn't have to be their formal legal name, but it must be sufficient to identify the person in question. If you believe there is any possibility of confusion, you might consider adding an address or other phrase of identification to clarify.
- In drafting class gifts define the class in terms of the identity of the class members and the specific date upon which the class is to be determined, generally the date of death. If the date on which the class is to be determined is other than the date of death then it should be specifically provided.
- First, in making a charitable gift, it is important to properly identify the charity. Go to the charity's web-site, call them on the telephone – but be sure to get it right. Google produces over 3900 results for the term "First Presbyterian Church" in Pennsylvania alone.
- Second, you must clearly state the purpose of the gift:

  "I give the sum of Five Thousand dollars ($5,000.00) to the Reading Hospital, 6 Spruce Street, Reading, Pennsylvania, or its successors, to be used to endow a bed in the name of my father, DAVID JONES."
- Finally, make sure the purpose is practical, however. Often the charity will prefer that the gift be unrestricted in its use:

  "I give the sum of Five Thousand dollars ($5,000) to the Reading Hospital, 6 Spruce Street, Reading, Pennsylvania, or its successors, to be used for its general purposes."

D. <u>What if the Heir Doesn't Exist?</u>

The PEF Code provides that:

- A devise or bequest to a child or other issue of the testator, or
- To his or her brother or sister, or
- To a child of his or her brother or sister, whether designated by name or as one of a class,
- Shall not lapse when the named beneficiary fails to survive the testator but leaves issue surviving the testator,

- But shall pass to such surviving issue, who shall take per stirpes the share which the deceased ancestor would have taken had he or she survived the testator,

- Provided that such a devise or bequest to such a brother or sister or child of a brother or sister shall lapse to the extent that it would pass to testator's spouse or issue as part of the residuary estate or under intestate law.

The anti-lapse statute does not apply if the decedent expresses a contrary intent, however. By making the gift subject to the condition that the beneficiary survives the testator, the gift will not be subject to the statute. It is also good drafting practice to specifically provide how the gifted property is then to be disposed. Language such as "… if she does not so survive, such property to her then living issue, per stirpes", or "… if she does not so survive, such property shall lapse" should be used to express the testator's actual intent.

E. Disposition of Personal Effects

□ *Overview*

Personal effects generally do not have significant economic value, but because of the sentimental value sometimes associated with this type of property, it may take on inordinate importance to the surviving family members. Don't discount this. The method by which these assets are divided among the heirs should be designed to avoid conflict and bad feelings.

□ *Alternative Provisions*

Here are some alternative provisions which you might consider in disposing of personal effects.

□ *Heirs Decide*

In this context counting on the agreement of the heirs is generally not a good idea. Therefore, you should generally not use a provision like the following:

"My personal effects to my children in substantially equal shares as they shall agree".

□ *Executor Decides*

Equally problematic could be a provision like this one:

"My personal effects to my children in substantially equal shares as my Executor may decide."

This provision is a poor way to avoid conflicts if, as is often the case, one of the testator's children is also serving as executor.

□ *Memorandum Clause*

One possible solution is having the will provide that personal effects be disposed of in a memorandum created by the client outside the will. The use of a memorandum separate and apart from the will which dictates how specific items of personal property are to be distributed is generally a good idea for several reasons.

First, it allows the testator some flexibility in distributing the property. The formalities of a re-executing the entire will and the involvement of a lawyer are not required every time the testator wishes to change the disposition. He or she simply has to change the memorandum. A memorandum provision also allows the testator to delineate the disposition of specific items of personal property to specific heirs without having to provide for a lengthy disposition in the will. Of course, since the client is usually the one who completes the memorandum, make sure that you review it to insure that the designation of the recipient and the property gifted are clear and unambiguous.

F. Identifying the Property

It is your job as the scrivener to describe the property which is the subject of the gift in such a manner that it can readily be identified by the executor.

- *Specific Property* - For gifts of specific property use descriptive terms to make the subject property more readily identifiable; if there is an external reference, such as an account number or license number (e.g., in the case of bank accounts, automobiles, boats, real estate, etc.) use it.
- *Bank Accounts and Investment Accounts*. In making testamentary gifts of bank accounts and investments accounts, make reference to the title of the account as it appears on the bank or investment statement, along with the account designation as referenced on the account statement.
- *Stock and Bonds.* If the gift is of a particular stock, bond or other investment property, rather than an account which holds such property, identify the property as specifically as possible by referencing the issuer, the type investment property which it represents (i.e., common stock, preferred stock, voting or non-voting stock, bond, debenture, etc.), and the certificate number, or CUSIP number.
- *Real Estate*. For gifts of real estate, describe the property as you would in an agreement of sale. That is, use the legal description, or a "commonly known as" reference such as the street address.
- *Collections.* In regard to collections and other property groups, the gift provision should clearly define what items are to be considered a part of the group and which items are to be excluded. It may be advisable for the

testator to create an external list, catalog, or other reference outside the will in order to make the identification of the collection or property group more definite.

G. <u>What if the Property Doesn't Exist?</u>

1. The Essential Question

In your discussions with your client and in your drafting, make a habit of addressing the question of "*What happens if the subject property doesn't exist in your estate?*" The type of gift, whether specific, general, demonstrative, or residuary, will determine whether the gift will adeem if the property does not exist in the estate and in what order gifts will abate if the estate is not adequate to fund all of the gifts provided in the will. Therefore, you must make clear exactly what type of gift the testator intends to make, and what his or her intentions are if the subject property is no longer held by the estate.

2. What if the Property Doesn't Exist? – Specific Gifts

- Specific gifts will adeem if the subject property does not exist in the estate. On the other hand, by its very nature, a general gift is not subject to ademption. General bequests are generally not adeemed by failure of the testator to own the particular property at death. In the case of a general gift, if the decedent does not own the subject property, the legatee or devisee may elect to have the value in cash or have the executor purchase the item of property. A general gift like the following could therefore prove problematic if the testator does not own the subject of the gift at the time of his or her death:

> *"I give the painting "Sunflowers", by Van Gogh to my son, Jason, provided he survives me."*

- Therefore, in drafting general gift provisions you should clearly express the testator's intention with language such as the following:

> *"I give ten shares of Ford Motor Company stock to my son, Jason, provided he survives me, and further provided that I own such property at the time of my death, otherwise such gift shall lapse."*

- Alternatively:

> *"I give ten shares of Ford Motor Company stock to my son, Jason, provided he survives me, and further provided that I own such property at the time of my death, otherwise my Executor shall fund such gift with equivalent value."*

4. *What if the Property Doesn't Exist? – Specific Gifts*

- A demonstrative bequest provides a preferential source of payment for a legatee, while at the same time providing that the bequest will be paid from other assets if the preferred source does not exist or is not sufficient. A demonstrative gift is therefore a type of gift which is a hybrid between a general

and a specific bequest. A demonstrative bequest is treated as if the property to which the fund is charged was specifically gifted to the beneficiary to the extent of the gift. If the fund is insufficient to cover the gift, payment is to be made from the general funds of the estate and the beneficiary is treated as a general legatee.

An example of a demonstrative legacy would be as follows:

"I give the sum of $10,000 to X, payable to the extent possible out of my Savings Account No 345556, at Somerdale Bank, NA, however if such account is insufficient to fully fund such gift the balance shall be paid out of the general assets of my probate estate, before administrative expenses."

- You should also keep in mind that a gift may fail to be funded if it is abated because the estate is insufficient to fund all of its expenses and liabilities. The order of abatement under the PEF Code was reviewed in Chapter 4. However, the will can, by language like the following, alter the statutory order of abatement:

"If my estate shall be insufficient to pay in full the legacies contained in my will then I direct that they shall abate proportionately."

- Also, keep in mind that the PEF Code provides that in the case of a specific gift, if the testator does not own a specific security at the time of death, which was owned by him or her at the time of the execution of his or her will, instead of the equivalent value, the legatee is only entitled to as much of those securities as remain part of the testator's estate at the time of his or her death. This includes any additional or other securities issued by the same entity thereon and owned by the testator by reason of a stock dividend, stock split or other action by the entity. Any securities acquired by exercise of purchase options for more than a fractional share, and securities of another entity received thereon or in exchange therefor and owned by the testator as a result of a merger, consolidation or reorganization of the entity or other similar change are excluded.[1]

- If, however, the intent of the testator runs contrary to the statute, the statute can be overridden with language like the following:

"I give one hundred shares of the stock of the KGH Corporation, and any successor thereto, to my friend, WILLIAM JONES, if he survives me. If between the date of this will and the date of my death the share capital of the KGH Corporation shall be increased or reduced, the bequest herein made shall be of a number of shares bearing the same proportion to the then total number of shares outstanding as the shares herein given bear to the present total number of shares outstanding."

H. <u>The Residue</u>

[1] 20 Pa. Cons. Stat. § 2514(17).

- Overview

The "residue" of an estate refers to all property not otherwise effectively disposed of by the testamentary instrument. In other words, what is left after the payment of all debts, taxes, expenses and the funding of all specific, general and demonstrative gifts. Any gift that fails because the beneficiary predeceased the decedent (unless preserved under the Anti-lapse statute) or fails for any other reason, falls into the residue and passes under the terms of the residuary clause

- *One Beneficiary*

In dividing the residue, the entire residue may pass to one beneficiary:

"I give the rest of my estate to my daughter, SARAH, if she survives me."

- *Shares*

"I give the rest of my estate in equal shares to such of my son, THOMAS, my son, RALPH, and my son, KEVIN, who survive me for a period of thirty (30) days."

- *Percentages*

"I give the residue of my estate to be distributed as follows; provided however, that the percentages stated below are for distribution from the net residue after the payment of administration expenses and the payment of any applicable death taxes. It is my intention that all expenses and taxes be paid before the percentages are applied.

A. Twenty (20%) per cent to ABC CHARITY;

B. Thirty (30%) per cent to XYZ CHARITY;

C. Twenty-five (25%) to my son, JOHN; provided he survives me for a period of thirty (30) days, or if not, to his issue then living; and

D. Twenty-five (25%) to my daughter, SUSAN; provided she survives me for a period of thirty (30) days, or if not, to her issue then living."

- *Additional Language*

If you are using a clause which is drafted in terms of shares or percentages you should also include a provision like the following:

"If there is no one eligible to take a share provided hereunder it shall be added pro rata to others shares so provided for which there are individuals or entities then eligible to take such share. Provided further that if there is no one eligible to any share provided hereunder the residue of my estate shall pass under the terms of paragraph VI, hereof."

- *"Pour Over" Provision*

In many cases, the residue may be passed to an inter vivos trust. This is referred to as a "pour over" will provision. An example follows:

"I give the rest of my estate to the Trustee of the MARY ALICE GORDON TRUST under that certain trust agreement signed on this date, but before this will, as an addition to the principal, to hold it upon the same terms as they exist as of the date of the execution of this Will, or the last codicil hereto, without any obligation to account for it as a part of my estate and subject to the obligation to account under the trust agreement only in the court of jurisdiction in which accounting shall be required."

- *Saving Clause*

If a provision like this is used, it is generally a good idea to also add the following provision in case the referenced trust is not in effect at the time of the testator's death:

"In the event such trust agreement is not in effect at the time of my death, the same shall be held by the trustee in trust on the same terms and conditions as those specified in such trust agreement as the same existed at the time of the execution of this Will or of the last codicil hereto, with like effect as if the terms thereof were set forth herein verbatim."

I. <u>The Wipe Out Clause</u>

- Overview

What if none of the named residual beneficiaries are living at the time the trust terminates? A "wipe out" provision provides for the disposition of the trust estate if no one who has been named as trust beneficiary survives. If there is nothing stated in the trust, then the intestate statute will determine who will be entitled to the trust property. Some people will not care at all, some will care very much, and still others will care more about who they don't want to receive the property, rather than who will. Naming one or more charitable beneficiaries may serve as a good wipe out clause. In any case, the trust should address the issue. Here is some sample language which will split the estate between the intestate heirs of the husband and the wife rather than having it go 100% to the heirs of the surviving spouse:

- Here is an example of a wipe out clause:

"If at any time there is no one living who is entitled to income or principal under the forgoing provisions, to pay the then-remaining principal as follows:

(1) One-half (1/2) thereof to my intestate heirs, such heirs to be identified and in such amounts, as determined as the time of my death, under the laws of the Commonwealth of Pennsylvania, as if I had died intestate, unmarried and without surviving descendants, and

(2) One-half (1/2) thereof to the intestate heirs of my wife, such heirs to be identified and to receive such amounts as determined under the laws of the Commonwealth of Pennsylvania, as if she had then died intestate, unmarried and without surviving descendants."

J. <u>Minors and Disabled Heirs</u>

- *Minor's Trusts*

A trust is the recommended alternative to both Guardianship and Custodianship for several reasons. First, the trust may be designed specifically to meet the needs of the individuals involved both in terms of how the funds are expended and how they are invested during the trust term. Secondly, the trust can continue until whatever age the testator feels appropriate, even far into adulthood or for lifetime.

In order to provide disposition of property to a minor in trust, the testator will either create the trust in his or her will (a "testamentary trust") or as a separate trust document created during lifetime (an "inter vivos trust"). In either case, the will generally adds probate assets to the trust at the time of death. Non-probate property can also be added by a designation of beneficiary naming the trust.

In the case of a married couple with minor children, it is recommended that upon the death of the second spouse, the will of that parent passes the residuary estate to a trust for the benefit of the surviving children. In such a case, rather than splitting the residuary estate into equal shares for the surviving children, the residue is typically held in a single trust for the benefit of all of the children until the youngest surviving child reaches a certain age, e.g., 25; with trust distributions permitted among the children at the discretion of the trustee. At the point the youngest child reaches the stated age, the trust is then generally split into equal shares, one for each child, and then either held in further individual trusts or distributed to them outright. In most cases when the children's individual shares are to be continued to be held in trust, the trustee will be given the discretion or the obligation to make distributions of income and/or principal to each trust beneficiary from their share.

