

**PROTECTING THE SURVIVING SPOUSE . . .AND PROTECTING
YOURSELF AFTER BELT V. OPPENHEIMER**

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PROTECTING THE SURVIVING SPOUSE . . . and Protecting Yourself After *Belt v. Oppenheimer*

I. INTRODUCTION -- THE FOREST OR THE TREES?

When planning a married couple's estate, it is easy to focus on the tax issues involved and overlook important practical issues. While most clients would like to save taxes, if they really thought about it, most would probably say avoiding family conflicts and protecting the surviving spouse are higher priorities than tax savings. An estate planner's task is to elicit these wishes and draft documents which are the most likely to achieve their goals.

This paper discusses some of the ethical issues involved in planning a married couple's estate, examines some common estate planning techniques from the perspective of the surviving spouse and suggests alternative techniques which offer greater protection to the surviving spouse while still achieving some or all of the tax planning objectives. It also focuses on planning issues which either are unique to surviving spouses or are heightened or accentuated for surviving spouses in many cases.

Also, this paper discusses some of the likely effects of *Belt v. Oppenheimer*, __ S. W. 3d __, 49 Tex. Sup. J. 598, 2006 Tex. LEXIS 440 (Tex. 2006) on estate planning for married couples and suggests ways for the estate planner to protect himself or herself from liability.

II. MEET THE BRADYS

Here's the story of a lovely lady who was bringing up three very lovely girls. All of them had hair of gold like their mother, the youngest one in curls. It's the story of a man named Brady who was busy with three boys of his own. They were four men living all together, yet they were all alone until one day when the lady met this fellow, and they knew that it was much more than a hunch that this group must somehow form a family. That's the way they all became the Brady Bunch.

Mike Brady was widowed with three sons (all minors): Greg, Peter and Bobby. Mike married Carol, a divorcee with three daughters (also all minors): Marcia, Jan and Cindy. Mike and Carol had this 70ish idea that they could merge their families into one big, happy family, with all six children treated as the children of both parents.

Mike and Carol Brady came to see you in 1994 for estate planning. Things had been going quite well for the Bradys at the time, and it appeared likely that their combined marital wealth would probably exceed \$1.5 million. Fortunately, they came in to see you, a young estate planning attorney, shortly after you returned from that year's Advanced Estate Planning and Probate Law Course, and you were equipped with several good estate planning ideas.

After your skillful explanation of the tax issues involved, and based on your energetic recommendation that they should take advantage of the tax savings afforded by credit shelter planning, Mike and Carol ask you to prepare wills for each of them with the following features:

- A pecuniary outright marital gift with a residuary bypass trust.
- The surviving spouse is executor and trustee, with Alice (the housekeeper) as successor executor and trustee until Greg reaches age 25 and with Greg as successor executor and trustee after he attains age 25.
- The bypass trust authorizes the trustee not only to make income and principal distributions to the surviving spouse based on a health, education, maintenance and support standard, but also to make "spray" distributions to any descendant of either spouse based on the same HEMS standard.
- Upon the surviving spouse's death, the property remaining in the bypass trust is distributed to the six children, or to their descendants, per stirpes.

When the Bradys come in to sign their new wills, Carol is a little concerned about all the complex tax and trust language in the will. Mike gives Carol a dirty look, and you are afraid that there may be an ugly scene. Quickly you smooth over the waters by explaining to Mike and Carol that these bypass trusts are just like outright dispositions, but with the added advantage of tax savings.

Seven years later, in 2001, Carol Brady calls you. She reports that Mike Brady has passed away (there were some nasty rumors about AIDS, but she assures you he had colon cancer) and that she needs to know what to do. The first thing you do is dig out your copy of Mike's will. Sadly, it doesn't look anything like your current wills. Still, it doesn't look too bad, and in due course you probate the will, fund the bypass trust and send Mrs. Brady on her way.

Now Mrs. Brady has come to see you again. (Funny, she doesn't look so bright and cheery now.) It seems that she is having trouble with her children. Ever since Mike died, she has been estranged from Greg and Peter. Bobby is the only one of Mike's children who is still on speaking terms with Carol, and he's a twenty-something year old who is jobless and still living at home. Peter is now a lawyer, and he's been peppering Mrs. Brady with letters demanding information and accountings. Mrs. Brady says she has decided that the whole tax savings thing isn't worth it, and that she just wants to undo the bypass trust and make a new will leaving everything to her daughter Jan. (After much prodding, you learn that Marcia (who has moved to Mount Shasta and changed her name to "Glistening Stone Under Falling Waters") and Cindy (who apparently has developed into something of an actress and dancer performing under the stage name "Sin-dee") have fallen into disfavor.) Mrs. Brady is especially interested in terminating the trust, since she lost a good deal of "her" money by investing in a failed fern bar called "Flowers and Friends."

What advice do you give Mrs. Brady?

III. ETHICAL ISSUES IN PLANNING A MARRIED COUPLE'S ESTATE

Let's turn the clock back to when Mr. and Mrs. Brady first came to see you about estate planning. What were the Bradys' estate planning goals? What effort did you make to discern if Mr. Brady's goals and Mrs. Brady's goals were the same? What did you do to assure that the plan you devised met the Bradys' goals? What steps did you take to protect yourself from later problems with the plan? What liability do you face as a result of preparing the Bradys' estate plan?

A. Who is the Client?

First, let's start with what appears to be a simple question: Who was your client when you prepared the Bradys' estate plan? Mr. Brady? Mrs. Brady? Both Mr. and Mrs. Brady? The Brady family? Most of us would probably say that our clients were both Mr. and Mrs. Brady. Hopefully we used an engagement letter which addressed this issue, although many of us would find no engagement letters in our 1994 estate planning files.

Identifying the client or clients can be tricky, especially when 20-20 hindsight affects the parties' recollection of the facts. The attorney-client relationship is governed by the law of agency and arises only upon the mutual consent of the attorney and the client. See *Duvall County Ranch Co. v. Alamo Lumber Co.*, 663 S.W.2d 627, 633 (Tex. Civ. App. -- Amarillo 1983, writ refiled. n.r.e.); *Thompson v. Vinson & Elkins*, 859 S.W.2d 617, 621-23 (Tex. App. -- Houston [1st Dist.] 1993, writ denied). However, consent to establish an attorney-client relationship may be inferred from the conduct of the parties. *Duvall County Ranch Co. v. Alamo Lumber Co.*, 663 S.W.2d at 633. Assume for the moment that one of the Bradys' children attended the estate planning conference. That child's recollection of the meeting might convince a jury that an attorney-client relationship existed between the attorney and the child, despite everything the attorney may say to the contrary. In *Vinson & Elkins v. Moran*, 946 S.W.2d 381 (Tex. App. -- Houston [14th Dist.] 1997, writ dismissed by agreement), which was an estate administration case, the estate beneficiaries successfully established the existence of an attorney-client relationship with the executor's attorneys based on "beneficiary meetings" with attorneys and letters sent directly from the lawyer to the beneficiaries.

If an engagement letter is used, the identity of the client or clients should be expressly stated. For example, the following language could be used:

You, and you alone, are my clients. I owe no duty to your family members or to your potential estate beneficiaries.

