Lifetime Trust Legislation

by Hon. C. Raymond Radigan

After my first report in 1991 as chairman of the EPTL Advisory Committee, in which we focused on the revision of the Right of Election and Descent and Distribution statutes, we recommended an examination and revision of the remaining articles of the Estate, Powers and Trusts Law (EPTL) and the Surrogate's Court Procedure Act (SCPA).

Upon the Senate and Assembly's adoption of the EPTL Advisory Committee's expanded scope, our committee evolved into the EPTL-SCPA Legislative Advisory Committee (committee). In my last column (The New York Law Journal, Jan. 21, 2004, at 3), I indicated I would review in this column what was set forth in our Fourth Report with respect to legislation governing the substantive and procedural aspects of inter vivos, or lifetime, trusts.

We felt it necessary to review and submit legislative amendment proposals for the laws regarding lifetime trusts as the use of these instruments had grown significantly. The suggestions of the practitioners of the Trusts and Estates Bar as well as our own preliminary investigations made clear that lifetime trusts were one of the most commonly utilized will substitutes in New York and, as such, a thorough review and amendment of the laws governing these instruments was necessary. The discussion below will examine the specific problems the committee was presented with, our analyses of such problems, our legislative proposals and the current state of law.

Background: Lifetime Trusts

The diligent trusts and estates practitioner is familiar with the mechanics of the probate system and the sometimes expensive and time-consuming nature, such as when attempting to probate a will where the identities or whereabouts of the decedent's distributees are unknown. For many years,

clients and practitioners alike sought to avoid or minimize some of the disadvantages related to the probate process. One way planners pursued this end, and continue to do so today, was through the use of lifetime trusts in which a person (commonly referred to as either creator, grantor, settlor or trustor) can create a trust indenture that provides for the management and disposition of such person's assets in a fashion that is operatively similar to that of a last will and testament. Very often individuals who seek the use of revocable living trusts are those individuals who wish to keep their dispositive plan and composition of assets private. These trusts are also often marketed to the elderly as a device to avoid the necessity of a court-appointed guardian in the event one is necessary to manage their assets during their lifetime. Practitioners also market the revocable lifetime trust to clients who own real property in another state, so as to avoid the need for ancillary probate for those foreign parcels properly transferred into the trust.

While such trusts could be established as irrevocable, ab initio, the revocable lifetime trust is the more popular choice. While we acknowledged the widespread use and, in certain instances, utility of revocable lifetime trusts in place of or in addition to wills, we noted that a concerning incongruity existed in that the law of wills was significantly more developed and effectively encompassing while trust-related legislation was scarce. One goal, thus, was to provide guidance through legislation to those, such as title companies and individuals that proceed to establish and administer trusts on a daily basis, who operate in the face of confusing or non-existent laws.

Committee's Recommendations

Given the fact that there existed no formal rules related to lifetime trust creation that paralleled those contained in the EPTL related to wills, but also bearing in mind that we did not desire to impose those same formalities on trusts, we sought to put into place requirements that would lessen confusion and discourage arbitrary revisions to the operative instrument, which would thereby greatly diminishing the utility of the instrument. As such, we

recommended that lifetime trusts be required to be contained in a signed writing and acknowledged in the same manner as that required for the recording of a deed to real property. In fact, at the time of our recommendations, EPTL § 3-3.7 already required that trusts created for the purpose of receiving property from a decedent's estate by way of pour-over provisions in wills be acknowledged. As to the required signatories, we recommended that the new legislation require that both the grantor and one acting trustee execute the trust agreement. As an alternative to the acknowledgment requirement, we recommended that the legislation accept as valid trusts executed in accordance with those formalities necessary for the execution of a will. In doing so, the committee sought to provide for instances where a settlor would be unable, whether by reason of serious illness or other incapacitating condition, to obtain a notary's acknowledgment as such would be impracticable.