- *Drafting the Minor's Trust*

As stated above, in the case of a married couple with minor children, it is recommended that in the event of the death of both parents, the will of the second parent to die pass the residuary estate to a testamentary trust for the benefit of the surviving children. Here is sample language:

"I give the residue of my estate to my wife, LINDA, provided she survives me by thirty days. If my wife, LINDA, fails so to survive me, then I give such residue to the Trustee hereinafter appointed, to be held and administered as follows:…"

Rather than split the residuary estate into equal shares for the surviving children at that time, the residue should be held in a single trust for the benefit of all of the children until the youngest surviving child reaches a certain age, e.g., 25, with trust distributions permitted among the children at the discretion of the trustee. The language of the trust could be as follows:

"1. If there is a child of mine under age twenty-five (25) on the date of my death, who survives me:

a. The Trustee shall pay to such one or more or all of my then living children so much of the net income of such Trust in such proportions, equal or unequal, as my Trustee, in the Trustee's sole and absolute discretion, deems advisable.

b. The Trustee may also pay to or apply for the benefit of any child of mine as much of the principal as my Trustee deems advisable for his or her maintenance, education, health and support after first considering funds available to him or her from other sources.

c. Distributions of income or principal shall not establish a pattern or entitlement for any subsequent distribution. All net income not so paid shall be accumulated and added to principal."

Notice that in the preceding paragraph the trustee is given the absolute discretion to make distributions of income from income among a class of trust beneficiaries made up of the testator's "then living children." The trustee also has the discretion to distribute principal to that same class but limited by the ascertainable standard of "maintenance, education, health, and support."

The logic behind retaining the residue in one trust in this fashion is to ensure that the younger child or children are provided for from the aggregate estate in the same way, e.g., in regard to education, as the older children were provided prior to the death of the parents, at least up to a stated age. The stated age should be the age that the youngest child will, in the parent's opinion, be largely self-sufficient.

At the point the youngest child reaches the stated age the trust is then generally split into equal shares, one for each child, and then either held in further trust or distributed to them outright. In most cases when the trust shares are to be continued to be held in trust, the trustee will be given the discretion or the obligation to make distributions of income and/or principal to each trust beneficiary from their share.

"2. Upon the expiration of the trust term under Section 1, or upon my death if all of my then-living children have attained age twenty-five (25), to divide the principal into as many equal shares as there are children of mine then-living and children of mine then-deceased represented by descendants then-living, and:

a. To pay the share of a then-deceased child to his or her then-living descendants, per stirpes, outright.

b. To retain in a further separate trust each share of a then-living child, and

(1) To pay the net income therefrom at least quarterly to such child.

(2) To pay to or apply for the benefit of such child so much of the principal of such child's separate trust as my Trustee deems advisable for his or her maintenance, education, health and support. In the exercise of this power for any person, funds available to him or her from other sources shall be considered by my Trustee."

Note this provision makes distributions of income to the beneficiaries mandatory, but principal distributions remain limited by the ascertainable standard of "maintenance, education, health, and support."

Often, the trust provides that a pro rata share of the principal be distributed outright and free of trust at certain intervals provided in the trust – for example 1/3 of the trust when the child reaches age 25, 1/2 of the balance at 30, and the remaining balance at age 35.

"(3) To pay the principal thereof to such child upon his or her written request, as follows:

(a) At any time after attaining age twenty-five (25), up to one-third of the fair market value.

(b) At any time after attaining age thirty (30), up to one-half of the difference between (i) the fair market value and (ii) any amount which such child could have, but has not, withdrawn under clause (a).

(c) At any time after attaining age thirty-five (35), the remaining principal.

(d) Fair market value as referred to in clauses (a) and (b) hereof shall be determined, and a child shall be entitled to withdraw principal, at the foregoing respective ages, at the termination of the above-referenced trust term or upon the death of the survivor of my said husband and me, whichever last occurs."

And finally a clause which determines the disposition of the trust property in the event a child dies before the entire principal balance is distributed:

"(4) Upon the death of any such child before the entire principal of his or her trust has been distributed, to pay the remaining principal:

(a) To such of my descendants (except such child), and their spouses (including the spouse of such child) in such manner and shares, for such estates, or upon such trusts as such child may appoint in his or her last Will by specific reference to this limited power;

(b) To pay the principal not effectively so appointed to the then-living descendants of such child, per stirpes; and in default of such descendants, to my then-living descendants, per stirpes. Any additional share of a child of mine for whom a trust is then in existence under this subparagraph shall be added to such trust, to be held under the terms thereof as applied to circumstances then existing.

(c) If at any time there is no one living who is entitled to income or principal under the foregoing provisions, to pay the then-remaining principal as follows

(1) Any income accrued or undistributed at the death of an income beneficiary shall be paid to the succeeding income or principal beneficiary."

- *Special Needs Trusts*

Estate planning for parents with disabled family members presents its own unique sets of problems. In addition to the usual concerns, parents must weigh their desire to provide for all of their children "fairly," with the need to adequately provide for the "special needs" child or children. In addition, the way that the special needs child is provided for must be done in a way which preserves, if possible, the child's eligibility for government benefits, such as Mental Health/Mental Retardation and/or Mental Assistance, and/or Supplemental Security Income ("SSI"). For such children, the form in which a bequest is made is extremely important. If a disabled person receives monies from an inheritance, the direct receipt of the funds may cause the disabled person to lose public benefits. A good planning solution, however, is often the "Special Needs Trust."

There are several different types of special needs trusts. So called "Self-Settled Special Needs Trusts," or "Payback Trusts," are trusts created with the disabled individual's own assets for their own benefit without disqualifying the individual for Medicaid assistance or Supplemental Security Income ("SSI"). In the context of drafting wills, however, it is a third type of special needs trust that we will be addressing in the following material. This type of trust is the common law discretionary trust, sometimes referred to as a "Third Party Special Needs Trust," or "Supplemental Needs Trust," and is funded with the assets of a third party for the benefit of the disabled individual.

- *Third Party Special Needs Trusts*

The purpose of the Third Party Special Needs Trust is, like Self-Settled Trusts, to preserve public benefits for the trust beneficiary while supplementing the beneficiary's lifestyle. There is a significant difference between Third-Party Special Needs Trusts and Self-Settled Special Needs Trusts, however. While the Special Needs Trust is funded with the trust beneficiary's own assets, a Third-Party Special Needs Trust is established with the funds of someone other than the beneficiary, typically a parent or grandparent. In the context of our discussion of will drafting, the Third Party Special Needs Trust is often funded with a bequest to be held in trust for the benefit of the disabled individual. If it is properly drafted, the funding of the trust will not disqualify the disabled individual from receiving public benefits.

A common law discretionary trust is a trust in which the trustee has full discretion as to the time, purpose, and amounts of all distributions. The trustee may pay to or for the benefit of the beneficiary, all or none of the trust as he or she considers appropriate. The beneficiary has no control over the trust. In order to ensure that distributions from a common law discretionary trust will not disqualify the disabled individual from receiving public benefits, the trust document should state clearly that the intent of the trust is merely to supplement and not supplant public benefits. It should be further provided that the trust distributions are only to be made for expenses not covered by public programs.

The appointed trustee must have the sole discretion in deciding whether to make distributions of income and principal from the trust. It goes without saying that the trust beneficiary should have no right to revoke the trust or to compel distributions for his or her

support and maintenance. It is important that a residual beneficiary be named. A residual beneficiary is not a current beneficiary of a trust, but one who will receive the residual benefit of the trust contingent upon the occurrence of a specific event, e.g., the death of the primary beneficiary. It is also important to state the intent of the grantor in establishing the trust to preserve at least some of the trust value for the benefit of the remaindermen, and that the trustee should consider their interest when making trust distributions. The trust must not only be properly drafted but properly administered. Improper distributions from a properly drafted and funded trust can result in loss of benefits. Trust distributions must not be made directly to the beneficiary. They must be made to third parties.

K. Waive Powers of Appointment

- PEF Code § 2514(13) provides that a general bequest of real or personal property, as well as a general pecuniary legacy shall operate as an execution of any power which the testator may have to appoint such property. In order to avoid an inadvertent exercise of a power of appointment the following clause should be included in the Will:

  "I decline to exercise any power of appointment given to me under any Will, Codicil or Deed of Trust."

L. Tax Clause

- *In General*

  A tax allocation provision acts to direct the executor in the manner in which death taxes incurred by the estate, both federal and state, are to be charged. In every case, the net after-tax-effect of the tax provision provided in the will on the client's probate and non-probate dispositions should be reviewed with the client. The question to be answered is "How much is the net-after-tax-gift each heir will receive after the allocation of the estate and inheritance taxes?"

- *Alternative Provisions*

  Some alternatives to the allocation provision cited above will be discussed in this section. The following example of a typical tax provision provides that the death taxes incurred are to be paid out of the residuary estate.

  "(a) All death taxes (and interest and penalties thereon) imposed as a result of my death shall be paid out of my residuary estate."

  Another way to word this is as follows:

  "(a) All death taxes (and interest and penalties thereon) imposed as a result of my death upon property regardless of whether passing under my Will, shall be paid out of the principal of my residuary estate, each share thereof, whether outright or in trust, to bear a pro rata portion of such taxes."

These provisions result in the taxes generated by both the probate estate and non-probate assets being paid out of the residue of the probate estate. This means that the residuary estate will be reduced by the death taxes generated by the entire estate, and other gifts will pass free of tax.

M. Administrative Provisions

The objective of the administrative provisions in the will is to avoid unnecessary complications in the administration of the estate, and to enable the executor to act without requiring court approval for actions which would normally be anticipated in estate administration

Here are some of the administrative provisions the Will should contain:

- The power to apportion receipts between income and principal;
- The power to borrow;
- The power to carry on business;
- The power to compromise claims;
- The power to distribute assets in kind;
- The power to expend or apply funds; and
- The power to purchase all forms of property.

N. Fiduciary Provisions

Appointment of a Guardian of the Person

In the event that the testator has minor children (defined in PEF Code § 102 as children under the age of 18), a guardian of the person should be named. Under PEF Code § 5112, a court will not appoint a guardian of the minor's estate who is either:

- Under the age of 18,
- A corporation not authorized to act as a fiduciary in Pennsylvania, or
- The surviving parent (unless the parent serves as co-guardian).

The appointment of the Guardian of the Person of a Minor Child is discussed in more detail in Chapter 8.

Appointment of a Personal Representative

If no executor is validly appointed in the will, the PEF Code in § 3155, provides the Orphans' Court with the following order of priority in filling the vacancy:

- Those entitled to the residuary estate under the will;
- The surviving spouse;

- Those entitled under the intestate law as the register, in his or her discretion, shall judge will best administer the estate, giving preference, however, according to the sizes of the shares of those in this class;
- The principal creditors of the decedent at the time of his death; and
- Other fit persons.

If anyone of the foregoing renounces his or her right to letters of administration, the Register of Wills in his or her discretion, may appoint a nominee of the person who is renouncing in preference to the persons set forth above. The Register of Wills has the discretion to refuse letters of administration to any individual not a resident of Pennsylvania.

If the will appoints an executor who is an individual, then he or she must be at least 18 years old. In order to qualify, a corporation must have fiduciary power in the state of Pennsylvania. There is no requirement that the executor actually is a resident of the state of Pennsylvania, but in order to serve a non-resident executor must post a bond with the Orphans' Court unless the will provides for a waiver of the bond. The provision which effectuates the waiver of the bond is discussed in the next section.

It is important that, in addition to the executor originally appointed, the will appoint one or more successors.

In the majority of cases married couples with children will appoint their spouse as their primary executor, followed by one or more of their children as the successor.

If children are appointed as the first choice or as successors in something other than in the order of age, oldest first, then it may be advisable for the testator to provide an explanation to the older child or children as to why this decision was made. Remember, the will can be the last document that speaks from the parent to the children. Even adult children are sensitive to this type of deviation from what might be perceived as the proper order of things. A letter left with the will, or a provision within the will itself, will go far to soften the blow for a child feeling slighted.

Generally, it is a good idea to appoint individuals over banks and trust companies. Why? Not because institutional executors charge fees – they as a rule provide a valuable service in administrating the estate, and in most cases have the required expertise and will earn the fees they are paid. The reason is simply if the institution is not doing its job, absent negligence, it is difficult to remove them without court intervention. On the other hand, an individual executor can hire the institution to perform the same administrative services it performs as executor, but if the institution does not perform as expected the individual executor can dismiss the institution at any time without difficulty.

O. <u>Waive the Bond</u>

- Under the PEF Code, it is no longer necessary for the will to specifically waive the posting of security provided the personal representative is a resident of Pennsylvania. However, it is still a good idea to include a provision like the following, in case an out of state executor is appointed:

  "My executor shall not be required to post security in any jurisdiction."

P. Proper Execution

- *In General*

It is the duty of the lawyer drafting the will to ensure that the document is properly executed, so that it may be granted legal recognition upon the testator's death. It goes without saying that the draftsman should be physically present during the execution process.

- *Explanation and Signing*

You should begin the execution process by explaining each provision of the document in order to be sure that the testator understands what he or she is signing and that it is consistent with his or her intent.

If the testator understands and is satisfied, then you can proceed with the execution of the document. You should consider using three witnesses since no state requires more. This will ensure that the document will be portable to any state. Also, it is good practice to have a notary public present in order to notarize the document. This will make the will "self proven."

You should avoid using beneficiaries as witnesses since a few states bar such individuals from witnessing the document. Get in the practice of having the testator sign on the side of each page, in order to lessen the possibility of fraudulent substitution of pages.

Before execution, ask the testator to affirm before the witnesses that the document is his or her last will and testament. Each witness should then sign, and remain in the room until the process is complete.

- *Statutory Requirements*

The PEF Code requires that the will "shall be in writing and shall be signed by the testator at the end thereof." Except where it is signed by mark, no witnesses are required. Any two witnesses can affirm the signature at probate.