This language may make things clear *vis a vis* the attorney and the persons he or she considers the clients, but it is only marginally helpful in defeating the claim of a family member who attempts to assert the existence of an attorney-client relationship. Should the attorney insist that a copy of the engagement letter be given to all potential estate beneficiaries? That seems extreme and is likely to be counter to the clients' best interests (since the clients may not wish to broadcast the fact that estate planning is occurring to all potential estate beneficiaries). However, if a potential estate beneficiary meets with the attorney and the clients at one or more of the estate planning conferences, then it is a good idea to provide a carbon copy of the letter to the potential beneficiary or, perhaps, a separate letter to the potential beneficiary confirming that no duty is owed.

In the vast majority of cases, both the husband and the wife will be the attorneys' clients. This multi-party representation, which practitioners in other areas of practice may shun, is the bread and butter of an estate planning practice. Thus, estate planning lawyers must live with the issues surrounding multi-party representation every day.

Rust E. Reid, in his paper entitled "Ethical Problems in Multi-Party Representation in Estate Planning, Probate, and Fiduciary Matters," 1996 Advanced Estate Planning and Probate Course, State Bar of Texas, points out that the most obvious (but not the only) problems presented in the representation of multiple parties have to do with communications -- (1) keeping client communications confidential and (2) keeping both clients reasonably informed.

Handling the problem with keeping client communications confidential is easy to solve, at least on the surface. An attorney cannot keep confidential information given by one client secret from the other client and still keep both clients reasonably informed. Therefore, both clients should agree that no communications between the attorney and either client will be kept confidential from the other. Consider having each married couple who comes in for estate planning sign the following agreement at or near the commencement of the initial estate planning conference:

Joint Representation Confirmation

It is commonplace for spouses to engage the same firm for estate planning. However, when a law firm represents both spouses with regard to common or related matters, certain conflicts of interest can arise within the ethical codes of the legal profession.

This is to confirm that our firm is to represent you jointly as husband and wife. As such:

- We will not maintain confidentiality between the two of you; the information we receive from either of you or from third parties will be shared with both of you.
- Each of you waive any objection to our representation of the other regarding potential conflicts of interest between you (such as involving marital property rights, spousal rights of election, property ownership and transfer matters, and trust as well as other asset arrangement matters).

Joint representation is appropriate in our experience. However, strict ethical

requirements dictate that we thoroughly disclose the ethical ramifications.

Please sign below to indicate your acknowledgment of these terms.

Dated: _____

Wife

Husband

In practice, the attorney is likely to run into problems where this tidy solution to the problem is challenged by messy facts. Assume, for instance, that the husband is the attorney's old college buddy and that this friendship is the reason the attorney-client relationship was established in the first place. If the husband shares information with the attorney which the husband assumes will be kept confidential (for example, news of an impending divorce), is the attorney going to keep that information confidential? Is the attorney in such a situation going to decline further representation of the friend?

The problems of keeping each client reasonably informed can be equally troubling. The client contact on an estate planning project is rarely equal. True, there are some cases in which a married couple comes to each planning session together. However, even in these cases there are likely to be telephone conferences with one spouse or the other. Also, the clients may participate unequally in planning conferences, and one client may understand the issues less than the other. Finally, one spouse may appear to dominate the other or make decisions for the other.

How does the estate planner assure that the estate planning document meets the wishes of both clients? One way is to rely more heavily on written communications (although this may in reality protect the attorney more than it protects the "quiet" spouse). Descriptions of strategic decisions involved in devising the estate plan can be included in engagement letters or transmittal letters. For example, the following language may be used to emphasize that meeting tax planning objectives meant sacrificing other objectives:

You have indicated that you want your estate plan to include provisions designed to save your family estate and/or gift taxes. By including these provisions, you should recognize that (a) your estate planning documents are likely to be more complex than they would have been if tax savings was not an objective and (b) restrictions may be placed on your beneficiaries (including the surviving spouse) that may make it more difficult to fully utilize and enjoy the property free from interference by and/or liability to others. This will confirm that we have discussed these issues at some length and that you have decided that the potential tax savings to be gained from this plan take priority over these potential detriments.

B. The Effects of *Barcelo*, *Belt* and Related Cases

But wait. Does the above language, which is intended to protect the attorney from claims that he failed to keep both clients reasonably informed about the plan, actually make it *more likely* that the attorney will be liable for damages after the death of one or both clients? Sadly, that may be the case in light of *Belt v. Oppenheimer*, __ S. W. 3d __, 49 Tex. Sup. J. 598, 2006 Tex. LEXIS 440 (Tex. 2006), decided by the Texas Supreme Court on May 5, 2006.

To understand the *Belt* case and how to address it in one's practice, one must start with every estate planner's favorite Texas Supreme Court case, *Barcelo v. Elliott*, 923 S. W. 2d 575 (Tex. 1996), and then look at the cases decided after *Barcelo*.

1. *Barcelo v. Elliott*

In *Barcelo*, the intended beneficiaries of an invalid trust brought a legal malpractice claim against the attorney who prepared the trust, alleging that the attorney's negligence caused the trust to be invalid. The Supreme Court held, in a split decision, that the attorney owed no professional duty to the intended trust beneficiaries because he did not represent them. Chief Justice Phillips writes in the majority opinion:

We believe the greater good is served by preserving a bright-line privity rule which denies a cause of action to all beneficiaries whom the attorney did not represent. This will ensure that attorneys may in all cases zealously represent their clients without the threat of suit from third parties compromising that representation. . . . We therefore hold that an attorney retained by a testator or settlor to draft a will or trust owes no professional duty of care to persons named as beneficiaries under the will or trust.

923 S. W. 2d at 578-9.

2. *Vinson & Elkins v. Moran*

While *Barcelo* may preserve privity as a defense to suits brought by estate beneficiaries, the beneficiaries may overcome this hurdle by proving that an attorney-client relationship existed between the attorney and themselves. As noted at page 2 above, in *Vinson & Elkins v. Moran*, 946 S. W. 2d 381 (Tex. App. -- Houston [14th Dist.] 1997, writ dismissed by agreement), estate beneficiaries were able to show the existence of an attorney-client relationship between the executor's attorney and themselves based on meetings with and correspondence to beneficiaries.

3. *McCamish, Martin, Brown & Loeffler v. F. E. Appling Interests*

McCamish, Martin, Brown & Loeffler v. F. E. Appling Interests, 991 S. W. 2d 787 (Tex. 1999), is not a probate or trust case, but it is important nonetheless in an analysis of claims by beneficiaries against attorneys for testators and fiduciaries. In *McCamish*, the Supreme Court expressly decides that a nonclient may bring a negligent misrepresentation cause of action against an attorney. The Supreme Court explains the tort of negligent misrepresentation this way:

[A] negligent misrepresentation claim is not equivalent to a legal malpractice claim. . . . Under the tort of negligent misrepresentation, liability is not based on the breach of duty a professional owes his or her clients or others in privity, but on an independent duty to the nonclient based on the professional's manifest awareness of the nonclient's reliance on the misrepresentation and the professional's intention that the nonclient so rely. . . . Therefore, an attorney can be subject to a negligent misrepresentation claim in a case in which she is not subject to a legal malpractice claim.

991 S. W. 2d at 792.

Given the “nonconfrontational” and “whole family” approach that estate planning attorneys are wont to employ, one can imagine the contexts in which negligent misrepresentation claims might arise in probate and trust law. The most obvious is in cases where the attorney represents the executor, trustee or other fiduciary. In that role, the attorney has occasion to make statements to (or, at least, in the hearing of) beneficiaries on which the beneficiaries may rely. A less obvious context, and the one which arose in *Estate of Arlitt v. Paterson*, 995 S.W.2d 713 (Tex. App.—San Antonio 1999, pet. denied), is the estate planning one. The attorney may be found to have implicitly or explicitly represented to the “family” that the estate plan was a good one, addressed tax concerns, etc. Since privity is not an essential element of this cause of action, no doubt beneficiaries will always include it in the laundry list of theories in seeking to recover from the testator's or fiduciary's lawyer.

