Heckerling Institute 2007
Reports from the event, as posted to the ABA-PTL List Serve

Report #5

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten years, and again with the permission of the University of Miami School of Law Center for Continuing Legal Education, we will be posting daily Reports to this list containing highlights of the proceedings of the 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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This Report contains coverage of the Wednesday sessions on Malpractice Claims Against Estate Planning Counsel, What Yesterday's FLP Calls For, and Emerging Issues Under the Twin UPIAs

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Defense Strategies, Risk Management and Evolving Theories and Trends in Malpractice Claims Against Estate Planning Counsel Wednesday afternoon, Special Session 2-A, January 10, 2007 Presenters: Kevin Rosen, Mary Beth Robinson and Pamela Bresnahan

Reporter: Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia

This breakout session panel included Kevin S. Rosen, who presented the main lecture on this subject, Mary Beth Robinson, in house counsel with a large malpractice insurance company, and Pam Bresnahan, chair of Vorys Sater's Washington D.C.'s litigation group.

The first thing a lawyer should do is identify the client – for example, husband, wife or both? Mary Beth suggested representing jointly is the safest approach. Similarly, must clarify who attorney represents in estate administration. Whatever the arrangement, it should be documented in writing and attorney must follow terms of the relationship once established.

A large percentage of malpractice claims derive from poor intake system. Should do basic due diligence on client – do they have history of suing counsel or not paying fees; are there conflicts of interest to consider/resolve.

Not only are engagement letters necessary, also a good idea to inform client in writing when relationship ends or in areas where there may be uncertainty, such as who attorney does – and does not - represent in an estate administration.

In litigation, if prospective client alleges they believed attorney represented them, if belief is reasonable, enough to get past summary judgment. Who attorney thinks they represent rarely matters. Absent written communication defining relationship or lack thereof, courts will generally favor individual and allow case to go forward.

From the standing perspective, privity rules are being expanded, again, courts generally give the benefit of the doubt to the individual.

If client contact is different from the client, panel urged lawyer to be careful. For example, if one child acts as spokesperson for elderly parent, they may be representing their own interest, not their parent's interest.

Attorney serving as fiduciary – good idea? If client asks, clearly document it was their request, not the attorney's suggestion. Be prepared to accept the additional risk of serving. If attorney represents estate, duty generally to the estate, but if they are also executor, they own duties to the beneficiaries in their fiduciary capacity. Can you reconcile these differences? There may also be malpractice coverage issues. Mary Beth suggests having the management committee approve the firm's attorneys serving in a fiduciary capacity. Questions to ask include experience of person, type of assets that will be managed, history of conflict between beneficiaries.

In Georgia, the Supreme Court has issued a form letter required for a lawyer to be appointed fiduciary in the state that serves a good guide on the issue. Was it client's idea? Did attorney suggest other possible fiduciaries? Discuss conflicts and payment of fees.

However, panel suggested that attorney as fiduciary is an easy target because, in retrospect (i.e. in litigation), it is always easy to argue that there was a better fiduciary alternative.

Another area of high malpractice risk arises when attorney works through client's other advisors and rarely has direct access to client. Attorney must make sure their recommendations are getting to client – safest way is through written communications sent directly to client. Communicating through other advisors also raises privilege issues.

If attorney has financial relationship with other advisors – proceed with extreme caution. Attorney must exercise informed, independent judgment, existence of relationship with advisor can create picture that attorney not independent in their counsel.

The panel then discussed their thoughts on opinion letters and legal memos. Make sure you clearly identify the topic/issue – i.e. define the question. State what the facts are, whether you independently investigated or relied on client. Identify risks associated with transaction.

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What Yesterday's FLP Calls For: Rejoicing or Repairing Wednesday afternoon, Special Session, January 10, 2007
Presenters: Ronald Aucutt and Daniel Markstein

Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Their materials for this afternoon session consisted of a brief discussion of applicable provisions of Subchapter K that apply to distributions from partnerships and four "fact patterns," which really were the facts of four of the "dirty dozen" IRC Sec. 2036/FLP cases.