- *What is a Signature?*

The purpose for requiring a signature is to authenticate the instrument, identify the testator, and establish testamentary purpose. The sole test as to whether or not a purported signing is a valid signature is whether it was made with the intent that it actually be a signature. Extrinsic evidence is admissible to aid in determining whether

the testator intended such to be his or her signature. Initials, unintelligible scribble, nicknames, maiden names, and even fingerprints have all been accepted as valid signatures.

A "mark," such a cross or an X, is allowable only if signed in the presence of two witnesses, who also sign the will. A signature by another is permitted provided that the testator is unable to sign, and the testator's name is subscribed in his or her presence and by his or her direction. This must be coupled with a declaration by the testator made in the presence of two subscribing witnesses that the instrument is his or her will, who then also sign in the testator's presence.

- *Two or More Instruments*

A person may have more than one will provided that the last document in time does not expressly or by implication revoke the prior wills. A valid will may be written on separate, not physically united, sheets of paper, only the last of which is signed. Good practice requires stapling of the pages, although this type of physical connection is not required. Integration may be inferred by internal coherence of the pages. As referenced earlier, signing of each page on the side, not the bottom, of the page will insure against fraud.

- *At the End Thereof*

The PEF Code requires that the will be signed at the end. An instrument that is not signed as required by the statute cannot be given effect as a will. Any words following the signature are invalid. The end contemplated by the statute is the logical end of the language used by decedent in expressing his or her testamentary purpose, and not the point which is physically farthest from the beginning of the writing. Thus, signing at the top or side of a page or the back of a printed form does not fulfill the requirement that the document be signed at the end. The question must be determined from the document itself, without the benefit of parol evidence.

- *Witnesses*

The signature of the testator should be proven by three witnesses. While under the PEF Code an unwitnessed will is still valid, make a practice of having at least three disinterested subscribing witnesses. This will insure the portability of the will, in case the testator relocates to a state that requires witnesses.

It is also a good idea to have the testator sign or initial each page of the will. This will prevent allegations of "slip paging." Do this on the side rather than the bottom of the page. Otherwise the testator may have actually executed a series of wills, signed at the end.

When probating the will, except in the case of a will signed by mark or by another, the proof should be by individuals who actually witnessed the execution of the document,

i.e., subscribing witnesses, if they are available. If the subscribing witnesses are not readily available, the testator's signature may be proven by others who are familiar with the testator's signature.

In the case of a will signed by mark or by another on behalf of the testator, the proof of the signature must be by subscribing witnesses, except to the extent that the Register of Wills is satisfied that such proof cannot be adduced by the exercise of reasonable diligence. In that event other proof of the execution of the will, including proof of the subscribers' signatures, may be accepted.

- *Notarization*

Unless there is a contest with respect to the validity of the will or unless the will is signed by mark or by another, an affidavit of the witnesses must be accepted by the Register of Wills as proof of the facts stated as if it had been made under oath before the Register at the time of probate.

An attested will may at the time of its execution or at any subsequent date be made self-proven by the acknowledgment thereof by the testator and the affidavits of the witnesses, made before an officer authorized to administer oaths under the laws of this Commonwealth, i.e., a notary public. In Pennsylvania, a document can also be notarized based on the affidavit of an attorney actually present at the signing.

- *Dated*

In Pennsylvania there is no requirement that the will be dated, but it is good practice to do so. The date of execution may have a material bearing on the rights of the beneficiaries, and will be the date on which the intention of the testator is determined.

V. Protect the Will

A. Client with Capacity Issues

- The test is whether the testator: (i) is at least 18 years of age; (ii) appreciates, in a general way, the nature and extent of his or her estate (property in possession); (iii) appreciates the natural objects of his or her bounty; and (iv) has a reasonable understanding of the disposition he or she wishes to make of his or her estate.

- In all cases when you are dealing with individuals of diminished capacity you should be aware of the requirements under Rule 1.4 of the Pennsylvania Rules of Professional Conduct. That Rule requires that when a client's capacity to make adequately considered decisions in connection with a representation is diminished, whether because of minority, mental impairment or for some other reason, the lawyer must, as far as reasonably possible, maintain a normal client-lawyer relationship with the client. Further, the Rule requires that when the lawyer reasonably believes that the client has diminished capacity, is at risk of

substantial physical, financial or other harm unless action is taken and cannot adequately act in the client's own interest, the lawyer may have to take reasonably necessary protective action. This action may include consulting with individuals or entities that have the ability to take action to protect the client and, in appropriate cases, seeking the appointment of a guardian ad litem, conservator or guardian.

- The defense of the will should begin with proper execution. The proper execution of the will raises a presumption of testamentary capacity, and shifts the burden of proving lack of capacity to the party contesting the will.
- The testimony of subscribing witnesses is also relevant.
- In order to bolster this testimony, you may wish to conduct a colloquy of sorts with the testator in the presence of the witnesses. This colloquy should be designed to establish that the testator in fact does recognize his or her family, the nature of his or her estate and the disposition of the estate which the testator wishes to make. In addition, it may be a good idea to have the witnesses document their observations in a contemporary memorandum, since they may be unavailable at a later date or be unable to remember what took place.
- Consultation with the testator's treating physician may also be advisable. The conclusions of a treating physician will generally carry heavy weight with the court. However, be reminded that the physician's conclusions should be specific to the issues of whether the client possesses the requirements for testamentary capacity, i.e. the ability to recognize the natural objects of his or her bounty, the nature of his or her estate and the disposition the testator wishes to make of that estate.
- Finally, a video of the testator, created closely in time to the execution of the will, during which the testator exhibits an awareness of the relevant issues, should also go far to establish the testamentary capacity of the testator.

B. <u>Client with Undue Influence Issues</u>

- As discussed in regard to the issue of capacity, the law presumes that a will that was properly executed is valid – in other words there was no undue influence. However, once a contestant of a will establishes that: (i) a person in a "confidential relationship;" (ii) receives a substantial benefit; (iii) from a testator of weakened intellect, the burden of proof shifts to the person occupying the confidential relation to prove affirmatively by clear and convincing proof the absence of undue influence.
- A "confidential relationship" exists when the circumstances make it certain the parties do not deal on equal terms, that is, on the one side there is an

overmastering influence, or, on the other, weakness, dependence or trust. In some cases the confidential relationship is a conclusion of law. A confidential relationship will exist as a matter of law between a scrivener and the testator, an attorney and his or her client, and a principal and an agent. In other cases, it is a question of fact to be established by the evidence. Such relationships may include kinship or marriage, doctor, banker, nurse, or attorney in fact.

- The term "influence" does not refer to any and all conduct capable of disposing a fully and self-directing mind in one's favor, but rather to the control acquired over another which virtually destroys the testator's free agency and operates as a present restraint upon him or her in the making of the will.
- You must satisfy yourself that the dispositional plan expressed by the will has not been influenced by a potential beneficiary. Be particularly careful when an elderly client is brought to your office by someone whom you are told is to benefit disproportionally under the will.
- In such a case, it is a recommended that you meet with the client without that individual being present in the room. During your meeting you must establish in your own mind that the disposition to be made in the will is actually consistent with the client's own intentions. It is also not a bad idea that you have someone else from your office sit in on the meeting, and have them record their own impressions as to whether the client is acting independently.
- It may also be advisable to have the testator execute a document which explains the dispositions made in the will. That document should ideally be in the handwriting of the testator and not the result of word processing or typing. A handwritten document will go far to eliminate allegations that the document was prepared by someone else and simply signed by the testator without being aware of its contents. Finally, as in the case of capacity, a video discussion of the rationale behind the dispositions of the will might also be helpful.

VI. Addressing Living Probate

A. General Power of Attorney

- Complete name and address and contact information.
- Age.
- Occupation or profession.
- Relationship between parties, if any.
- Details of any past or present physical or mental disability.
- Proposed details of power of attorney desired.

- ☐ If special power, details of transaction or activity involved.
- ☐ Limitations on power, if any.
- ☐ Duration of power.
- ☐ Terms and conditions under which power may be revoked prior to expiration.
- ☐ If one or more parcels of real property are to be specifically mentioned in power of attorney, addresses and legal descriptions of parcel or parcels.
- ☐ If personal property subject to registration (such as automobile, truck, trailer, boat, or airplane) is to be specifically mentioned in power of attorney, specific registration information (such as make, year, model, license number, and registration number of vehicle or other item).
- ☐ Name and address of any other agent appointed by same principal, and details of powers given.
- ☐ If power of attorney is intended to revoke a previous power of attorney or to substitute new agent:
- ☐ Name and address of grantor of previous power of attorney.
- ☐ Name and address of agent appointed by previous power of attorney.
- ☐ If previous power of attorney was filed or recorded, date and county of filing or recording.
- ☐ Include required notice to principal in capital letters at beginning of power

All powers of attorney are required to include a notice explaining the purpose, effect, and limitations of the power of attorney. The notice must be included in capital letters at the beginning of the power of attorney, and must be signed by the principal. Effective January 1, 2015, the notice requirement does not apply to certain types of powers.

- ☐ Draft introductory language identifying principal and agent
- ☐ If general power is to be given, draft provision giving broad powers
- ☐ If a power of attorney grants to an agent authority to do all acts that a principal is authorized to perform, the agent has all of the statutory powers that may be incorporated by reference
- ☐ If special power is to be given, draft provisions describing nature of powers granted and limits of exercise.
- ☐ If power is to be irrevocable, include clause expressing that intent.
- ☐ If power is to become effective on occasion of principal's disability or incapacity, include clause expressing that fact.

- ☐ Include applicable signature block:
- ☐ Execution by principal's signature.
- ☐ Execution by principal's mark.
- ☐ Execution by another at direction of principal.
- ☐ Include acknowledgment, of principal's signature or mark, if required

For a power of attorney executed on or after January 1, 2015, the signature or mark of the principal, or the signature or mark of another individual signing on behalf of and at the direction of the principal, must be acknowledged before a notary public or other individual authorized by law to take acknowledgments. The person taking the acknowledgment cannot be the agent designated in the power of attorney. This acknowledgment requirement does not apply to a power of attorney which exclusively provides for health care decision making or mental health care decision making.

- ☐ Include block for signatures of witnesses, if required.

Effective January 1, 2015, the signature or mark of the principal or other person must be witnessed by two individuals, each of whom is 18 years of age or older. A person acting as witness cannot be the individual who signed the power of attorney on behalf of and at the direction of the principal, the agent designated in the power of attorney, or the notary public or other person authorized by law to take acknowledgments before whom the power of attorney is acknowledged [20 Pa. Cons. Stat. § 5601(b)(3)(ii)]. Include acknowledgment executed by agent.

B. <u>Advance Health Care Directive/Living Will</u>

- ☐ Personal information on health care recipient.
- ☐ Name, address, and telephone number of health care recipient.
- ☐ If health care recipient is not client, relationship to client.
- ☐ Age of health care recipient.
- ☐ Whether health care recipient is:
- ☐ Competent adult.
- ☐ Incompetent person.
- ☐ Minor.
- ☐ If health care recipient is incompetent person or minor, name, address, telephone number, and relationship of legal guardian or closest relative.
- ☐ Marital status of health care recipient.
- ☐ Military service by health care recipient.

- ☐ If the health care recipient is a veteran, medical care may be available through veterans' benefits programs
- ☐ Information on health care providers.
- ☐ Name, address, and telephone numbers of health care recipient's physician or physicians.
- ☐ Name, address, and telephone number of hospital, nursing home, clinic, health care center, or other facility involved.
- ☐ Name, address, and telephone number of other health care professionals contacted by health care recipient, such as nurses or psychologists.
- ☐ Health care desired or required by health care recipient.
- ☐ The level of health care a particular individual needs should be determined by a health care professional. However, general information on the medical condition of the health care recipient will aid the attorney in determining which legal services, if any, may be involved and in suggesting alternative health care.
- ☐ Nature of health care recipient's medical condition.
- ☐ Type of disability, disease, or condition.
- ☐ Extent to which affliction is infectious or communicable.
- ☐ Degree of harm to which health care recipient and other persons in contact with recipient may be exposed because of condition.
- ☐ Whether recovery is possible or affliction is terminal.
- ☐ If health care recipient is pregnant, whether term of pregnancy is first, second, or third trimester.
- ☐ Mental alertness of health care recipient and ability to conduct coherent conversation.
- ☐ Extent to which health care recipient is ambulatory.
- ☐ Amount of assistance health care recipient requires with meals, personal grooming, and other daily personal activities.
- ☐ Medical treatment provided to health care recipient.
- ☐ Dates of visits to physician, other health care professional, or outpatient facility for:
- ☐ Advice regarding medical condition.
- ☐ Performance of medical procedures.

- Follow-up examinations.
  - For each visit to physician, other health care professional, or outpatient facility, nature of advice given and medical procedures performed. If health care recipient is no longer under care of physician, other health care professional, or outpatient facility, date of last visit.
  - Whether health care recipient is presently hospitalized or admitted to another health care facility.
  - Date of admission to hospital or other health care facility.
  - Medical services and surgical procedures performed or refused during stay in hospital or other health care facility.
  - Date of discharge from hospital.
  - Whether discharge was against advice of health care professional treating health care recipient.
- Medical treatment desired by health care recipient.
  - Specific medical service or surgical procedure.
  - Intention to refuse particular medical services or surgical procedures.
  - Intention to reside temporarily or permanently in health care facility.
  - Intention to live in own residence.
  - Information on health care recipient's financial sources.
  - Health care recipient's sources.
  - Insurance or prepaid health services by health maintenance organization (HMO).
    - Personal savings.
    - Home and other real property.
    - Personal property.
    - Stocks, bonds, and similar assets.
    - Business interests.
    - Pension and retirement benefits.
    - Other assets.
  - Other sources of funds.
    - Relatives, family, or friends.