4. Belt v. Oppenheimer

In *Belt v. Oppenheimer*, ___ S. W. 3d ___, 49 Tex. Sup. J. 598, 2006 Tex. LEXIS 440 (Tex. 2006) , decided May 5, 2006, Chief Justice Jefferson’s opinion says the Court is upholding the principles of *Barcelo v. Elliott*. In reality, however, the case turns its back on *Barcelo*’s guiding principle – that protecting the estate planning attorney’s undivided loyalty to the client is the overriding public policy goal.

In *Belt*, to avoid the *Barcelo* privity defense, the personal representatives of the deceased estate planning client’s estate sued, rather than the beneficiaries of the estate. The lower courts followed *Barcelo* and said that the suit was barred by lack of privity. The Supreme Court distinguished *Barcelo* by holding that the personal representatives of the estate planning client’s estate stood in his shoes, and that the malpractice claim survived the client’s death. Thus, the Supreme Court said that the personal representatives of the deceased estate planning client’s estate could sue the lawyer for failing to maximize estate tax savings. Chief Justice Jefferson writes:

Limiting estate-planning malpractice suits to those brought on behalf of a client’s estate by a personal representative will prevent the client from “losing control of the attorney-client relationship,” because the interests of the estate—which merely “stands in the shoes” of the client after death—are compatible with the client’s interests. Additionally, limiting the class of potential estate-planning malpractice claimants to the personal representatives of a client’s estate will ensure that estate-planning attorneys are not subject to “almost unlimited liability.”

Finally, we note that precluding both beneficiaries and personal representatives from bringing suit for estate-planning malpractice would essentially immunize estate-planning attorneys from liability for breaching their duty to their clients. As the *Barcelo* dissent noted, however, allowing estate-planning malpractice suits may help “provide accountability and thus an incentive for lawyers to use greater care in estate planning.” 923 S.W.2d at 580 (Cornyn, J., dissenting). Limiting estate-planning malpractice suits to those brought by either the client or the client’s personal representative strikes the appropriate balance between providing accountability for attorney negligence and protecting the sanctity of the attorney-client relationship.

___ S. W. 3d at ___.

The really frightening thing about the *Belt* case is that it allows second-guessing about estate planning strategies with no opportunity for input from the estate planning client. A planner could be sued for failing to use a family limited partnership (FLP), grantor retained annuity trust (GRAT), a qualified personal residence trust (QPRT), etc., even if the client clearly indicated that he or she wished to avoid such complicated and expensive options and even though the effectiveness of those strategies depended on facts not known at the time of planning (*e.g.*, the date of the client’s death, future market conditions, and changes in the law).¹

5. Drafting Engagement Letters After Belt

Consider again the following language from an estate planning engagement letter:

You, and you alone, are my clients. I owe no duty to your family members or to your potential estate beneficiaries.

Could this language be beefed up to eliminate *Belt*-like claims? What about the following language:

¹ These same factors may make it difficult to prove negligence and/or damages, but *Belt* probably allows the case to get to the jury.

You, and you alone, are my clients. I owe no duty to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate.

Since the basis of liability in *Belt* is that the personal representatives stand in the shoes of the estate planning client, perhaps the personal representative would be bound by this provision. How about this:

You, and you alone, are my clients. I owe no duty to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate, and you waive any such duty or liability to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate.

What about putting the reasoning from *Barcelo* in the letter, *then* saying that the duty to the estate and its personal representatives is waived? Try this:

You, and you alone, are my clients. In representing you in preparing your estate plan, I want it to be clear that I have your intentions and interests at heart and that I will not be distracted by worrying about what your family members, your potential beneficiaries, or the personal representatives of your estate may think could have been done or ought to have been done. To assure my undivided loyalty to you, this will confirm our understanding that I owe no duty to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate, that you waive any such duty or liability to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate, and that such persons are barred from suing me after your death.

I think an estate planning attorney can make a credible argument that this duty of undivided loyalty is important enough, and reasonable enough, that the attorney and the client could contractually agree to limit the personal representative's right to recover damages after the death of the client. Note, however:

- Will clients willingly agree to this waiver?
- Be careful to sign any such agreement with a client before fiduciary duties arise. It is much harder for an attorney to enforce an agreement with a client if the agreement was signed after the attorney assumed a role as the client's fiduciary. See Frank N. Ikard, Jr.'s paper entitled "Negotiating Fee Contracts and Recovering Fees in Fiduciary Litigation" presented to the State Bar of Texas Advanced Estate Planning and Probate Law Course in 2003.

How can the attorney reliably be able to show that the client considered and rejected other estate planning options? This may call for a two-fold approach:

- First, give each client a description of various estate planning techniques.
- Second, include language in the engagement letter or the transmittal letter for drafts that makes it clear that the client considered and rejected other alternatives.

On the first point, some attorneys writing on listservs since the result in *Belt* was announced have suggested giving each estate planning client a document describing various estate planning strategies and asking them to request information about any strategies that interest them. This may be where the industry goes, and perhaps this is the safest course. However, it seems much more likely that descriptions of other

techniques will occur in the initial client conference and will be more customized to the client's expressed needs and interests. If no written description is used, other means must be used to provide proof at a later trial that other strategies were considered. For example, good note-taking could support the attorney's testimony.

Consider this language in the engagement letter or transmittal letter for drafts:

This will confirm that, while we presented you with other estate planning options, you decided not to pursue other options.

This language is helpful, and it is hard to imagine a case in which it should not be used (in light of *Belt*). Its effectiveness, however, is dependent upon being able to prove that the attorney in fact presented other possible strategies, which were rejected by the client. Consider modifying this sentence in every engagement letter to specifically mention other strategies that were considered and, if appropriate, why they were rejected. For example, married clients with taxable estates occasionally reject basic bypass planning. This may be because they have no children and do not want the surviving spouse to owe fiduciary duties to remainder beneficiaries of a bypass trust. It is not hard to imagine a situation where a financial planner referred the couple to the attorney after running a computer model showing the virtues of bypass planning. If the clients reject bypass planning, the attorney should add something like this to the engagement letter:

Based on the information you provided to me, it is possible that the estate of the surviving spouse will be subject to estate tax. This tax could be eliminated or reduced by employing one or more tax planning strategies. We discussed some of these strategies, including the use of a credit shelter, or "bypass," trust, but you decided not to use any of these options because you preferred the simplicity and greater control of the plan described above.

It seems obvious that customizing this part of the engagement letter will make it much more likely that the attorney can convince a jury that other options were in fact considered and rejected.

C. Death Planning vs. Divorce Planning

An estate plan that is an estate and gift tax masterpiece can be a disaster for either or both spouses if their marriage ends in divorce rather than death. See Robert H. Kroney and Thomas P. Goranson, "Estate Planning/Divorce Interface," 18th Annual Advanced Estate Planning and Probate Course (1994), State Bar of Texas. Hopefully we all cover this issue in our estate planning conferences. Even if the issue is discussed, it should also be covered in written form. The following language may be included in the engagement letter:

In helping you with your estate plan, my objective will be planning for the death or disability of either or both of you; I will not be considering the effects of a possible divorce. Either or both of you may be adversely affected by your estate plan in the event your marriage ends in divorce. If you have any questions about how this plan may affect you in the event of a divorce, please consult with an attorney experienced in family law matters.