Aucutt took up the first fact pattern, which contained the facts of Strangi. He urged the attendees to assume that these facts occurred during lifetime of the client, who still has time to "fix" the problems or to do something about it. He and Markstein then began to take up different variables.

The first such variable was the amount of a client's property in an FLP as a percentage of the client's net worth, which is an FLP organization issue. The panel suggested either collapsing the FLP or getting assets out of the FLP in order to reduce the percentage of the client's estate. They called particular attention to personal use assets, which they advised should not be a part of the FLP asset base.

The second variable was the small or unnecessary FLP, which can occur either at the outset (an FLP organization issue) or due to post-formation issues such as changes in the law or net worth. In these cases, they recommended collapsing the FLP.

The third variable was the FLP formed on behalf of the incompetent client, particularly where the agent is "standing on all sides of the transaction." While Aucutt indicated that, in his opinion, he was unsure that this variable, standing alone, would be enough for a court to apply IRC Sec. 2036 to the FLP, it was still something that should be addressed by looking at checks and balances on the power holder.

The fourth variable, another organization issue, was sloppy formation facts, e.g., failing to file certificate of limited partnership, failing to timely fund, etc. The panel recommended doing an FLP audit and to fix the problems found. They also suggested the potential for adding partners, etc.

The fifth variable, an operational issue, was consistency with the FLP agreement. Examples of inconsistency included non pro rata distributions, commingling, etc. The panel strongly recommended fixing that problem by repaying the excess with interest. Markstein strongly advised all to exchange checks in this regard and not to do the fix through bookkeeping changes to the capital account.

The sixth variable, another operational issue, was facts that could give rise to the existence of an implied agreement. The panel recommended tightening of the checks and balances on the controlling/violating party and even transferring control to the younger generation.

At this point, the panel was interrupted by a stream of questions and comments, unfortunately too many of which were far afield from the subject.

Markstein went through the outline material on Subchapter K, which he described as a "cheat sheet."

The panel concluded with a very brief discussion of the applicability of IRC Sec. 2035 on FLP's, the materials for which were set forth in Aucutt's main session outline.

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Emerging Issues Under the Twin UPIAs Wednesday afternoon, Special Session 2-C. January 10, 2007 Presenters: Susan Porter and Alan Acker

Reporter: Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado

The purpose of this session was to review the Uniform Prudent Investor Act and the Uniform Principal and Income Act.

Porter started with a discussion of the duty to diversify in the Prudent Investor Act. She said that the only particular action mandated by this Act is the duty to diversify trust investments, but that the Act gives the trustee latitude in exercising that power.

She first discussed the history and the prudent man standard that required the trustee to review the prudence of each investment. The Bank of New York (Spitzer), 1974, held that this was true even though the performance of the trust fund as a whole was excellent.

She then reviewed several cases illustrating practical aspects of imposing a duty of diversification.

Some cases hold that the concentration of trust investments is not a breach of duty. Each of the cases cited included language that the trustee hold the stock position. Susan said that this language overrides the duty of loyalty.

Some cases also hold that lack of diversification, even with the above language, subjected the trustee to liability. One case held the trustee liable because the instrument did not have a specific power to hold bank stock.

Another case, Estate of Charles G. Dumont, had held that the corporate trustee was liable for holding Kodak stock, even though the instrument provided "neither my Executors nor my said trustee shall dispose of such stock for the purpose of diversification of investment and neither they [n]or it shall be held liable for any diminution in the value of such stock." When the case was decided in 2004, the court awarded substantial damages to the beneficiaries. This case has been discussed at the Institute in the past two years.

In 2006, the appellate Division reversed that holding, although the grounds for reversal were narrow and the decision was not an approval of the corporate trustee's actions regarding diversification. The Court of Appeals denied the objectants leave to appeal in September, 2006.