- Names and relationship of individuals.
- Amount of funds they are able to contribute.
- Benefits from Social Security, Medicare, Medicaid, Veteran's Administration, or other public assistance.

 Choices

I direct that treatment be limited to measures to keep me comfortable and to relieve pain, including any pain that might occur by withholding or withdrawing life-sustaining treatment.

In addition, if I am in the condition described above, I feel especially strong about the following forms of treatment:

I □ do □ do not want cardiac resuscitation.

I □ do □ do not want mechanical respiration.

I □ do □ do not want tube feeding or any other artificial or invasive form of nutrition (food) or hydration (water).

I □ do □ do not want blood or blood products.

I □ do □ do not want any form of surgery or invasive diagnostic tests.

I □ do □ do not want kidney dialysis.

I □ do □ do not want antibiotics.

I realize that if I do not specifically indicate my preference regarding any of the forms of treatment listed above, I may receive that form of treatment.

VII. Trust Drafting Issues

A. Introduction

The manner in which the will gifts property to individual heirs is an important consideration. Some people are not equipped to inherit property outright. This may include minors, disabled individuals, and others who simply cannot handle money. For many there may be a need to protect assets from creditors, and for others the concern is the need for tax planning or the preservation of the subject property. In these situations a transfer in trust made in the will, i.e., a "testamentary trust," is the appropriate solution.

B. Issues to Address

 Trust Purpose

 Trustee's Discretion

 Provide Trust Flexibility

- Consistent Tax Clauses
- Removal and succession provision for Trustees
- Spendthrift clause

C. Trusts in General

A testamentary trust should be drafted to accomplish the testator's purpose in establishing the trust by considering the needs of the individuals involved, both in terms of how the trust funds are expended and how they are managed during the trust term.

A trust may be created by a transfer in trust made in a testamentary document, or a transfer in trust during the settlor's lifetime (an "inter vivos trust"). A trust can also be created by a simple declaration by the settlor that he or she holds property as trustee, or by the exercise of a power of appointment appointing property to a person as trustee. Legally, a "trust" is created when an individual manifests the intention to create a trust relationship, which subjects a trustee to duties to deal with property for the benefit of a charitable or individual beneficiary, "at least one of whom is not the sole trustee."

When a trust is created the trustee takes legal title to and management responsibility over the trust property. In addition, the trustee assumes a "fiduciary duty" to the beneficiary or beneficiaries of the trust. Under the law of trusts the fiduciary duty includes duties of loyalty, prudence, and a host of subsidiary obligations that reinforce the duties of loyalty and prudence. As a result, the interests of the beneficiaries are protected under law against mismanagement or misappropriation by the trustee.

A trust may be created only for purposes that are lawful, not contrary to public policy, and that are not impossible to achieve. A trust may be created for charitable purposes or for non-charitable purposes, or for a combination of the two. A charitable trust may be created for the relief of poverty, the advancement of education or religion, the promotion of health, governmental or municipal purposes, or other purposes the achievement of which is beneficial to the community.

A trust or a particular trust provision is not valid if: (i) "its purpose is unlawful or its performance calls for the commission of a criminal or tortious act;" (ii) "it violates rules relating to perpetuities;" or (iii) "it is contrary to public policy." The fact that the trust purpose cannot be achieved by lawful means will not necessarily "invalidate the trust if there is a substantial valid purpose that can be achieved by methods that are not unlawful." If, however, the invalid purpose is "so essential to the settlor's objective(s) that the permissible and impermissible purposes cannot be separated," the trust would still be invalid. Also, a non-charitable private trust, or a particular provision in the trust, may be invalid because all of the purposes for which a trust is created are so indefinite they cannot be enforced. Finally, if all of the trust purposes are impossible to perform, the trust will be invalid as well.

D. Creating the Trust in the Will

1. Overview

In order to create a valid trust (i) the settlor must have the requisite capacity, (ii) there must be an indication by settlor of an intention to create a trust, (iii) there must be a definite beneficiary or beneficiaries, (iv) the trustee must have definite duties to perform, and (v) the same person must not be the sole trustee and sole beneficiary. The validity of a trust created by will is ordinarily determined by the law of the decedent's domicile. If the will creating the trust is valid in the jurisdiction where it was executed, the trust is also valid. The trust agreement must also clearly provide the manner in which the income and principal of the trust is distributed or retained during the term of the trust, as well as the disposition of the trust corpus upon the termination of the trust.

To summarize, as the scrivener of the will, your job requires drafting trust provisions which:

- Manifest the testator's intent to create a trust,
- Identify the trust property,
- Identify the trust beneficiaries,
- Appoint a trustee, and
- Define the duties of the trustee, and the beneficial interests created by the trust.

2. Capacity

In order to create a trust, the person creating the trust, the settlor, must have the requisite mental capacity. In order to create a revocable inter vivos trust or a testamentary trust, the settlor must have the capacity to make a will. In order to create an irrevocable trust, the settlor must have capacity during lifetime to transfer the property free of trust. The capacity required to create a testamentary trust is directly related to the question of whether the testator has capacity to execute his or her will.

3. Manifesting the Intent to Create a Trust

In order to create a trust, there must be an outward expression by the trust settlor of his or her intention to create a trust. No particular words are required to create the trust and the words may be written or spoken. No notice to, or acceptance by, the trust beneficiary or trustee is required to form a trust, and a trust can be created without consideration.

Here is some language which you might use to create a testamentary trust in the will:

"I give the residue of my estate to my trustee, to hold upon the following terms:"

4. Identify the Trust Property

Basically "any property may be trust property." This includes "real and personal property, tangible and intangible property." Also, "undivided interests, terms of years, contingent future interests, and choses in action" may be trust property. There are two

qualifications - property that is not transferable and property that is not definite and ascertainable cannot be trust property. As a result, you as the scrivener of the will must specifically identify the property which is to be held by the trust:

"FIRST: Settlor hereby establishes with trustee a trust for the benefit of settlor's grandson, MICHAEL, to consist of the property described in Schedule A annexed hereto and such additions as may from time to time be made, to be held pursuant to the terms of this agreement."

Alternatively:

"…the sum of Five Hundred Thousand ($500,000) Dollars to be held by them, and to dispose of the net income and principal …"

5. Identify the Trust Beneficiary

 In General

At common law, any person who could take legal title to property can be a trust beneficiary. This implies that minors and others who lack legal capacity cannot be trust beneficiaries. The Comment to § 43 of Restatement (Third) Trusts makes it clear, however, that minors and others who lack legal capacity can in fact be trust beneficiaries. Also, corporations and unincorporated associations which have the legal ability to take legal title to property can also be trust beneficiaries. Under the Uniform Trust Code, a trust may also be created for the benefit and care of an animal alive during the settlor's lifetime.

 Definite Beneficiary Requirements

In order for a trust to be created it must have definite beneficiaries. This means that either the trust beneficiaries be identifiable "at the time the trust is created or ascertainable within the perpetuities period." Under the common law, if the beneficiaries cannot be so identified a trust is not created. Here is an example of an introductory clause which identifies the trust beneficiaries:

> "Settlor hereby establishes with trustee a trust for the benefit of my wife, SARAH, and the remaindermen hereinafter named, as follows:…"
>
> Often, the trust beneficiaries are identified within the body of the trust itself:
>
> *"Upon the death of the Settlor, if the Settlor's Spouse survives the Settlor, the entire Trust Estate shall be held in trust for the following uses and purposes:*
>
> *a. To pay all of the net income from the entire QTIP Trust to the Settlor's Spouse, annually or at more frequent intervals.*
>
> *b. To pay to the Settlor's Spouse or apply for the health, support, and maintenance of the Settlor's Spouse, at any time and from time to time such sums from or such part of the principal of the trust, including the whole thereof, as the Trustee may, in the Trustee's sole discretion, determine."*

6. Trust Purpose

A well drafted trust should include a statement of the settlor's intent in establishing the trust in regard to both the treatment of the trust beneficiaries and the management of trust assets. The extent of the interest of the beneficiary in a trust depends upon the manifestation of intention of the settlor. As discussed in the prior Chapter 11, a court will generally determine the settlor's intent from an examination of the trust instrument, the surrounding circumstances, and the condition of the estate and the family. In construing various provisions to arrive at the settlor's intent a court will not read into an otherwise clearly worded trust instrument an additional condition.

 Areas to be addressed.

Some of the areas to be addressed should be the settlor's intent in regard to the following:

- Taxation – both estate and income;
- Investment of trust assets;
- Allocation of expenses between income and principal; and
- Treatment of beneficiaries in terms of intent, and priority.
- Taxation

Here is Sample Language:

"It is my intention in establishing this trust to qualify the property passing under the Marital Deduction Share for the federal estate tax marital deduction. Any provision of this Agreement which may appear to conflict with my intention to qualify the Marital Deduction Share for the federal estate tax marital deduction shall be construed so as to accomplish that intention."

"It is my intention in establishing this trust that it be treated under IRC §§ 671 through 678, as a grantor trust for federal income tax tax purposes."

 Investment of Trust Assets

"It is my intention that my trustee maximizes the income interest provided for my spouse under the Marital Trust established under Article III, hereof; therefore I direct that all investments related to such Marital Trust be made in a manner consistent with such objective."

 Allocation of Expenses between Income and Principal

"The trustee shall have the power to allocate any property received or charge incurred to principal or income or partly to each, as the trustee may think reasonably appropriate."

 Treatment of beneficiaries in terms of intent, and priority.

"My first priority and intention in establishing this trust is the care and maintenance of my wife during her lifetime, and my Trustee shall in all respects in administering this Trust make every effort to fulfill that intention."

7. The Beneficial Interests Created by the Trust

□ *Drafting Objective*

The interests of the trust beneficiaries in the income and principal of the trust are determined by the trust document. The document, if properly drafted, will ensure that the settlor's objectives in regard to the current beneficiaries and remaindermen are realized. In many cases beneficial interests provided in the trust may be subject to the discretion of the trustee. In other cases, the trustee's discretion may be limited by an "ascertainable standard;" and in still other cases, trust distributions may be mandatory. The trust agreement may also grant the trust beneficiary or beneficiaries the right to withdraw income or principal at their own discretion. In drafting a testamentary trust, it is your job to first determine the objectives of the settlor in creating the trust, and then draft the trust document to fit those objectives.

□ *Distributions of Income and Principal*

The question of what type of discretion is granted to the trustee to make distributions of income and principal, and what rights the beneficiaries have to cause such distributions, must be addressed in the trust document. Distributions of principal and income are generally either: (i) within the discretion of the trustee, (ii) within the discretion of the trustee but subject to an ascertainable standard, (iii) mandatory; i.e., the trustee has no discretion in determining whether a distribution should or should not be made, or (iv) subject to a right granted to the trust beneficiary to require a distribution of income or principal.

An important point, when we are discussing "income" and "principal" for this purpose, remember we are referring to "income" and "principal" as defined for fiduciary accounting purposes. This means "income" earned during the trust term, and is defined in a manner similar to how that term is defined for tax and accounting purposes; i.e., dividends, interest, rents, royalties, etc., and principal is basically everything else. The most notable difference is that the gain realized on the sale or exchange of principal, e.g., capital gain for tax purposes, is for fiduciary accounting purposes considered principal and not income.

□ *The Discretion of the Trustee*

In certain trusts, the exercise of a power to make distributions of principal or income of the trust is left to the discretion of the trustee. For example the trust could provide:

"The settlor's spouse shall be entitled to such distributions of principal and income as determined in the discretion of the trustee."

According to the Comment under § 87 Restatement (Third) Trusts, a court will not normally interfere when that conduct is "reasonable, not based on an improper interpretation of the terms of the trust, and not otherwise inconsistent with the trustee's fiduciary duties."

However, a court can intervene in order to prevent “a trustee's abuse (including by misinterpretation) of discretionary authority.”

- *Absolute Discretion*

In some cases the trust provision may imply a greater degree of discretion in the exercise of the trustee's discretionary judgment. This may be indicated by words such as “absolute discretion" “sole discretion” or "uncontrolled discretion.” This is sometimes referred to as “extended discretion.” Both the common law and the UTC provide that, notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, the trustee must exercise that discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries. Here is an example:

“To make principal distributions to my son, ROBERT, to ensure his well-being as determined in the absolute discretion of my Trustee.”

- *Discretion Subject to an Ascertainable Standard*

In certain cases, the trust will provide that the trustee’s discretion is limited by a standard. A trust could provide something like the following:

“The settlor’s spouse shall be entitled to such distributions of principal to provide for her health, education, support, and maintenance.”

This standard of discretion is often referred to as an “ascertainable standard.” This means the term will have an accepted and defined meaning which provides a standard by which the exercise of discretion by the trustee can be measured. If such a standard is provided in the trust it both directs the action of the trustee, and at the same time creates an entitlement to the defined benefit on behalf of the beneficiaries which is enforceable by the court.

According to§ 50(2) of the Restatement (Third) Trusts, “the benefits to which a beneficiary is entitled, and what may constitute an abuse of discretion by the trustee, depend on the terms of the discretion, including the proper construction of any accompanying standards, and on the settlor's purposes in granting the discretionary power and in creating the trust.”

For example, the terms "support" and "maintenance” are generally construed to mean the beneficiary's “accustomed standard of living or station in life.” The term "education," without elaboration, is defined “as extending to payment of living expenses as well as fees and other costs of attending an institution of higher education, or the beneficiary's pursuit of a program of trade or technical training, and the like, as may be reasonably suitable to the individual and to the trust funds available for the purpose.”

- *Mandatory Provisions*

Often a trust instrument will require that the trustee make mandatory distributions of income and principal. Such distributions could be required at stated intervals, such as the following:

"One half of the principal in the trust shall be paid to the child at age 25, and the balance at age 30."

Alternatively, mandatory trust distributions might be required upon the occurrence of significant events such as graduating college, marriage or the birth of a child.