D. Client Communications

Has there ever been a paper addressing ethical issues which did *not* emphasize the importance of client communications? This paper is no different. As may be gleaned from the above discussion, a number of the ethical dilemmas which arise in representing a married couple in estate planning can be addressed, if not totally avoided, in an attorney's correspondence with the client.

1. Terminating the Relationship at the End of Planning

Consider including the following language in the letter transmitting original, executed documents to the clients:

7. My representation of you. Please read through the enclosed documents carefully over the next two weeks. If I have made any mistakes, or if there is something you do not like or understand, please call me, and I will clear things up. If I have not heard from you within two weeks, I will assume everything is the way you want it, and my representation of you in this matter will cease.

In this matter, you and you alone have been my client. I owe no duty to any of your family members or other possible beneficiaries. I have no continuing duty to update your plan or otherwise represent you. Of course, I look forward to working with you again in the future should you wish to hire me to help you with revising your estate plan or with another matter.

A speaker at the Advanced Estate Planning and Probate Course several years ago suggested this approach, including giving the client a couple of weeks to review the documents. In several years of using this language, the author has rarely had a client call back during the two-week period with a problem.

Terminating the attorney-client relationship is important so that there is no confusion about whether or not the attorney has a duty to keep the client informed of law changes and to update documents as necessary. While estate planning attorneys may hope, and expect, to represent clients again in the future, owing a continuing duty to clients can create a liability nightmare, especially considering how mobile our clients are. It is hard to fulfill continuing duties to clients who move with no forwarding address.

2. Too Much of a Good Thing?

It is easy to get carried away in client communications. Document assembly programs now make it possible to produce "understandable" abstracts of estate planning documents which can accompany the documents themselves. Living trust factories produce impressive binders and document descriptions which their customers obviously like. Estate planning attorneys understandably feel pressure to do likewise.

The goal in client communications should not be detailed descriptions of every aspect of the representation, but rather general discussions of the key points. A section-by-section description of each document presents the following potential problems:

- The client may wonder why the documents were so "un-understandable" that a description had to accompany them.
- The client may confuse the description with the document itself.
- Discrepancies between the description and the document are inevitable. If this was not the case, then the document could be as simple as the description, and the description could be eliminated.

Thus, rather than a section-by-section description of the bypass trust, consider more general descriptions in transmittal letters to get the necessary points across:

[Each of your estate plans will include a] Will, which provides (among other things) for the creation of a "Bypass Trust" as a means to preserve the estate and gift tax credit of the first spouse to die. This credit, which currently is equivalent to \$2,000,000 in assets, may allow the two of you to pass more of your combined marital wealth to your descendants or other estate beneficiary free of the estate tax. The Bypass Trust in each Will is funded by means of a formula. This formula contains language which is intended to maximize the amount of property passing into the Bypass Trust without causing there to be any tax due on the death of the first spouse to die. Funding of the Bypass Trust pursuant to this formula is mandatory on the death of the first spouse -- the surviving spouse has no power to choose whether or not to fund the Bypass Trust.

Another practice which may create some problems while solving others is the use of estate planning questionnaires. Before preparing and using a questionnaire, the attorney should ask himself or herself: What is the purpose of the questionnaire? It may be marketing tool. For example, in answering the questions, the potential client may convince himself or herself that estate planning is needed or give the attorney discussion points in the initial client conference which will help close the deal. Or it may be a tool for the attorney to use to better plan the estate. For example, it may include obscure questions which are easily missed in the initial client interview.

Whatever its purpose, the attorney should review the questionnaire for malpractice traps. Imagine, for example, that the attorney representing the Bradys used a questionnaire which asked the following [the Bradys' responses are shown]:

Please indicate which of the following are your estate planning goals and rate those goals where "1" is the most important goal and "10" is the least important goal:

- 3 Tax savings
- 4 Providing for my children
- 6 Providing for my grandchildren
- 1 Providing for the surviving spouse
- 5 Asset protection
- 2 Preventing family disputes

Now imagine that the plan the attorney came up with for the Bradys involved a bypass trust with the surviving spouse as the trustee and a spray power to the spouse and descendants based on a health, education, maintenance and support standard. If Mrs. Brady is sued by one of her grandchildren for breach of fiduciary duty, and if she digs out her copy of the questionnaire (or it is produced in discovery) and finds that providing for the surviving spouse and preventing family disputes were given the highest priorities, what position will the attorney be in?

IV. FROM WHAT ARE WE PROTECTING THE SURVIVING SPOUSE?

Before examining several traditional estate planning techniques and possible alternatives, consider what evils lurk out there from which the surviving spouse should be protected. This paper focuses on these: (1) fiduciary claims of descendants and remaindermen, (2) claims of creditors, (3) incompetent management of

assets, (4) problems arising as a result of disclaimers, (5) problems involving disability and incapacity and (6) invasion of privacy.

While all of these "evils" may be present in varying degrees in every planning context, the particular circumstances of each married couple or surviving spouse usually make one or two predominate.

A. Fiduciary Claims of Descendants and Remaindermen

Most common estate planning techniques, including basic credit shelter and GST planning, seek to reduce estate and gift taxes. Achieving this goal directly benefits descendants and remaindermen, usually at the expense of the donor/testator and his or her spouse. It is crucial for the estate planning attorney to discuss this phenomenon with his or her clients in client conferences and in correspondence with the client. Most married couples with taxable estates who make it into an estate planner's office are going to opt for tax planning over outright bequests to the surviving spouse, but they should be given the choice of a simple "I love you" will.

If the surviving spouse is the trustee of a trust, he or she has fiduciary duties, unless he or she has a general power of appointment. See *Westerfeld v. Huckaby*, 474 S.W.2d 189 (Tex. 1971), and *Wilkerson v. McClary*, 647 S.W.2d 79 (Tex. App. -- Beaumont 1983). Clients need to be told in the planning phase about these duties.

To an estate planner, what constitutes a fiduciary duty and what it takes to breach such a duty may seem to be limited only by the imagination of a fiduciary litigator. Frank N. Ikard, Jr., once listed these 15 fiduciary duties:

- The duty of prudence;
- The duty of loyalty;
- The duty of impartiality;
- The duty of good faith and fair play;
- The duty to take possession of trust property;
- The duty to segregate trust assets and not to commingle;
- The duty to carry out the directions of the settlor;
- The duty to keep beneficiaries informed and to account to them;
- The duty to preserve and protect the trust property;
- The duty not to delegate trust responsibilities;
- The duty to keep accurate books and records;
- The duty to make trust property productive;
- The duty to review trust investments periodically;
- The duty to uphold and defend the trust; and
- The duty to investigate the acts and omissions of predecessor fiduciaries.

See Frank N. Ikard, Jr., "Administration of Community Property After a Spouse's Death," 1996 Advanced Estate Planning and Probate Course, State Bar of Texas. Most commentators believe that recent Texas trust legislation (in particular, the Uniform Prudent Investor Act, effective January 1, 2004) makes it harder for an individual trustee to meet his or her fiduciary duties.

Outright bequests to the surviving spouse eliminate all potential fiduciary claims against the surviving spouse. This is obvious, but it bears repeating with emphasis: ***Outright bequests to the surviving spouse eliminate all potential fiduciary claims against the surviving spouse.***² If the family situation warrants, do not blindly go forth with bypass planning, etc., without giving the clients the choice of opting out.