In addition to the foregoing, we examined the funding aspect of lifetime trusts, which concerned both self-settled and third-party-trustee lifetime trusts. The committee noted the perplexity among title companies and transfer agents when the latter two attempted to ascertain which assets are subject to the provisions of the trust. In response thereto we suggested that, in the case of all lifetime trusts, something beyond a mere informal declaration be required in order to justify subjecting specified assets to the provisions of the trust instrument. We thought it appropriate to suggest that the trust actually be funded with the particular property in order to subject such property to the trust's provisions. Pursuant to our recommendation, whether or not an item would be deemed transferred should be made dependent upon the nature of the asset. That is to say, if the asset to be transferred were a stock, bond or bank account, such property would be deemed properly transferred when the owner transfers title, re-registers the item in the trustee's name or other action consistent therewith depending on the nature of the asset. In the case of a tangible item of property, the committee recommended that this legislation regarding funding require that an instrument of assignment accompanied by actual delivery. As to the issue

of whether after-acquired property is included among that property subject to a general dispositive provision such as, "all of my stock to X," the committee recommended that after-acquired assets not be subject to the trust unless, of course, such after-acquired property is registered or re-registered, as the case may be, in the name of the trust or trustee.

The committee also examined the common law merger doctrine whereby a trust is collapsed (that is, declared unenforceable) in the event the same person is the sole beneficiary and is the sole serving trustee. The doctrine's effect held true also where there was one person who is both sole trustee and sole beneficiary even though there were beneficiaries whose interests vested at the death of sole trustee and beneficiary. Prior to the committee's examination and recommendations, the New York State Bar Trusts and Estates Section introduced a bill and accompanied by a memorandum advocating for the elimination of the antiquated merger doctrine. The rationale supporting our recommendations closely paralleled that of the New York State Bar Trusts and Estates Section's several years prior. We recommended that where the same person acts as both sole beneficiary and trustee, the trust should remain intact provided that there is a next eventual estate. Such an amendment also necessitated an amendment to the statute that prohibited a trustee from making principal or income distributions in favor of himself or herself and, as such, we did so recommend that such distributions be made permissible.

Among the other of the committee's recommendations were those addressing the age limitation for the creator of a lifetime trust and defining what property may be properly disposed of by a lifetime trust. We recommended that legislation pass to require that settlors of lifetime trusts be at least 18 years of age. In addition, we thought it necessary and proper for purposes of inclusiveness to recommend that Article 7 of the EPTL be amended to include a provision identical to that of EPTL § 3-1.2, which provided that "[e]very estate in property may be devised or bequeathed."

It was brought to our attention that the revocatory effect of EPTL § 5-1.4 should be extended to revocable lifetime trusts so as to avoid undesired results in the event a decedent dies survived by an ex-spouse but without amended trust provisions providing for the disposition of such decedent's property in favor of such ex-spouse. That section provides that, in the event of a divorce or annulment, any disposition of property or nomination to fiduciary office in favor of the former spouse is revoked. We observed many instances wherein ex-spouses were receiving benefits upon the death of the other ex-spouse as a result of the latter's failure to change the dispositive provisions of a revocable lifetime trust which typically acts as the receptacle for a pourover will. Naturally, then, we recommended that the Legislature act to promote uniformly our public policy revoking testamentary dispositions to a former spouse and extend it to apply to revocable lifetime trusts.

As to proceedings dealing with lifetime trusts, we recommended that a section be added to the SCPA specifically authorizing such proceedings. The committee submitted that the legislature should enact a new SCPA § 1510 to specifically authorize proceedings concerning, among other things, construction, validity and accounting for revocable lifetime trusts. Just as recommended years before with regard to wills, we considered including among our recommendations a provision permitting the commencement of a proceeding to contest the validity of a revocable lifetime trust during the lifetime of the settlor thereof. The committee realized, however, that public policy would not advocate a proceeding wherein an instrument that is effectively testamentary in character may be challenged during its creator's lifetime, save, of course, instances where such creator was incapacitated and the court necessarily exercised its discretion. As such, we limited our recommended legislative enactment to the latter. Congruent with this proposed section, the committee also recommended that the Legislature include a section to provide for the class of persons entitled to commence such a proceeding. Generally, the recommended class included the creator, beneficiaries, fiduciaries and, if adversely affected by the trust's provisions,

distributees.

Although the foregoing procedural recommendations were accepted by neither the legislature nor the Trusts and Estates Section as they viewed such legislation as inviting an unnecessary and unwanted increase in court intervention, a revised version of the remainder of our foregoing recommendations was enacted by the legislature two years later in June 1997. Revocable lifetime trusts are still widely used today and, as such, I submit that a lack of procedural statutory guidance will serve to necessitate litigation in interpreting their use and administration. It is likely, then, that the committee will reexamine the proposed lifetime trust procedural statutes in the future.

Forthcoming

In my next article I will discuss the committee's studies, findings and recommendations, contained in our Fifth Report, regarding the changes to the definition of trust accounting income under EPTL Article 11.

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