"I direct the trustee then serving to distribute $10,000 to each of my grandchildren upon their graduating from college."

Sometimes, trust documents will include a provision which requires the mandatory distribution of trust income, such as the following:

"Income shall be distributed on an annual basis in quarterly installments."

Mandatory income provisions like those above have an income tax effect which should be considered. For the most part, trusts are taxed in much the same manner as individuals; however, there are some significant differences. One significant difference is that trusts are allowed a deduction against taxable income for distributions of income made to beneficiaries. Simplistically, trusts are taxed on the income retained by the trust and the beneficiaries are taxed on the income distributed to them. For this reason, estates and trusts are sometimes referred to for tax purposes as "semi- conduits."

The Internal Revenue Code makes a distinction between what are termed "simple trusts" and "complex trusts." This distinction is important for purposes of understanding and applying the concept of "distributable net income." A "simple trust" is a trust which is required under the terms of the trust to distribute currently all of its income for the taxable year. A "complex trust," on the other hand, is any trust other than a simple trust.

In the case of a "simple trust," IRC § 651(a) allows a deduction for the "amount of the income" for the taxable year which is "required to be distributed currently." Complex trusts are allowed a deduction under IRC § 661(a) equal to the sum of: (i) any amount of income required to be distributed currently; and (ii) any other amounts properly paid or credited or required to be distributed. This means that a provision that requires all of the income of the trust to be distributed will insure that the income earned by the trust will be taxed to the beneficiaries of the trust. This result occurs even if the income that must be distributed is not actually distributed. This occurs because the trust beneficiary could through an appropriate court proceeding cause the trustee to distribute that income currently. This is a good idea from the point of view of taxation since trusts are taxed at the highest income tax rates at a comparatively lower level of taxable income compared to individual taxpayers. Whether this is a good idea from the point of view of managing the trust in the best interest of the trust beneficiary is another matter.

Another, possibility is that the trustee could be required to distribute all of the trust income, but be allowed the discretion as to the amounts to be paid to various trust beneficiaries. This is sometimes termed a "sprinkle power." The following is an example:

"To pay to such one or more or all my children all the net income of the Trust each year, in such proportions, equal or unequal, as my Trustee, in my Trustee's sole discretion, deems advisable."

Alternatively, the trust may require that income be retained by the trust, and added to principal:

"The income of the trust shall be accumulated and added to principal until my son, ROGER, attains age 21 years old, and thereafter shall be distributed to him no less frequently than annually."

- *Withdrawal Rights Held by the Trust Beneficiary*

In certain cases the testator may wish to grant a trust beneficiary the right to withdraw amounts from the trust at his or her option. A provision like the following could be used:

"My wife shall have the right every year to withdraw the entire balance of the trust by written request delivered to the trustee.

Often this right of withdrawal is limited as provided in the following way:

"My wife shall have the right every year to withdraw the greater of (1) Five Thousand Dollars ($5,000) or (2) five percent (5%) of the value of the trust on December 31 of that year."

This provision is sometimes termed a "five and five" power. The failure to exercise a withdrawal power is considered a release of the power which results in a taxable gift for federal gift tax purposes, but only to the extent the property which could have been withdrawn through the exercise of such power could have exceeded the greater of $5,000, or 5% of the aggregate value of the trust.

- *The Total Return Trust*

Traditionally, a trust might be structured along the following lines:

L forms a trust which provides that all of the "income" of the trust is distributed no less frequently than annually to his son, M. Upon the death of M, the remaining balance of the trust, including principal and undistributed income, is distributed outright and free of trust to K.

Such a structure often created a conflict for the trustee in regard to the manner in which the trust assets should be invested. M as income beneficiary, would presumably like to see the trust assets invested in high yield investments in order to maximize the current yield and the income of the trust. On the other hand the remainderman, K, would most likely favor investments that produced long term growth and therefore growth of principal. A natural conflict arises for the trustee because unless the trust instrument provides otherwise, the

trustee is bound by a duty of impartiality to both the income beneficiary M, and the remainderman, K.

Modern portfolio theory as embodied in the Uniform Prudent Investor Act acknowledges and addresses this conflict. Section 2(b) of the Act provides that "A trustee's investment and management decisions respecting individual assets must be evaluated not in isolation but in the context of the trust portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust." This approach allows the trustee to formulate an overall investment strategy which looks to total return on investment, i.e., both income and growth of principal, and is not focused simply on maximizing either income or principal appreciation.

From a drafting and planning point of view, the "total return trust" is an attempt to resolve the conflict by replacing the traditional income interest with a "unitrust" interest, which might read as follows:

"The trust shall pay to L, no less than annually an amount equal to five (5%) percent of the net fair market value of the assets of the trust valued as of the first day of each taxable year of the trust (the "valuation date")."

In terms of fiduciary accounting, the issue raised by the advent of modern portfolio theory and the total return trust is whether traditional definitions of "income" still apply. That is, if the trust contains a unitrust provision is the trustee allowed to fund it with what would be considered "income" under traditional fiduciary accounting concepts?

- *Disposition of the Remainder Interest*

Of course, it is important that the trust provides for the disposition of the balance remaining in the trust at the end of the trust term. The following are examples of such a provision:

"Upon my wife's death, the then remaining trust balance shall be divided into equal shares and distributed to each of my then living children, outright and free of trust."

Alternatively -

"When a child of the Settlor reaches the age of twenty-five (25) years, or upon division of the trust estate into shares if such child has then reached that age, the Trustee shall distribute to the child the balance of his or her trust share."

8. Administrative Duties of the Trustee

- *General Powers and Duties of Trustees*

In administering a trust, subject to the trustee's fiduciary duties discussed in the preceding material, a trustee generally holds the powers conferred by the terms of the trust, and except as limited by the terms of the trust all powers over the trust property which an unmarried competent owner has over individually owned property. In addition, the trustee is

generally vested with any other powers appropriate to carry out "the terms and purposes of the trusts," and achieve the proper investment, management, and distribution of the trust property.

Under the common law, a trustee has the affirmative duty to not comply with trust provisions which are impractical or impossible to perform, or which are "unlawful or against public policy." When in doubt as to the proper interpretation of the powers or duties of the trustee, the trustee or trust beneficiary "may apply to an appropriate court for instructions."

- *Specific Powers of Trustee*

In addition to the general powers discussed in the preceding material, § 816 of the Uniform Trust Code provides a trustee will generally hold the following specific powers unless otherwise restricted by the provisions of the trust:

PEF Code § 7780.5 provides that except as provided in the trust, a trustee has all the powers over the trust property that an unmarried competent owner has over individually owned property and may exercise those powers without court approval from the time of creation of the trust until final distribution of the assets of the trust. Under PEF Code § 7780.6, these powers include the following:

"(a) Listing. --The powers which a trustee may exercise pursuant to section 7780.5 (relating to powers of trustees -- UTC 815) include the following powers:

(1) To accept, hold, invest in and retain investments as provided in Chapter 72 (relating to prudent investor rule).

(2) To pay or contest a claim; settle a claim by or against the trust by compromise, arbitration or otherwise; and release, in whole or in part, any claim belonging to the trust.

(3) To resolve a dispute regarding the interpretation of the trust or the administration of the trust by mediation, arbitration or other alternative dispute resolution procedures.

(4) To prosecute or defend actions, claims or proceedings for the protection of trust assets and of the trustee in the performance of the trustee's duties.

(5) To abandon or decline to administer any property which is of little or no value, transfer title to abandoned property and decline to accept title to and administer property which has or may have environmental or other liability attached to it.

(6) To insure the assets of the trust against damage or loss and, at the expense of the trust, protect the trustee, the trustee's agents and the beneficiaries from liability to third persons arising from the administration of the trust.

(7) 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. The trustee has a lien on the trust assets as against the beneficiary for an advance under this paragraph, including interest on the advance.

(8) To pay taxes, assessments, compensation of the trustee and employees and agents of the trustee and other expenses incurred in the administration of the trust.

(9) To receive additions to the assets of the trust.

(10) To sell or exchange any real or personal property at public or private sale, without obligation to repudiate an otherwise binding agreement in favor of better offers. If the trustee has been required to give bond, no proceeds of the sale of real estate, including proceeds arising by the reason of involuntary conversion, shall be paid to the trustee until:

(i) the court has made an order excusing the trustee from entering additional security; or

(ii) the court has made an order requiring additional security and the trustee has entered the additional security.

(11) 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.

(12) To grant options for sales or leases of a trust asset and acquire options for the acquisition of assets, including options exercisable after the trust terminates.

(13) To join in any reorganization, consolidation, merger, dissolution, liquidation, voting trust plan or other concerted action of security holders and to delegate discretionary duties with respect thereto.

(14) To vote a security, in person or by general or limited proxy, with or without power of substitution.

(15) To borrow funds and mortgage or pledge trust assets as security for repayment of the funds borrowed, including repayments after the trust terminates.

(16) To make loans to and buy property from the personal representatives of the settlor and the settlor's spouse. Loans under this paragraph shall be adequately secured, and the purchases under this paragraph shall be for fair market value.

(17) To partition, subdivide, repair, improve or develop real estate; enter into agreements concerning the partition, subdivision, repair, improvement, development, zoning or management of real estate; impose or extinguish restrictions on real estate; dedicate land and easements to public use; adjust boundaries; and do anything else regarding real estate which is commercially reasonable or customary under the circumstances.

(18) With respect to possible liability for violation of environmental law:

(i) to inspect or investigate property the trustee holds or has been asked to hold or property owned or operated by an organization in which the trustee holds or has been asked to hold an interest, for the purpose of determining the application of environmental law with respect to the property;

(ii) to take action to prevent, abate or otherwise remedy any actual or potential violation of environmental law affecting property held directly or indirectly by the trustee, whether taken before or after the assertion of a claim or the initiation of governmental enforcement;

(iii) to decline to accept property into trust or disclaim a power with respect to property that is or may be burdened with liability for violation of environmental law;

(iv) to compromise claims against the trust which may be asserted for an alleged violation of environmental law; and

(v) to pay the expense of inspection, review, abatement or remedial action to comply with environmental law.

(19) To operate, repair, maintain, equip and improve any farm or farm operation; to purchase and sell livestock, crops, feed and other property that is normally perishable; and to purchase, use and dispose of farm equipment and employ one or more farm managers and others in connection with farm equipment and pay them reasonable compensation.

(20) To make ordinary or extraordinary repairs or alterations in buildings or other structures; demolish improvements; and raze existing or erect new party walls or buildings.

(21) To enter into a lease or arrangements for exploration and removal of minerals or other natural resources or enter into a pooling or utilization agreement.

(22) To exercise all rights and incidents of ownership of life insurance policies held by the trust, including borrowing on policies, entering into and terminating split- dollar plans, exercising conversion privileges and rights to acquire additional insurance and selecting settlement options.

(23) To employ a custodian; hold property unregistered or in the name of a nominee, including the nominee of any institution employed as custodian, without disclosing the fiduciary relationship and without retaining possession and control of securities or other property so held or registered; and pay reasonable compensation to the custodian.

(24) To apply funds distributable to a beneficiary who is, in the trustee's opinion, disabled by illness or other cause and unable properly to manage the funds directly for the beneficiary's benefit or to pay such funds for expenditure on the beneficiary's behalf to:

(i) the beneficiary;

(ii) a guardian of the beneficiary's estate;

(iii) an agent acting under a general power of attorney for the beneficiary; or

(iv) if there is no agent or guardian, a relative or other person having legal or physical custody or care of the beneficiary.

(25) To pay funds distributable to a minor beneficiary to the minor or to a guardian of the minor's estate or to apply the funds directly for the minor's benefit.

(26) To do any of the following:

(i) Pay any funds distributable to a beneficiary who is not 21 years of age or older to:

(A) the beneficiary;

(B) an existing custodian for the beneficiary under Chapter 53 (relating to Pennsylvania Uniform Transfers to Minors Act) or under any other state's version of the Uniform Transfers to Minors Act;

(C) an existing custodian for the beneficiary under the former Pennsylvania Uniform Gifts to Minors Act or under any other state's version of the Uniform Gifts to Minors Act; or

(D) a custodian for the beneficiary appointed by the trustee under Chapter 53.

(ii) Apply the funds for the beneficiary.

(27) To pay calls, assessments and other sums chargeable or accruing against or on account of securities.

(28) To sell or exercise stock subscription or conversion rights.

(29) To continue or participate in the operation of any business or other enterprise and to effect incorporation, merger, consolidation, dissolution or other change in the form of the organization of the business or enterprise.

(30) To select a mode of payment under a qualified employee benefit plan or a retirement plan payable to the trustee and exercise rights under the plan.

(31) To distribute in cash or in kind or partly in each and allocate particular assets in proportionate or disproportionate shares.

(32) To appoint a trustee to act in another jurisdiction with respect to trust property located in the other jurisdiction, confer upon the appointed trustee all the powers and duties of the appointing trustee, require that the appointed trustee furnish security and remove the appointed trustee.

(33) To exercise elections with respect to Federal, State and local taxes.

(34) To execute and deliver instruments which will accomplish or facilitate the exercise of the trustee's powers.

(b) Effect. --The trustee shall have no further responsibility or liability for funds upon any of the following:

(1) Payment under subsection (a)(24).

(2) Payment under subsection (a)(25).

(3) Payment or application under subsection (a)(26)."

Because these powers are so comprehensive you may only feel it necessary to include a provision such as the following:

"Administrative Powers of the Trustee

The Trustee then serving shall have the powers conferred on the Trustee under Pa.C.S. Sec. 7780.5, which shall include all of the illustrative powers provided in Pa. C.S. Sec. 7780.6."

9. Investment Provisions

The PEF Code – The Prudent Investor Rule

Under PEF Code § 7780.6 (a)(1), absent contrary provisions in the trust document a trustee has the power:

"(1) To accept, hold, invest in and retain investments as provided in Chapter 72 (relating to prudent investor rule)."