Often the primary goal of estate planning is to put the surviving spouse as close as possible to where he or she would be if an outright disposition had been used without crossing the line that makes the assets in the Bypass Trust includible in his or her estate. While that may be the goal, estate planners should resist the temptation to understate the distinctions between outright dispositions and trust dispositions when counseling estate planning clients. Bypass trusts are not "just like owning it outright," and clients should not be told this.

While potential fiduciary claims may be more likely (and obvious) when clients have children from their prior marriages, nuclear families are by no means exempt from family fights over money. The likelihood of a fiduciary claim seems directly proportional to the amount of property held by the fiduciary. Even in the most congenial family situations, the possibility of future conflict should be considered and addressed.

The fiduciary liability aspects of specific planning techniques are discussed below.

B. Protection from Creditors

The surviving spouse may need protection from creditors. Creditors come in many shapes and sizes:

1. Tort Creditors of Deceased Spouse

The surviving spouse's separate property is not liable for any of the deceased spouse's liabilities, whether or not the liability is based on a tort. Tex. Fam. Code §3.202(a). All community property is subject to the tort creditors of the deceased spouse. Tex. Fam. Code §3.202(d). Creative use of provisions in the Probate Code favoring the surviving spouse may help protect some community property from the tort creditors of the deceased spouse. See, e.g., Tex. Prob. Code Ann. §177(b) and 270 -- 293. Also, investing marital assets prior to the death of the first spouse to die in investments which are exempt from creditors' claims may afford some protection.

2. Non-Tort Creditors of Deceased Spouse

The non-tort creditors of the deceased spouse cannot reach the separate property of the surviving spouse or the sole management community property of the surviving spouse. To avoid loss of creditor protection for the surviving spouse's sole management community property, such property either should not be listed on the probate inventory or the inventory should include a provision stating that the surviving spouse is not waiving his or her rights under Tex. Prob. Code Ann. §177(b). See Frank N. Ikard, Jr., "Administration of Community Property After a Spouse's Death," 1996 Advanced Estate Planning and Probate Course, State Bar of Texas.

² The surviving spouse receiving an outright bequest may be an attractive target for a guardianship proceeding to wrest control of assets, but that is not a fiduciary problem.

3. Creditors of Surviving Spouse

If the surviving spouse is likely to have creditor problems, spendthrift trust planning should be considered. For example, an obstetrician may want his or her spouse to utilize a bypass trust/QTIP trust arrangement so that those assets will be beyond the reach of future tort claimants. The probability of harm from fiduciary claims for the doctor may be much lower than the probability of a tort claim.

Recent changes in Texas law make it clear that a spendthrift trust is protected from a beneficiary's creditors even if the beneficiary also is the trustee, so long as the beneficiary's power to make distributions to himself or herself is limited by an ascertainable standard such as health, education, maintenance and support. Tex. Trust Code §112.035.

C. Incompetent Management of Assets

One spouse may wish to protect his or her spouse from incompetent³ management of assets. This incompetence could be in one of two forms: (1) the testator could worry about his or her spouse's ability to manage the assets (as trustee or otherwise) or (2) the testator could worry about the incompetence of a third-party trustee.

If one spouse has handled a couple's financial affairs to the exclusion of the other, he or she may legitimately worry about the ability of the out-of-practice spouse to handle things. This may be an awkward issue to discuss with the couple, but it is important to get the issue out in the open. (Of course, that is a lot easier to write in this paper than it is to do in practice.)

If a spouse may be unable to handle the property, consider bypass trust/QTIP trust planning. If the spouse is named as trustee, review carefully the successor trustee and incapacitated trustee provisions of the instrument.

If a corporate trustee or other third party trustee is used, consider giving the surviving spouse the power to remove the trustee and appoint a successor.

D. Disclaimer Issues

One of the handiest estate planning techniques for mid-sized estates is disclaimer trust planning. Rather than foregoing tax planning entirely (at one extreme) or encumbering the surviving spouse with a mandatory bypass trust even if the circumstances at the death of the first spouse do not justify such a trust (at the other extreme), disclaimer trust planning enables the surviving spouse to decide shortly after the death of his or her spouse whether or not to fund the bypass trust and with which assets. See “Funding the Bypass with a Formula Clause vs. a Disclaimer” at page 17 below. The current uncertainty over the tax-free amount for federal estate tax purposes makes disclaimer trust planning an attractive option for many clients.

There are other, non-fiduciary issues to consider when contemplating disclaimers, however. First, consider whether or not the surviving spouse will be able to handle the pressure of making the disclaimer decision within nine months of his or her spouse's death. A widow's or widower's grief may cloud her or his thinking during this period. Second, what effect will children and stepchildren have on making the disclaimer decision? Third, what creditor protection and Medicaid planning effects will the disclaimer decision have?

Of course, a surviving spouse may consider disclaiming property he or she would otherwise receive from his or her spouse even if the deceased spouse's will does not provide for a disclaimer trust benefitting the surviving spouse. In the proper case, it may make sense for a surviving spouse to disclaim property, allowing

³ The word “incompetent” is used in this context to refer to good old-fashioned dunderheadedness and not mental incapacity or disability.

it to pass outright or in trust for his or her children. What factors should be considered in making this decision?

E. Issues Involving Incapacity and Disability

Even if the planner has taken every step imaginable to place the surviving spouse in a position of control and to insulate him or her from liability to creditors or remaindermen, the survivor may be exposed to potential harm in the event of incapacity due to injury or illness. While a planner may not prevent the incapacity⁴ of his or her client, he or she may have a positive effect on the surviving spouse's life during the incapacity.

When both spouses are living, most of the incapacity planning decisions seem fairly obvious. In all but a handful of cases, spouses will want to name each other as their agents on powers of attorney, directives to physicians, etc. While holding the powers of an agent under one's spouse's power of attorney may enhance one's ability to wrongfully loot the marital estate, as a practical matter a spouse with this purpose in mind usually does not need the power of attorney to accomplish it. Thus, most couples give little or no thought to power of attorney planning while both spouses are living.

However, casual decisions about alternate agents made while both spouses are living can become critical after the death of the first spouse. Suddenly the surviving spouse does not have the comfortable and customary surrogate decisionmaker — his or her former spouse — to fall back on. The choices of which child to anoint, whether to use multiple agents, etc., all come rushing to the fore.

A related issue is Medicaid planning. When both elderly spouses are alive, each can often help take care of the other, avoiding the need for assisted living. After the death of the first spouse to die, the survivor is much more likely to need assisted living, especially in today's society, where family (and potential caregivers) are widely dispersed. Private pay nursing home costs are high, and many families end up facing the tough issues of asset preservation vs. nursing home Medicaid qualification vs. quality of life enhancement. There are things that can be done both before the death of the first spouse to die and after the death of the first spouse but before the nursing home need is acute to put the surviving spouse and his or her family in a better position if an extended stay in the nursing home is in the future.