She then reviewed the changes in the Restatement (Third), Trusts - the Prudent Investor Rule. The Restatement and the Uniform Prudent Investor Act made five fundamental changes to the criteria for prudent investing:

- The standard of prudence applies to the trust as a whole;

- The overall investment strategy should incorporate risk and return objectives reasonably suited to the trust;

- The duty to diversify is in general a part of the investment strategy;

- No investment is imprudent, per se; and

- The delegation of investment authority is permitted subject to safeguards.

The law has been changed regarding assets in the trust at inception and the holding of inception assets is now not much protection. Also, Susan discussed language to negate the duty to diversify.

Acker pointed out an Article in the most recent issue of the ACTEC Journal that indicates there is a duty to diversify, even in an irrevocable insurance trust. He does not know if this is correct.

There was also discussion of a Nebraska Case and a law review article that special assets such as a family farm, should not be diversified.

The discussion then turned to the Uniform Income and Principal Act. The trustee owes a duty of impartiality to all beneficiaries and cannot act to favor one beneficiary over another unless directed or permitted to do so under the governing instrument.

With this caveat in mind, Acker discussed the power to adjust under UPIA §104. There are conditions that must be met to exercise the power to adjust:

1. The trust must be invested as a prudent investor;

2. The trust must describe the amount that may or must be distributed by referring to the trust's income; and

3. The trustee must determine that to administer the trust impartially, an adjustment is necessary.

There are limitations on adjustments. Most of these are tax driven - no adjustment may be made if the adjustment would cause the trust to fail its intended purpose, e.g. in a marital trust if the adjustment would cause the trust to fail to qualify for the marital deduction. He questioned whether a downward adjustment would ever be made in a marital trust.

An adjustment may not be made if all of the trustees are beneficiaries or if the adjustment would benefit the trustee. However, if one of the trustees is not in either of these classes, then that trustee may make the adjustment.

Another factor to consider is the intent of the settlor. However, he does not know how a trustee would determine the intent. He feels that this is a challenge. Ackers also noted that the adjustment in not a needs based test - the object is to be impartial.

Ackers briefly discussed the unitrust concept and indicated that he is not a supporter of a unitrust. He pointed out that the unitrust was considered by the drafters of the Act and rejected in favor of the power to adjust. He also discussed the various unitrust percentages (3 - 5%), the 643 regs and the problems determining which is appropriate.

Issues continue to emerge. One is the determination of income accrued before death. In the prior act, this would be prorated. In the current act, this is income when paid. The rule applies to payments such as rents, dividends and interest. Both agreed that the trustee does have the power to adjust.

Section 401 provides that the general rule is that cash from entities is income and property is principal. An exception is when the entity designates the payment as a liquidation payment, or if the payment is greater than 20% of the entity's gross assets, in which case the payment is principal.

Porter discussed section 105 of the Act. This was a separate section regarding notice that was added to the Principal and Income Act after it was initially approved. She stated that the 105 does not give the court the power to second guess the judgment of a fiduciary.

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More News From The Vendor Hall

All of the vendors seem plenty busy, especially the software vendors. Two vendors seemed to be not very busy were Lawgic and Inheritance plus West's Cowles and Fastax, but that may just be our timing.

Don Kelly is working hard on the interstate stuff where the different states have different taxes. He said there are now 20 states that have a different tax structure. Vince Lackner is also coming out with a program for this.

Someone at the Miami alumni lunch said that the number of attendees was 2,600+ but they do not have the final numbers on the walk-ins. Regardless, this is probably the second best audience that they have ever had.

Finally, the questionnaire in the materials has a question about the facilities. It asks whether to come back and how people feel. It also states that rates in South Florida have gone sky high and that the rooms cost about $350 now. It will be interesting to see what people think about this new venue.

We anticipate a full report on the vendors from Jason Havens in the next day or so.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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