Section 7203 of the PEF Code adopts the "prudent investor rule," which provides the standard by which a trustee must invest and manage property held in a trust unless it is otherwise provided in the trust document. Under the prudent investor rule, a trustee must invest trust funds as a prudent investor would, by considering the purposes, terms and other circumstances of the trust and by pursuing an overall investment strategy reasonably suited to the trust. A fiduciary may invest in every kind of property and type of investment, including, but not limited to, mutual funds and similar investments, but in making investment and management decisions, a fiduciary shall consider, among other things, to the extent relevant to the decision or action:

- The size of the trust;
- The nature and estimated duration of the fiduciary relationship;
- The liquidity and distribution requirements of the trust;
- The expected tax consequences of investment decisions or strategies and of distributions of income and principal;
- The role that each investment or course of action plays in the overall investment strategy;
- An asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries, including, in the case of a charitable trust, the special relationship of the asset and its economic impact as a principal business enterprise on the

community in which the beneficiary of the trust is located and the special value of the integration of the beneficiary's activities with the community where that asset is located;

- To the extent reasonably known to the fiduciary, the needs of the beneficiaries for present and future distributions authorized or required by the governing instrument; and

- To the extent reasonably known to the fiduciary, the income and resources of the beneficiaries and related trusts.

- Under the prudent investor rule, the standard of prudence is applied to any investment as part of the total portfolio, rather than to individual investments. In the trust context the term "portfolio" embraces all the trust's assets. Balancing risk and return is identified as the fiduciary's central consideration, and all categorical restrictions on types of investments have been abrogated. As a result, the trustee can invest in anything that plays an appropriate role in achieving the risk/return objectives of the trust and meets the other requirements of prudent investing. The long familiar requirement that fiduciaries must diversify their investments has been integrated into the definition of prudent investing. The much criticized former rule of trust law forbidding the trustee to delegate investment and management functions has been reversed, and delegation of investment authority is now permitted, subject to safeguards.

- Under PEF § 7780.6(a)(1), the governing instrument may override the prudent investor rule. If that is consistent with the settlor's intent, a provision like the following could be used:

  "The Trustee shall only be authorized to invest the trust estate in triple A rated municipal bonds, irrespective of any statutes or rules of law permitting the investment of trust funds in other types of investments."

9. Appointment and Removal of the Trustee

Overview

The "trustee" is the person or entity that holds legal title to the trust property and manages that property for the benefit of the trust beneficiary. The interests of the beneficiaries are protected under law against mismanagement or misappropriation by the trustee. In performing its duties the trustee is held to a "fiduciary standard" of conduct. Fundamentally, the fiduciary standard requires a duty of loyalty and a duty of prudence – that is, the trustee must act for the sole benefit of the trust beneficiaries and in a prudent manner in administering the trust. The fiduciary standard also includes a host of subsidiary duties which act to reinforce the duties of loyalty and prudence. The duties and powers of the trustee will be discussed in the following material.

Who Can Serve

Any individual who has the capacity "to hold property as a beneficial owner" has capacity to serve as a trustee. This generally means that minors and incompetent adults may not serve. In some jurisdictions non-residents and non-citizens of the United States are also barred from serving as trustees. A corporation can also serve as trustee unless it is limited by the law of the jurisdiction in which it operates. In Pennsylvania for example, only banks, trust companies, and certain savings banks are authorized to act as trustees. Under the doctrine of "merger" the same person or entity cannot be the sole trustee and the sole beneficiary of a trust. However, a trust does not terminate "when one of several beneficiaries becomes one of several trustees, or the sole trustee," or when "the sole beneficiary becomes one of several trustees."

Choosing the Trustee

Choosing a trustee is an individual choice based on the facts and circumstances of each case. Obviously, whoever is chosen should be a responsible individual who is sensitive to the needs of the beneficiaries but also willing to adhere to the purposes for which the trust was created. It is also important that the document appoint a successor trustee, and that the document provide an internal mechanism for the appointment of a trustee if there is an unfilled vacancy.

If the wrong trustee is chosen, the settlor, a co-trustee, or a beneficiary may request that the Orphans' Court remove the trustee. The Orphans' Court may also remove a trustee on its own initiative if it finds that removal of the trustee best serves the interests of the beneficiaries of the trust, is not inconsistent with a material purpose of the trust, and a suitable co-trustee or successor trustee is available. In addition, the court must believe that either: (i) the trustee has committed a serious breach of trust; (ii) the lack of cooperation among co-trustees substantially impairs the administration of the trust; (iii) the trustee has not effectively administered the trust because of the trustee's unfitness, unwillingness or persistent failures; or (iv) there has been a substantial change of circumstances.

- *Trustee Provisions*

Of course you will need to include a provision such as the following in order to appoint the original trustee. It is always a good idea to appoint at least one successor trustee in case the original trustee fails to serve for whatever reason.

"XV. Trustees.

A. I appoint my wife, ELLEN, as Trustee. If my wife, ELLEN, fails to qualify or ceases to act for any reason, I appoint ROBERT MITCHELL, Trustee in her place."

The following provision deals with how co-trustees shall agree to decisions:

"B. If more than two Trustees are serving hereunder then all decisions shall be as agreed by the majority; if two Trustees are serving then all decisions shall be unanimous."

This provision allows the trustee or trustees then serving to appoint a successor trustee. This will avoid the need to petition the Orphans' Court to fill an unanticipated vacancy.

"C. Each individual Trustee of any trust hereunder, then serving, may unanimously appoint, in writing:

1. An individual to serve with them as co-Trustee;

2. An individual to serve in his or her place; provided that any such appointment shall not supersede any designation made above of a successor Trustee.

D. The individual Trustees, with the written consent of the above described class of persons, may appoint a corporation organized under the laws of the United States or any State thereof and possessed of trust powers, which has trust assets of at least One Hundred Million Dollars ($100,000,000), as successor corporate Trustee."

The following provision waives the need to post for the Trustee to post a bond:

"E. The Trustee shall not post security in any jurisdiction."

10. Other Essential Provisions

□ *The Rule Against Perpetuities*

The common-law Rule Against Perpetuities prohibits a grant of an estate unless the interest must vest, if at all, no later than 21 years (plus a period of gestation to cover a posthumous birth) after the death of some person alive when the interest was created. Under this rule it is sometimes said that a trust must end within lives in existence plus twenty-one years. Pennsylvania has adopted the "wait and see approach" to the rule, as codified in Section 6104 of the PEF Code. That section provides that the expiration of the period allowed by the common law rule against perpetuities is measured by actual rather than possible events.

You might consider a "savings clause" like the following which should make sure the Rule is not violated:

"Notwithstanding any other provisions hereunder, If any trust created under this instrument has not already terminated by its terms, it shall terminate one day before the expiration of twenty-one years after the death of the survivor of such of my descendants that are living at my death. In the case of such termination, the remaining income and principal of such trust shall then be distributed absolutely to the then income beneficiaries of the trust in proportion to their respective interests in the income."

□ *Spendthrift Clause*

A spendthrift clause protects the trust assets from creditors of any beneficiary, transferees or others making a claim through or against a beneficiary. A beneficiary may not transfer an interest in a trust in violation of a valid spendthrift provision. With certain exceptions, a creditor or assignee of the beneficiary of a spendthrift trust may not reach the interest or a distribution by the trustee before its receipt by the beneficiary.

A spendthrift provision is unenforceable against: (a) a beneficiary's child who has a judgment or court order against the beneficiary for support or maintenance, to the extent of the beneficiary's interests in the income and principal of the trust; (b) any other person who has a judgment or court order against the beneficiary for support or maintenance, to the extent of the beneficiary's interest in the trust's income; (c) a judgment creditor who has provided services for the protection of the beneficiary's interest in the trust; and (d) a claim of the United States or the Commonwealth to the extent Federal law or a statute of this Commonwealth provides.

A claimant against whom a spendthrift provision cannot be enforced may obtain from a court an order attaching present or future distributions to or for the benefit of the beneficiary. The court may limit the award to such relief as is appropriate under the circumstances. Under 20 Pa. CSA § 7742(a) of the PEF Code, a spendthrift provision is valid only if it restrains both voluntary and involuntary transfer of a beneficiary's interest. A trust instrument providing that the interest of a beneficiary is held subject to a "spendthrift trust," or words of similar import, is sufficient to restrain both voluntary and involuntary transfer of the beneficiary's interest.

A typical spendthrift clause reads as follows:

“Until distributed, no gift or beneficial interest shall be subject to anticipation or to voluntary or involuntary alienation.”

- *Tax Clause*

In General

A tax allocation provision will determine which gifts bear the burden of the death taxes incurred by the estate. Absent such a provision, the PEF Code will dictate the allocation.

The Statutory Rules

Federal Estate Tax

Under PEF Code 20 Pa. CSA § 3701, a testator may direct how the federal estate tax or the federal generation-skipping transfer tax, including interest and penalties, are to be apportioned among the various gifts made under the will. Alternatively, 20 Pa. CSA § 3701 allows the testator to grant the discretionary power to someone else, such as the executor, to make the determination. Absent directions in the will, PEF Code 20 Pa. CSA § 3702 provides that the federal estate tax is to be apportioned equitably among all parties interested in property includible in the gross estate for federal estate tax purposes in proportion to the value of the interest of each party, subject to certain limitations. Under 20 Pa. CSA § 3702, no apportionment is made to pre-residuary gifts, and the tax is allocated to the residue as an administration expense. However, if a gift of a portion of the residue gives rise to a charitable or marital deduction, taxes will not be apportioned to that gift unless the remaining assets are insufficient to pay the taxes.

Example:

The testator dies with a net probate estate of $10,500,000. Bequests under the will include the following: (i) a specific bequest of property with a fair market value of $5,250,000 to the son of the testator, and (ii) the residue of the estate to the daughter of the testator. The federal estate tax incurred by the estate is $2,100,000. Absent a tax allocation provision to the contrary, that tax is apportioned under the PEF Code as follows: (i) no tax is apportioned to the $5,250,000,000 specific bequest distributed to the son, and (ii) the entire $2,100,000 federal estate tax is apportioned against the residue passing to the daughter. As a result, the testator's son inherits $5,250,000, and, after the tax bill is paid, the testator's daughter inherits $3,150,000.

Example:

The testator dies with a net probate estate of $15,750,000. Bequests under the will include the following: a specific bequest of property worth $5,250,000 to the testator's son, and the residue is to be divided equally between the testator's spouse and daughter.

Again, the federal estate tax on the estate is $2,100,000, because in this example the one-half of the residue which passes to the spouse qualifies for the federal estate tax marital deduction and will not be subject to the estate tax. Absent a tax allocation provision to the contrary, that tax is apportioned under the PEF Code as follows: (i) again, no tax is apportioned to the $5,250,000, specific bequest distributed to son, and (ii) no tax is apportioned to the portion of the residue which passes to the testator's spouse, which qualifies for the federal estate tax marital deduction. The entire $2,100,000 of federal estate tax will be apportioned against the residue passing to the daughter. As a result, the testator's son inherits $5,250,000 and the testator's spouse inherits $5,250,000, both unreduced by federal estate tax. After the federal estate tax bill is paid, the testator's daughter inherits $3,150,000.

<u>Pennsylvania Death Taxes</u>

Pennsylvania death taxes include both Pennsylvania Inheritance Tax and the Pennsylvania Estate Tax. The testator has the power to apportion both the Inheritance Tax and the Estate Tax as directed by a provision in the will. Absent a contrary intent in the will, the tax on outright pre-residuary gifts falls on the residue as a general administration expense. Liability for tax on non-probate assets rests with the recipient of the property. The apportionment of the Pennsylvania Estate Tax is determined in the same way as the federal estate tax, as discussed previously.

Example

The testator dies with a net probate estate of $600,000. Bequests under the will include the following: a specific bequest of $200,000 to the son of the testator, which under the Pennsylvania Inheritance Tax will be taxed at 4.5%; ½ of the residue to the brother of the testator taxed at 12%; and ½ of the residue to the daughter of the testator taxed at 4.5%. The total tax on the estate is $42,000, apportioned under the PEF Code as follows: (i) the $200,000 specific bequest is distributed to son unreduced by tax, (ii) the entire $42,000 of Pennsylvania

Inheritance Tax is apportioned against the residue as an administration expense, leaving $358,000, after tax to be divided equally between the testator's brother and daughter, with each receiving $179,000.

- Tax Allocation Provisions

In General

A tax allocation provision acts to direct the executor in the manner in which death taxes incurred by the estate, both federal and state, are to be charged. In every case, the net after-tax-effect of the tax provision provided in the will on the client's probate and non-probate dispositions should be reviewed with the client. The question to be answered is "How much is the net-after-tax-gift each heir will receive after the allocation of the estate and inheritance taxes?"

Alternative Will Provisions

Some alternatives to the allocation provision cited above will be discussed in this section. The following example of a typical tax provision provides that the death taxes incurred are to be paid out of the residuary estate.

"(a) All death taxes (and interest and penalties thereon) imposed as a result of my death shall be paid out of my residuary estate."

Another way to word this is as follows:

"(a) All death taxes (and interest and penalties thereon) imposed as a result of my death upon property regardless of whether passing under my Will, shall be paid out of the principal of my residuary estate, each share thereof, whether outright or in trust, to bear a pro rata portion of such taxes."

These provisions result in the taxes generated by both the probate estate and non-probate assets being paid out of the residue of the probate estate. This means that the residuary estate will be reduced by the death taxes generated by the entire estate, and other gifts will pass free of tax. If the following provision were used, a different result would occur:

"(a) All death taxes (and interest and penalties thereon) imposed as a result of my death upon property passing under my Will, shall be paid out of the principal of my residuary estate, each share thereof, whether outright or in trust, to bear a pro rata portion of such taxes."