F. Privacy Considerations

Many widows and widowers are quite concerned about keeping their affairs private and confidential. Of course, virtually no one wants more information available to the public about their affairs than is necessary. Elderly persons, however, often have a heightened sense of the importance of privacy for one or more of the following reasons:

- *A Pre-Internet Sense of Privacy.* Younger persons are used to the wholesale invasions of privacy prevalent in today's society. Which person under age fifty hasn't memorized his or her social security number, driver's license number, etc., from countless repetition at college registration desks, check-cashing establishments, etc.? Older persons do not share this same experience — at least not to the extent of their younger neighbors. Of course, Medicare has changed all that for many persons over age 65.
- *Fear of Elder Abuse.* Many well-to-do elderly persons do not live a well-to-do lifestyle. Through a lifetime of care and frugality, they may have built up significant wealth, even though their houses, cars,

⁴ If one takes a holistic approach to health, then freeing the surviving spouse from some of the burdens of creditor claims and fiduciary claims discussed above may have a positive effect on his or her health. Planners work in a dynamic family environment, and it is not much of a stretch to say that an experienced, capable planner can enhance the health of his or her client, if not the family as a whole.

etc., do not make this obvious. These persons may reasonably fear that they will be targeted by con men⁵ who will discover their wealth and seek to take advantage of them.

V. TRADITIONAL PLANNING TECHNIQUES AND SUGGESTED ALTERNATIVES

Assuming that creditor protection, asset management or other priorities do not supersede protecting the surviving spouse from claims by descendants and remaindermen, what are some techniques that offer greater protection to the surviving spouse?

A. Will-Based Planning vs. Revocable Trust Planning

A full examination of the pros and cons of will-based estate planning versus living trust-based planning is beyond the scope of this paper. Nevertheless, there are some circumstances either unique to or prevalent with surviving spouses that make living trust planning especially worth considering:

1. Will/Trust Contests

Although not strictly a fiduciary claim, the probability of a will contest or trust contest could be a serious threat to the surviving spouse.

If a contest is expected, consider using a funded revocable management trust as the primary planning vehicle. (An unfunded trust accomplishes little or nothing in this regard if the will must be probated to pour over assets into the trust.) See Frank N. Ikard, Jr., "Drafting to Avoid Will Contests and Fiduciary Litigation," 1996 Advanced Drafting: Estate Planning and Probate Course, State Bar of Texas.

Whether the primary vehicle is a will or trust, an *in terrorem* clause should be considered.

2. Fiduciary Claims

Texas statutes and courts have recognized the validity of revocable trusts where the settlor also is the trustee and primary beneficiary of the trust and, in fact, has a general power of appointment. See *Westerfeld v. Huckaby*, 474 S.W.2d 189 (Tex. 1971), and *Wilkerson v. McClary*, 647 S.W.2d 79 (Tex. App. -- Beaumont 1983). If the settlor/trustee can terminate the trust at any time and pay the trust property to herself, then she effectively has no fiduciary duties. In that sense, a fully revocable trust is like an ambulatory will for fiduciary liability purposes.

The fiduciary problems with revocable trust planning are likely to arise when the first spouse dies. In the typical case, the husband and wife establish a single management trust while both spouses are living that splits into two or more trusts when the first spouse dies. Unless the surviving spouse has a general power of appointment over both such trusts (which is unlikely), the surviving spouse will owe fiduciary duties to remaindermen.

Thus, if you accept the premise that a "standard" revocable management trust splits into at least two trusts when the first spouse dies and that the surviving spouse has no general power of appointment over at least one of the trusts, while a "standard" will for a married couple makes an outright bequest to the surviving spouse, then the "standard" revocable management trust gives the surviving spouse less protection from fiduciary claims than the protection given by a "standard" will.

Of course, if a credit-shelter trust is going to be used with the spouse as trustee and, then the spouse is going to have fiduciary duties whether the trust is set up by will or by inter vivos instrument.

⁵

Gender correctness check: Is it "con men" or "con persons?"

3. Family Allowance, Exempt Property

If the planner knew the surviving spouse would benefit from taking advantage of the exempt property and family allowance provisions of Texas law, he or she would probably opt for a will-based plan. This is because it is possible -- perhaps even likely -- that the family allowance and exempt property protections under the Probate Code are lost, to the extent that the probate estate is insufficient to provide them.

4. Use of a Living Trust for Disability Planning Purposes

Occasionally a revocable management trust may be the best choice for disability planning purposes.

a. Use of a Living Trust When Incapacity is Likely

In most cases, disability planning is a purely theoretical exercise — while it is possible that one’s client may become disabled prior to death, it is not a certain, or imminent, event. In such cases, powers of attorney present an attractive, inexpensive alternative to living trust planning.

When a client’s disability moves from the theoretical, distant realm into the not-too-distant reality, the additional cost of a living trust may be justified. There is little doubt that, in a long-term disability, a living trust is a better management device than a power of attorney. The trust instrument enables the settlor to be very specific about how his or her property is to be administered. Third parties are much more comfortable dealing with trustees and are much more likely to accept the authority of the trustee to act. The body of common law and statutory law regarding trusts is much better developed, so that there is much more likely to be an answer to issues which may arise. Trusts do not fail for want of a trustee, so the trust will continue even if all named trustees and successor trustees fail to act, while a power of attorney goes away if all named agents and successor agents fail to act.

b. Consider Prohibiting Revocation by the Settlor’s Guardian

For the same reasons that a declaration of guardian should be used to back up a power of attorney (see “Durable Powers of Attorney for Property and Declarations of Guardian” at page 27 below), in most cases the living trust instrument should prohibit the settlor’s guardian of the estate from revoking the living trust. Without this protection, a disgruntled nontrustee could seek a guardianship as a way to revoke the living trust — hardly what the settlor intended when he or she set up the trust as a disability planning device.

c. Corporate Trustee (or Successor Trustee) versus Family Member Trustee

If the purpose of the living trust is dealing with an imminent disability rather than wealth transfer planning, consider using a corporate trustee either as the initial trustee of the trust or as the successor trustee of the trust when and if the settlor ceases to act as trustee during his or her lifetime. Traditional corporate trustees (banks and independent trust companies, rather than brokerage-firm offshoots) are experienced at dealing with incapacitated beneficiaries and should offer competent, impartial service. Family members can be given the authority to make personal and health care decisions, but they may not do the best job of taking care of dad’s property while dad is in the nursing home.

5. Privacy Issues

One of the big selling points at living trust seminars (after “avoiding probate”) is the enhanced privacy available with living trust planning. It is true. Assets in a fully funded living trust need not be placed on the probate inventory, which of course is filed in the probate records and is available for public inspection.

A revocable management trust can provide greater privacy for a surviving spouse, but only if and to the extent it is funded prior to death. There may be reasons that assets are kept out of the trust until they are poured into the trust by will after death. For example, many lawyers recommend leaving the homestead out of the trust to be assured of the preservation of the creditor protection given to homestead property.

Of course, privacy is only one of the considerations that goes into determining whether a client will be better served with a living trust-based estate plan or a will-based plan.

B. Funding the Bypass with a Formula Clause vs. a Disclaimer

Most credit shelter trusts are funded by means of a formula clause. The most common type of funding clause in Texas probably is the pecuniary marital deduction/residuary bypass clause (or, in cases where the marital deduction gift exceeds the bypass gift, a pecuniary bypass/residuary marital clause).

Not all credit shelter trusts are funded by means of a formula, however. Treas. Reg. §25.2518-2(e)(2) permits the surviving spouse to disclaim property into a credit shelter trust and serve as trustee of the trust, so long as the spouse possesses no power to direct the beneficial enjoyment of the disclaimed property that is not limited by an ascertainable standard.

When comparing formula funding and disclaimer funding of the bypass trust, the formula funding approach has three distinct advantages:

- The bypass trust is sure to be funded (in other words, all that good tax planning is not dependent upon the decision of a grieving widow or widower to disclaim);
- The surviving spouse can be given a special power of appointment over the trust; and
- A formula clause coupled with appropriate special needs trust language may make it possible for the surviving spouse to qualify for Medicaid payment of nursing home costs while still protecting the bypass trust, while disclaimer funding exposes the bypass trust to the Medicaid transfer penalty.

However, from the surviving spouse's perspective, the first "advantage" of the formula clause method may be a huge disadvantage -- the surviving spouse cannot opt out of the tax-planned trust when the first spouse dies.

As is discussed below, a special power of appointment can be a significant disincentive for a potential remainderman to complain about the surviving spouse's actions as trustee. Since a disclaimer-funded bypass trust cannot include a special power of appointment, and since the decision to disclaim must be made within nine months of the date of death, the planner and his or her clients who are worried about a potential problem with descendants are forced to make a key choice in the planning process (while both spouses are living):

- Should the disclaimer method be used so that the surviving spouse can opt out of the bypass trust entirely if problems appear likely to arise within nine months of death; or
- Should the formula method, coupled with a special power, be used to guard against problems that may not surface until after the nine-month disclaimer deadline is long gone?

While certainly there are exceptions, in general the younger a couple is (except, perhaps for *very* young and immature couples), the more likely that disclaimer planning makes sense.

C. Other Disclaimer Issues

1. Creditor Protection

If the surviving spouse faces current creditor problems or is likely to face creditor problems in the future, a disclaimer can be used to protect the disclaimed assets from the creditors of the person making the disclaimer. Tex. Prob. Code Ann. § 37A provides in part that a disclaimer meeting the provisions of the statute “shall be effective as of the death of decedent and shall relate back for all purposes to the death of decedent *and is not subject to the claims of any creditor of the disclaimant.*” [Emphasis added.] The statute was strengthened in this respect in 1993 after the case of *Dyer v. Eckols*, 808 S. W. 2d 531 (Tex. App. — Houston [14th Dist.] 1991, writ dismissed).

Obviously, if the will of the first spouse to die is drafted with a disclaimer in mind, it can provide for creation of a disclaimer trust benefitting the surviving spouse as discussed above. If the disclaimer trust contains a spendthrift provision (which, of course, it should in virtually all cases), then the surviving spouse's creditor protection can continue during his or her lifetime while he or she benefits from the disclaimer trust.

However, the potential for using a disclaimer should not be overlooked even if the will fails to provide for a disclaimer trust. In most such cases, the will will provide for the disclaimed property to pass to the children or other descendants of the deceased spouse, and this disposition may be preferable to having it used to satisfy the debts of the surviving spouse.

2. Medicaid Issues

Disclaimers may work for creditor protection purposes, but they do not work for Medicaid planning purposes. Under federal law, disclaimers are treated as transfers by the disclaimant for purposes of determining if the transfer penalty applies. 42 U. S. C. §1396p(c)(1)(A) and 42 U. S. C. §1396p(e)(1). If the surviving spouse disclaims property into a disclaimer trust, the five-year transfer penalty applicable to trusts applies. If the spouse disclaims property and, as a result of the disclaimer, the property passes to another person (such as the decedent's descendant), the three-year transfer penalty applies.

Obviously, therefore, one must consider the likelihood that the surviving spouse will need to qualify for nursing home Medicaid prior to (a) using disclaimer trust planning for a wife and husband, (b) counseling a surviving spouse about making a disclaimer into a disclaimer trust, and (c) counseling a surviving spouse about making any other type of disclaimer. If bypass planning is called for, a formula approach or asset-specific approach should be used, and backup special needs trust language should be included in the bypass trust in appropriate cases.⁶

3. The Importance of Good Advice

The availability of disclaimers — and the relatively short period of time for making disclaimers — highlights the need for the surviving spouse to get well-informed, level-headed advice promptly after the death of his or her spouse. Well-intentioned but misinformed advice can waste this opportunity and, in many cases, work to the surviving spouse's detriment.

Let us return to Disclaimers 101 for a moment: By its very nature, a disclaimer does not give the disclaimant the power to direct property as the disclaimant wishes. Rather, all the disclaimant may do is say whether or not he or she wants the property. If the disclaimant does not want the property and makes a disclaimer, the ultimate recipient of the disclaimed property is determined by the will or trust of the decedent or by the laws of descent and distribution. The default rule is set forth in Tex. Prob. Code Ann. § 37A:

Unless the decedent's will provides otherwise, the property subject to the disclaimer shall pass as if the person disclaiming . . . had predeceased the decedent and a future interest that would otherwise take effect in possession or enjoyment after the termination of the estate or interest that is disclaimed takes effect as if the disclaiming beneficiary had predeceased the decedent.

[Emphasis added.]

Funding a bypass trust with a disclaimer works only if the decedent's will specifically provides that property disclaimed by the surviving spouse passes into the bypass trust. If the will is silent as to the effect

⁶ It may seem farfetched to discuss Medicaid planning and bypass trust planning in the same breath, but there are many land-rich, cash-poor Texans for whom this is a very real issue. If the potential Medicaid recipient lives on a farm or ranch worth greater than \$2,000,000, he or she could have a taxable estate while at the same time be able to have the farm or ranch treated as an unavailable resource for Medicaid purposes, since one's home can be an unavailable resource and since Texas does not yet have an estate recovery plan to place or enforce a Medicaid lien on one's home.

of a disclaimer, then the will must be read as if the disclaiming person predeceased the decedent to determine who is entitled to receive disclaimed property.

Attorneys advising clients about disclaimers need to know these fundamental principles (in addition to other principles perhaps equally as fundamental and critical to the disclaimer decision). Alas, some attorneys do not understand these concepts but nevertheless undertake to advise widows and widowers about disclaimers. Also, nonlawyers — family members, accountants, financial advisers, friends at the health club, etc. — often are quick to give advice. Disclaimers are irrevocable. It is sad when the disclaimant first discovers the true recipient of disclaimed property from the probate judge rather than from his or her own lawyer.

It may seem obvious, but level-headed advice is needed as well as well-informed advice. Estate planning is not a game, and this is particularly true when disclaimer decisions are being made. Disclaimer decisions are irrevocable and should not be made lightly or in reliance on (unenforceable) promises of support by children and other family members. Planners must be aware of creative techniques such as disclaimers, but they should not lose sight of reality when employing them.

4. Minimizing the Pressures Surrounding a Disclaimer Decision

The disclaimer decision must be made within nine months of death. This is a time when grief, stress and the “help” and demands of family members can overwhelm the surviving spouse. While the attorney representing the surviving spouse should not be patronizing, he or she should never assume that the surviving spouse is operating at peak efficiency. If it appears to the attorney that a disclaimer should be considered, he or she should discuss it with the surviving spouse repeatedly over several visits. If it appears that the surviving spouse forgets the disclaimer discussion from one visit to the next, or if the surviving spouse does not appear to understand the disclaimer concept after several explanations, the attorney should seriously consider dropping the disclaimer strategy altogether. In extreme cases, the attorney should consider whether a guardianship is necessary or appropriate to fully protect the surviving spouse’s interests. Rule 1.02(g) of the Texas Disciplinary Rules of Professional Conduct requires a lawyer to:

[T]ake reasonable action to secure the appointment of a guardian or other legal representative for, or seek other protective orders with respect to, a client whenever the lawyer reasonably believes that the client lacks legal competence and that such action should be taken to protect the client.