Under this provision, a person receiving an IRA distribution would be responsible for the Inheritance Tax incurred by that distribution the balance would fall on the residue. Perhaps a more equitable result could be achieved if the following clause could be employed:

"(a) The death taxes (and interest and penalties thereon) imposed as a result of my death shall be paid follows:(1) the liability for such tax on property passing under this will, to be

charged against each such gift in the amount of tax incurred by each such gift; and (2) the liability for tax on non-probate assets shall rest with the recipient of such property."

Consistency with Will

In drafting a tax clause for a trust instrument it is important that the tax clause in the Trust be consistent with that in the Will. If the intent is that the trust bear all of the death taxes, the following clauses could be considered

In the Will:

"All "death taxes", as hereinafter defined, incurred by reason of my death shall be paid directly from the principal of the John Doe Revocable Trust as provided in paragraph NINTH of such trust."

In the Trust:

"NINTH: Upon the Grantor's death, the Trustees shall pay to the grantor's estate an amount equal to the total of all estate, inheritance and other death taxes (including any interest thereon and penalties with respect thereto), federal, state and other, imposed by reason of the Grantor's death in respect of property held by the trust, passing under the terms of the Grantor's will or otherwise."

If the Trust is only to bear its fair share of the taxes, the following clauses could be provided:

In the Will:

"The "death taxes", to be paid by the John Doe Revocable Trust by reason of my death shall be paid directly from the principal of the John Doe Revocable Trust as provided in paragraph NINTH of such trust."

In the Trust:

"NINTH: Upon the Grantor's death, the Trustees shall pay to the grantor's estate an amount equal to the trust's fair share, determined as provided below, of all estate, inheritance and other death taxes (including any interest thereon and penalties with respect thereto), federal, state and other, imposed by reason of the Grantor's death in respect of property held by the trust or otherwise. The trust's fair share of such taxes shall be determined by the executors or administrators for each tax separately and, for each tax, shall be the proportion of the tax which the value of the property held by the trust in respect to which the tax is imposed bears to the value of all property in respect to which the tax is imposed. A tax shall not be considered imposed in respect to property to the extent of any deduction, credit, exemption or exclusion allowed in respect to such property. The determination by the executors or administrators of the amount payable under this article shall be final, and the Trustees shall pay such sums without making inquiry into their accuracy. Upon making payment of the amounts determined, the

Trustees shall be discharged from any liability with respect to such payments and from further accountability therefor. Such payments shall be made out of the principal of the trust."

- Business Clause

Court approval is required for a trustee to carry on business activities of the decedent in the absence of a provision in the trust instrument granting such power. 20 Pa CSA §3314 by reference, provides that the Orphan's Court, aided by the report of a master if necessary, may authorize the personal representative to continue any business of the estate for the benefit of the estate and in doing so the court, for cause shown, may disregard the provisions of the governing instrument, if any.

In order to allow the trustee to carry on a business of the settlor within a trust, a business powers clause should be included in the trust instrument. The powers that are typically included in the business powers clause are the following: (a) liquidate the business; (b) enter into partnerships; (c) incorporate; (d) vote to merge or consolidate; and (e) borrow funds;

The following is a sample Business Powers Clause:

"Business Powers. With respect to any interest I may have at my death in any closely-held business whether as partner, stockholder or otherwise and any business with which such closely-held business may merge or consolidate, I give my Trustee the authority to deal with any business interest as freely as I could have done during my lifetime. This authority shall be subject to any Agreement binding upon this Trust, which affects such interest. Without limiting the general authority granted under this Paragraph, I give my Trustee the following specific authority:

(a) To do anything my Trustee considers advisable with respect to the incorporation, operation or liquidation of any such business and with respect to any change in its purpose, nature or structure, including but not limited to the following:

1. To enter into partnership agreements and amendments thereto.

2. To organize a corporation, without leave of court, to carry on any business alone or with others, and to contribute all or part of the assets of such business as capital to such corporation and to accept stock in the corporation in exchange therefore.

3. To vote the shares of any closely-held corporate stock and to determine the advisability of, fix the terms of, and participate in, any corporate reorganization, merger, consolidation, dissolution, public offering, pooling of interest, exchange of stock or similar transaction.

(b) To elect or employ as director, officer, employee or agent of any such business, any person, including my Trustee, or any employee of a corporate Trustee, and to delegate authority to, compensate and remove or discharge any such person.

(c) To create or cause to be created within any such business such deferred compensation or other employee benefit plan, as my Trustee considers advisable.

(d) To extend to any employee of any such business an option to participate in the ownership thereof, or profits therefrom, upon such terms and conditions as my Trustee considers advisable.

(e) To cause to be made and to consent to the making or the continuation of any loans to such business, and to pledge assets of such business as collateral therefor, with any bank or other financial institution.

(f) The fact that my Trustee may be an officer, director or employee of any such business and may own an interest in such business in an individual capacity shall not, insofar as this Trust is concerned, constitute an adverse or conflicting interest, and the acts of my Trustee as such shall be considered as if my Trustee owned no stock and did not serve as an officer, director or employee of said business.

(g) I release my Trustee from any liability for any depreciation in value or loss by reason of the retention of any such business interest except for depreciation or loss resulting from fraudulent acts of my Trustee in connection therewith."

- Situs Clause.

20 Pa. CSA § 7708, of the PEF Code provides that provisions of a trust instrument designating the situs of the trust are valid and controlling if: (a) a trustee's principal place of business is located in or a trustee is a resident of the designated jurisdiction; (b) all or part of the trust administration occurs in the designated jurisdiction; or (c) one or more of the beneficiaries resides in the designated jurisdiction.

If the trust instrument does not specify a situs the situs of a testamentary trust is in the county where letters were granted to the personal representative if letters have not been granted, in a county where the letters might have been granted. The situs of an inter vivos trust whose settlor is domiciled in this Commonwealth when the trust becomes irrevocable or, in the case of a revocable trust, when the first application is made to a court concerning the trust during the settlor's lifetime, either in the county of the settlor's principal residence or in the county in which any of the trustees resides or has a place of business; and after the settlor's death either; (i) in the county in which letters have been granted to the settlor's personal representative; (ii) in a county in which letters might have been granted; (iii) in a county which is the principal place of the trust's administration; or (iv) in a county in which any trustee resides or has a place of business.

The situs of an inter vivos trust whose settlor either is living and not domiciled in this Commonwealth at the time when the first application is made to a court concerning the trust or was not domiciled in this Commonwealth at the settlor's death after which the first application to a court concerning the trust is made thereafter shall be in a county where: (i) a trustee's

principal place of business is located or a trustee is a resident; (ii) all or part of the trust administration occurs; or (iii) one or more of the beneficiaries reside.

Sample language

"This Trust has been accepted by my Trustee in the Commonwealth of Pennsylvania, and except as provided in Paragraph EIGHTEENTH (g), its situs shall be in that Commonwealth, and all questions pertaining to its validity, construction and administration shall be determined in accordance with the laws of that Commonwealth."

Note: Paragraph Eighteenth (g) could provide that the trustee or trustees has the power to transfer the situs of the trust as follows:

"If any corporate or individual Trustee is located in a State other than the Commonwealth of Pennsylvania, my Trustees acting unanimously may, but are not required to, direct in writing that the situs of the Trust be transferred to the State in which such Trustee is located. Any such transfer of situs shall be effective only if the court then having jurisdiction over the Trust shall concurrently transfer jurisdiction over the Trust to the appropriate court in said State. In the event of a transfer of situs, all questions subsequently arising pertaining to the construction and administration of the Trust shall be determined in accordance with the laws of the State to which situs and jurisdiction have been transferred."

VIII. Automatic Modification by Circumstances

- *Overview*

The occurrence of certain changes in circumstances or the occurrence of certain events will automatically act to modify a will without the further act of the testator. Under the PEF Code, there are four circumstances which create a statutory modification:

- Divorce;
- Marriage;
- Birth or adoption of a child; and
- Murder of the testator.

- *Divorce or Pending Divorce*

Under § 2507(2) of the PEF Code, any provision in a testator's will in favor of or relating to the testator's spouse becomes ineffective for all purposes unless it appears from the will that the provision was intended to survive a divorce, if the testator: (i) is divorced from such spouse after making the will; or (ii) dies domiciled in Pennsylvania during the course of divorce proceedings, no decree of divorce has been entered and grounds have been established.

- *Marriage*

If the testator marries after making a will, § 2507(3) of the PEF Code provides that the surviving spouse will receive the share of the estate to which he or she would have been

entitled if the testator had died intestate, unless the will provides a greater share or it appears from the will that the will was made in contemplation of marriage to the surviving spouse.

- *Birth or Adoption*

Section 2507(4) of the PEF Code provides that if the testator fails to provide in his or her will for a child born or adopted after making the will, unless it appears from the will that the failure was intentional, that child is entitled to receive out of the probate estate not passing to a surviving spouse, the share as the child would have received if the testator had died unmarried and intestate owning only that portion of the estate not passing to a surviving spouse.

- *Slaying*

Any person who participates either as a principal or as an accessory before the fact in the willful and unlawful killing of any person is barred under §2507(5) of the PEF Code, from acquiring property or receiving any benefits as the result of the willful and unlawful killing.

- *Revocation*

A will or codicil in writing, or any part thereof, can only be revoked or altered: (i) by another will or codicil; (ii) by another writing declaring the same, executed and proved in the manner required of wills; or (iii) by being burnt, torn, canceled, obliterated, or destroyed, with the intent and for the purpose of revocation, by the testator or by another person in the testator's presence and by his or her express direction. If such act is done by any person other than the testator, the direction of the testator must be proved by the oaths or affirmations of two competent witnesses.

If, after the making of any will, the testator executes a later will which expressly or by necessary implication revokes the earlier will, the revocation of the later will shall not revive the earlier will, unless the revocation is in writing and declares the intention of the testator to revive the earlier will or, unless after such revocation, the earlier will is re-executed. Oral republication is ineffective to revive a will.

- *Spousal Election*

The surviving spouse's right to "take against the will" is governed by PEF Code §2202, et seq. Under that section, when a married person domiciled in Pennsylvania dies, his or her surviving spouse has a right to an elective share of one-third of the following property:

- Property passing from the decedent by will or intestacy.
- Income or use for the remaining life of the spouse of property conveyed by the decedent during the marriage to the extent that the decedent at the time of his or her death had the use of the property or an interest in or power to withdraw the income thereof.

- Property conveyed by the decedent during his or her lifetime to the extent that the decedent at the time of his or her death had a power to revoke the conveyance or to consume, invade or dispose of the principal for his or her own benefit.

- Property conveyed by the decedent during the marriage and another or others with right of survivorship to the extent of any interest in the property that the decedent had the power at the time of his or her death unilaterally to convey absolutely or in fee.

- Survivorship rights conveyed to a beneficiary of an annuity contract to the extent it was purchased by the decedent during the marriage and the decedent was receiving annuity payments therefrom at the time of his death.

- Property conveyed by the decedent during the marriage and within one year of his death to the extent that the aggregate amount so conveyed to each donee exceeds $ 3,000, valued at the time of conveyance.

With certain exceptions, an election by a spouse to take the elective share shall be deemed a disclaimer of any beneficial interest of the spouse in the following, to the extent that such interest would otherwise be payable to or enjoyed by the spouse after the decedent's death:

- Property subject to the spouse's election not awarded to the spouse as part of his or her elective share.

- Property appointed by the decedent's exercise of a general or special power of appointment, and property passing in default of appointment to the extent that the decedent had power to exclude his or her spouse from any interest therein.

- Property in any trust created by the decedent during his or her lifetime.

- Proceeds of insurance, including accidental death benefits, on the life of the decedent attributable to premiums paid by the decedent, his or her employer, partner or creditor.

- Any annuity contract purchased by the decedent, his or her employer, partner or creditor.

- Any pension, profit sharing, stock bonus, deferred compensation, disability, death benefit or other plan established by an employer for the benefit of its employees and their beneficiaries, exclusive of the Federal social security system and railroad retirement system, by reason of services performed or disabilities incurred by the decedent.

- Community property in the proportion that it represents the decedent's earnings or contributions.

- All intangible or tangible personal property and all real property owned by the decedent and his or her spouse by the entireties or jointly with right of survivorship, in the proportion that such property represents contributions by the decedent.

- All intangible or tangible personal property and all real property given to his or her spouse by the decedent during his lifetime which, or the proceeds of which, are still owned by his or her spouse at the time of the decedent's death.

In order to make the election the surviving spouse must file a signed writing with the clerk of the Orphans' Court division of the county where the decedent died domiciled, within six months of the decedent's death or before the expiration of six months after the date of probate, whichever is later. Failure to file an election in the manner and within the time limit set forth in this section shall be deemed a waiver of the right of election.

IX. Planning for Non-Probate Assets

Overview

As the draftsman of a last will and testament, your primary job is to ensure that probate assets are disposed in a manner consistent with the client's wishes, but as an estate planner you should also be concerned with the disposition of the non-probate assets as well. In reviewing the disposition of non-probate assets, the following should be reviewed:

Designation of Beneficiary Forms

The client should be questioned as to whether he or she has named a beneficiary of an investment account, or added a co-signatory to a bank account. In either case, the will does not control the disposition of these types of accounts. Instead, the account will pass to the named beneficiary or co-signatory. Finally, property that has been placed in a trust is not probate property. Such property will be disposed of by the terms of the trust and not the client's will.

The client should be asked to produce current designation of beneficiary forms in regard to all life insurance policies, IRAs, 401ks, and other retirement accounts. In reviewing these documents, pay attention not only to who has been named as the primary beneficiary (i.e., the person first in line to receive the disposition if the owner dies) but also the manner in which the contingent beneficiary is designated. Typically a client's will provides that in the event that their spouse does not survive them, their estate should be divided equally among their children. The will may provide further that if one of the children does not survive the client, the share of the deceased child is to pass in equal shares to the children of the deceased child. The will provision might be worded as follows:

"...to my wife, MOLLY, if she is then living, otherwise to my children, THOMAS, MARY, and WILLIAM, in equal shares, provided that if a child of mine does not survive me, the share that would have otherwise passed to such child shall pass to his or her then living descendants in equals shares, per stirpes."

On the other hand, the designation of beneficiary forms in regard to the life insurance of that same client, for example, may provide that if the spouse does not survive, then the life insurance proceeds are to pass to children individually named. The wording of the designation of beneficiary may provide the following:

"Primary Beneficiary: my wife, MOLLY.

Contingent Beneficiary: my children, THOMAS, MARY, and WILLIAM"

In this case if one of the children does not survive, only the surviving children will likely receive the proceeds of the insurance policy. The children of the deceased child would receive nothing. This is probably not what the client wants. At the very least, the dispositions of the estate and the non-probate assets, in our example the life insurance, are inconsistent, and should be reviewed with the client.

X. Other Issues

A. The Art of Disinheritance

In some cases, it is the testator's intent not to make a bequest or devise to a person who would normally expect to receive such a benefit under the Will. When this occurs, it may be desirable to include an explanation as to why no such gift is made. It has never been a law in Pennsylvania that it is necessary to leave some nominal sum or other gift to an heir in order to disinherit them, but such a gift will buttress the point that exclusion of the beneficiary of the gift has not been left out inadvertently.

PEF Code § 2101(b) provides as follows:

"Modification by decedent's will. – A decedent by will may expressly exclude or limit the right of an individual or class to succeed to property of the decedent by intestate succession. If the individual or a member of that class survives the decedent, the share of the decedent's intestate estate to which the individual or class would have succeeded passes as if that individual or each member of that class had disclaimed his intestate share."

Here are some alternative clauses:

"I have not provided for any specific gifts to my stepchildren, not because of any lack of love and affection, but because adequate provision can be made for them through my gift to their mother as provided hereinabove.

"I have not provided for son, William, not because of any lack of love and affection, but because of his own wishes and resources."

"Except as otherwise provided in this will, I have intentionally failed to provide for any other relatives or other persons, whether claiming to be heirs of mine or not. Insofar as I have failed to provide in this will for any of my issue now living or later born or adopted, such failure is intentional and not occasioned by accident or mistake."

B. In Terrorem Clauses

If a nominal beneficiary contests the Will, an in terrorem clause can be used to disinherit that beneficiary. However, an in terrorem clause is unenforceable "if probable cause exists for instituting proceedings." Remember, if the individual to whom the in terrorem clause is directed has nothing to lose under the terms of the will, then the clause will not serve as a

meaningful deterrent. Therefore, the testator might consider providing a significant benefit which will be forfeited if a will contest is brought without reasonable cause. The following are some alternative clauses to consider:

"If any devisee, legatee or beneficiary of any gift under this will directly or indirectly objects to the probate of this will or contests this will or any part thereof or exercises or attempts to exercise any right of election to take any part of my estate against the provisions of this will, then any such objecting or contesting devisee, legatee or beneficiary shall be treated for the purposes of this will as if he or she had predeceased me, and any devise, legacy or bequest of any kind intended for him or her shall be void and of no effect."

"Any gift, in trust or outright, to any beneficiary who endeavors to defeat the purposes of my will by raising objections to my executors probating the same or trying to set aside my will or contesting the same or appealing any decision sustaining the validity of the same shall be revoked."

C. Dealing with Pets

□ *Validity of Bequests*

In the past, bequests created to provide for the ongoing care of pets have been upheld as charitable trusts. PEF Code § 7738(a) now provides the following:

"(a) Creation and termination.—A trust may be created to provide for the care of an animal alive during the settlor's lifetime. The trust terminates upon the death of the animal or, if the trust was created to provide for the care of more than one animal alive during the settlor's lifetime, upon the death of the last surviving animal."

□ *Drafting Trust Provisions for the Care of a Pet*

In drafting a trust for the care of a pet many of the same issues that you must deal with in drafting a trust for a human beneficiary must be addressed. The following is a list of recommended provisions for inclusion in a trust for pets.

□ *Identifying the Pet*

The terms of the trust should identify the pet in a way that will, at the very least, permit third parties to identify the pet after the settlor's death, and preferably, prevent the caretaker from replacing the original pet with a new one to fraudulently perpetuate his or her right to distributions.

□ *Identifying Subsequent Pets Acquired by the Settlor*

Of course, including future pets in the terms of the trust saves the effort of having to formally amend the trust whenever a new pet enters the picture.

□ *Setting the Amount of Caretaking Funds*

The will should provide for the amount that will fund the trust. It should be noted however that under § 7738(c), the court can reduce the trust, if it believes that the amount "exceeds the amount required for its intended use."

- *Identifying Any Other Assets to be Used to Care for the Pet Animal*

If there is any additional property which is necessary for the care and maintenance of the pet it should also be identified and transferred to the trust.

- *Designating the Caretaker and the Trustees*

The caretaker is the person or persons designated to care for the pet. The trustee or trustees will administer and distribute the funds held by the trust, watch over the caretaker-beneficiary, and take care of any other matters pertaining to the trust (e.g., filing any fiduciary income tax returns). As with all trusts, the testator should designate a successor trustee, and also a successor caretaker, in case the first choice is unable or unwilling to serve. At the very least the trust document should provide a mechanism for appointing a successor trustee without the necessity of court intervention.

- *Defining the Powers of the Trustee over the Caretaker-Beneficiary*

One of the primary purposes of using a trust for the care of pets is to provide a check upon the caretaker if the caretaker is not providing adequate care for the pet. Therefore, the document should grant the trustee the power to remove and replace the caretaker, if warranted.

- *Defining the Duties of the Trustee and the Caretaker*

The trust should delineate the duties of both the trustee and the caretaker. Remember, it is the duty of the trustee to administer the trust funds and supervise the caretaker, who is responsible for the care and maintenance of the pet.

- *Providing for Distributions to the Caretaker*

There are a number of ways to structure distributions to the caretaker-beneficiary. One simple way to deal with the issue is to provide that a fixed amount be distributed by the trust at fixed intervals. A better alternative, however, may be to provide that distributions are to be made in the discretion of the trustee. If the trust is structured in this way, the caretaker must substantiate the need to the trustee before a distribution is made.

- *Defining the Standard of Care for the Pet*

At the very least, the terms for distributions to the caretaker-beneficiary should permit expenditures for food, shelter, medication, veterinary care, toys, boarding or pet-sitting, and costs for the disposition of the pet's remains. The settlor may also want to set more specific standards for such care – e.g., what type of food, how often the pet is to receive check-ups by the vet, how often the pet is to be walked. In drafting the document, try to make sure that the standards are not unreasonable, and are flexible enough to deal with unforeseen contingencies.

 Providing Guidance for Euthanizing the Pet

One potential issue of controversy is euthanasia, especially if the caretaker's interest in the trust ends with the death of the pet. That is, the document should clearly set forth the circumstances when euthanasia is appropriate – e.g., the veterinarian certifies that the pet has a terminal illness or will experience significant physical suffering for the rest of its life. In the alternative, the settlor should clearly indicate who has the discretion to make that decision – the trustee, the caretaker-beneficiary, or both.

 Providing Directions After the Death of the Pet

In most cases, the settlor has particular ideas about the disposition of the pet after its death – e.g., cremation of the animal and burial of the remains in a particular place. The terms of the trust should expressly include such provisions.

 Designating the Remainder Beneficiary

The trust should designate a remainder beneficiary or beneficiaries or, at the very least, provide a mechanism for the trustee to designate a remainder beneficiary (other than him or herself). In considering this decision, the settlor should realize that the remainder beneficiary's financial incentives will run counter to the pet living a long life with the benefit of the trust funds. For this reason, the settlor could consider defining the class of remainder beneficiaries as non-profit, tax-exempt organizations that have a stated purpose of caring for animals.

Presumably, such organizations would be bound by law (if not principle) to refrain from challenging the generosity of the amount of caretaking funds or the liberal use of such funds by the trustee or the caretaker-beneficiary in spoiling the pet. Moreover, if all else fails, there will be yet another eye with legal standing to look out for the pet's well-being.

 Terminating the Trust

The terms should provide that the trust is to terminate upon the earlier of:

- The death of the pet and disposition of the pet's remains;
- The exhaustion of the funds of the trust or a determination by the trustee that the amount of the funds renders continued administration uneconomical; or
- The expiration of the perpetuities savings period.

 Durable Power of Attorney

The client might also consider incorporating appropriate provisions in his or her durable power of attorney in order to deal with the care of pets in the event that the settlor becomes incapacitated during his or her lifetime. Here is some sample language:

"My agent shall be further authorized to exercise the powers granted hereunder to provide for the reasonable care and maintenance of my pets."

D. Disposition of Bodily Parts

- *Statutory Authority*

The rules and procedures governing the gift of a body or bodily parts for medical research and education or transplantation are contained in the Pennsylvania Anatomical Gift Act. The Act applies only to anatomical gifts that take effect at death. A ''donor'' is defined in the Act as an individual who makes a gift of all or part of his or her body. A person must be of sound mind and at least eighteen years of age to make an anatomical gift.

In order to expedite successful transplantation or donation after the donor's death, it is recommended that a donor carry a donor card, other document of gift, or identification card or driver's license that identifies the person as an organ donor. Moreover, the donor should inform all family members, as well as his or her physician, of an intended anatomical gift so that on the donor's death the appropriate medical authorities can be notified. Donations of bodily parts can be accomplished either through testamentary documents or by inter vivos gifts.

- *Testamentary Gifts*

Any person who has testamentary capacity (as defined in PEF Code § 2501) may make an anatomical gift by will. The gift becomes effective on the death of the testator without waiting for probate. To the extent that a testamentary gift has been acted on in good faith, the gift is still effective and valid, even if the will is not probated or is held to be invalid. A gift of the whole body must be made in writing at least fifteen days prior to the date of death, unless consent is obtained from the legal next of kin. The consent of the adult children of the deceased (who are not children of the surviving spouse) is also required for a gift of the whole body for anatomical study.

Although a testamentary anatomical gift becomes effective on the death of a testator whether or not the will is probated or declared valid for testamentary purposes, the gift will be frustrated if the will is not found in time to complete the necessary surgical procedures. Therefore, the testator should carry on his or her person a card or some document that refers to the testamentary anatomical gift. If the testator simply wishes to reflect his or her desire to make an anatomical gift in his or her will, he or she may first make the gift by a non-testamentary pledge or by a donor card and then include a provision in his or her will confirming the gift.

- *Gifts by Other Documents*

An anatomical gift may be made by a non-testamentary document. The document must be signed by the donor in the presence of two witnesses, who in turn must then sign the document in the donor's presence. If the donor is physically unable to sign the document but is mentally competent to signify his or her desire to do so, another individual at the donor’s direction may sign the document, in his or her presence, and in the presence of two witnesses who must then sign the document in

the donor's presence. The same requirements for gifting the entire body apply to a non-testamentary document as to a gift of the body made in a will.

The gift document may be in the form of an identification card issued by the Department of Transportation or the donor's driver's license, with a notation on the front that the holder intends to donate his or her organs or tissue. A notation on an individual's identification card or driver's license that the person intends to make an anatomical donation is sufficient to satisfy all requirements for consent to organ or tissue donation.

Delivery of the gift document during the donor's lifetime is not necessary to make the gift valid. However, delivery of an executed copy of the gift document is recommended to expedite donation to or transplantation procedures for a designated donee upon the donor's death. The gift document or an executed copy may be deposited in any hospital, bank or storage facility that accepts it for safekeeping or for facilitation of procedures after death.

Institutions that regularly accept anatomical gifts may use a pre-printed form. Sometimes the pre-printed documents include provisions or prescribe execution procedures that are peculiar to the institutions that prepare and use them. Even though the card or license may be an easier method of affecting an anatomical gift, a formally drafted and executed instrument has certain advantages over a card or a notation on a driver's license. For example, a donor card generally does not have enough space to designate a specific donee or to specify all the conditions or limitations that the donor wishes to impose on the gift. Similarly, the driver's license notation merely indicates that the person intends to make a donation.

There are four types of donor cards that may be used to make gifts of a body or body parts under the Pennsylvania Anatomical Gift Act:

- Gift document card issued by the Humanity Gifts Registry;
- The Uniform Donor Card issued by the Humanity Gifts Registry;
- The Uniform Donor Card issued by the Delaware Valley Transplant Program; and
- The Uniform Donor Card issued by the Transplant Organ Procurement Foundation.

An anatomical gift made by will may be inserted into a will if the testator wishes to make an anatomical gift in a testamentary instrument. This testamentary document can include a provision for a donor who wishes to donate his or her entire body or a provision that the donor wishes to donate only specified body parts.

- ANATOMICAL GIFT

"It is my desire at the time of my death that my body be released to the Humanity Gift Registry of the Commonwealth of Pennsylvania for anatomical studies at one of the medical schools with ultimate cremation with others and burial of the ashes in the burial plot of the Humanity Gifts Registry."

E. Special Funeral and Burial Instructions

Recommended Practice

Since the will may be in a locked safe deposit box or otherwise not immediately accessible, it is recommended that the testator's wishes regarding the burial be communicated to family members in advance of death. Moreover, any written instructions should be contained in a separate memorandum, which is easily accessible at the time of death. The instructions can direct, for example, where the services are to be held, where the body is to be interred, and out of what fund the funeral expenses will be paid.

DIRECTION FOR DISPOSITION OF REMAINS—BURIAL

"I direct my executor to engage the services of THE MILLER FUNERAL HOME, to perform a burial similar in all respects to that furnished for my deceased father, GERRY JONES. In my lifetime I purchased a burial lot in East Laurel Cemetery, Bala Cynwyd, Pennsylvania and I direct that my remains be interred therein."

DIRECTION FOR DISPOSITION OF REMAINS—CREMATION

"I direct that my body shall be cremated and the ashes scattered over the Grand Canyon, and that the expense thereof be reimbursed out of my estate as a funeral expense