In most cases, of course, the failure of the surviving spouse to remember or understand the disclaimer strategy when it is explained to him or her is not an indication of a level of incapacity requiring a guardianship. Rather, it may just be a sign for the attorney to let the decedent’s estate flow where it flows without a disclaimer. From a legal and moral perspective, the attorney is less likely to be criticized for failing to get his or her client to make a disclaimer than for being so overbearing that the client makes a disclaimer without fully understanding its effects.

The greatest pressures on the surviving spouse about the disclaimer decision are likely to come not from the lawyer but from children and other family members. Most disclaimers have a positive effect on children, descendants and other remaindermen while having a neutral or negative effect on the disclaimant. For example, if the surviving spouse disclaims property which instead passes directly to the decedent’s children, the decedent’s children directly benefit from the decision to make the disclaimer. Also, if the surviving spouse disclaims property into a disclaimer trust for estate tax purposes, the children or other remaindermen stand to benefit from the estate tax savings. Even well-intentioned children may get carried away with the disclaimer idea and put undue pressure on their mother or father to disclaim.

To guard against undue pressure on the surviving spouse from children and other remaindermen, be careful to have private meetings with the surviving spouse where the disclaimer decision is discussed. Since many elderly clients rely heavily on one or more of their children for advice, it probably is unrealistic never to discuss the disclaimer in the presence of these family members, but be sure that some of the discussions exclude these “helpers.” Also, remember the lesson of *Vinson & Elkins v. Moran*, 946 S. W. 2d 381, (Tex. App. -- Houston [14th Dist.] 1997, writ dismissed by agreement) — make it clear in writing to these “helpers”

that you do not represent them. The disclaimer decision is one issue where the Texas Supreme Court's decision in *Barcelo v. Elliott*, 923 S. W. 2d 575 (Tex. 1996), makes sense — the attorney representing the surviving spouse must have that client's interests in mind and must owe no duty to other estate beneficiaries or the family as a whole.

D. Spouse as Trustee vs. Neutral Trustee

One way to insulate the surviving spouse from fiduciary liability is to avoid making him or her a fiduciary. This may be particularly appropriate in second marriages.

If a trustee other than the spouse is to be used, and if the goal is protecting the surviving spouse, then a corporate trustee (with the spouse holding the power to remove the trustee and replace it with another corporate trustee) usually offers greater protection than another family member. Even if the family member is "loyal" to the surviving spouse (such as the surviving spouse's daughter in a second marriage situation), the loyal trustee's allegiance to the surviving spouse likely can be used against him or her by "disloyal" family members to gain an advantage in fiduciary litigation. A corporate trustee is more immune from such attack and hopefully can be kept in line by the surviving spouse's power to remove it and replace it.

In this changing world of financial services, it is important to remember that not all corporate trustees are equal. In the old days, say six years ago, there were two basic choices — banks with trust powers and independent trust companies. Stereotypically, banks were conservative as to investments but generally safe choices regarding beneficiary services, while trust companies were more aggressive on investments but perhaps spotty on beneficiary services. (Obviously, there were exceptions.)

Today every Tom, Dick and Harry (or, more appropriately, every Charles (Schwab), Merrill (Lynch) and Smith (Barney)) has a trust operation and most banks and "traditional" trust departments have been through multiple mergers. With the stock market soaring higher and higher, there is a tendency for clients to look to maximum investment return when considering a corporate trustee. Sure, investment performance is an important consideration, but attorneys should be careful to protect their clients from getting swept into a bad trust arrangement for the sake of satisfying someone else's (often a child or other remaindermen) idea of good trust services. It is no big stretch to say that a warm, cooperative, *known* voice on the other end of the telephone line is probably more important to an elderly surviving spouse than an extra three percent of total return.

E. HEMS Income Distribution Standard vs. All Income to Spouse

Does this sound familiar? In a bypass trust with the surviving spouse as trustee, the trustee is given the power to make principal and income distributions to the spouse based on a health, education, maintenance and support standard, taking into consideration other resources available to the knowledge of the trustee. Because of the compressed income tax rates applicable to trusts, the trustee's attorney and/or accountant recommend that all income be distributed to the surviving spouse so that the effective income tax rate is reduced. For ten straight years, all of the bypass trust income is distributed to the spouse, even though his or her own assets are sufficient to provide for his or her needs. This is a fairly common fact pattern, isn't it?

In the eleventh year, the remaindermen sue the surviving spouse as trustee, claiming various breaches of fiduciary duty. Plaintiff's Exhibit No. 1 is the trust accounting showing that, for ten straight years, all trust income was distributed to the surviving spouse.

A trustee has a duty to administer the trust in accordance with the trust instrument. *See* Restatement (Second) of Trusts §169; Bogert and Bogert, *The Law of Trusts and Trustees* § 583 (2nd ed. 1985); Texas Trust Code §113.082. When there are two or more beneficiaries of a trust, the trustee has a duty to deal impartially with them. *See* The Restatement (Second) of Trusts, §183. A trustee may be held liable not only for abuse of discretion, but also for the failure to exercise discretion. *See State v. Rubion*, 158 Tex. 43, 308 S. W. 2d 4 (1957).

In the above hypothetical, it should be fairly easy for the plaintiffs to show that the spouse/trustee either abused his or her discretion or failed to exercise his or her discretion by paying all of the income to the spouse/beneficiary each year. It will be hard for the spouse/trustee to argue that he or she applied the standard stated in the trust instrument and decided each year that the amount of trust income precisely equaled the spouse/beneficiary's health, education, maintenance and support needs, taking into account other available resources to the knowledge of the spouse/trustee/beneficiary.

It is also likely that the plaintiff will be able to show that the spouse/trustee breached his or her duty of impartiality by distributing all income to himself or herself -- especially if the spouse also held a power as trustee to spray distributions to descendants on a health, education, maintenance and support standard.

It seems logical to favor an HEMS income distribution standard over a mandatory income distribution standard in the bypass trust. Usually the goal is to permit the bypass trust to grow by accumulating as much income as possible. While a mandatory income distribution provision is required in QTIP trusts, bypass trusts have the flexibility to permit accumulation of income.

On the other hand, if it seems fairly likely that all of the income will be distributed to the surviving spouse (as might be the case where a smaller estate includes bypass planning), why put the spouse/trustee in a position to possibly abuse his or her discretion or fail to exercise his or her discretion by imposing a health, education, maintenance and support standard on income distributions? If the trust described in the above hypothetical had an "all income to spouse" distribution provision, there would have been no breach of the duty of impartiality, no abuse of discretion and no failure to exercise discretion.

F. Traditional Trust vs. Unitrust

In second marriage situations where it is desirable to have the surviving spouse or child from the first marriage as trustee, consider using a unitrust. Much of the controversy over the trustee's decisions go away if a fixed percentage of the value of the trust is paid to the surviving spouse. Regardless of the personal interests of the trustee, both the income beneficiary (surviving spouse) and remainder beneficiaries (child of first marriage) benefit if the trust grows.

A pure unitrust does not give the surviving spouse access to the principal of the trust if needed for health, maintenance or support. A unitrust could be coupled with a provision permitting the trustee to invade the principal for the surviving spouse's health, maintenance or support, but that may defeat the purpose of the unitrust since disputes may arise over the extent of those needs.

G. Spray Power vs. Special Lifetime Power vs. None of the Above

It is tempting to push for maximum flexibility when planning an estate. After all, the clients pay the estate planner to anticipate a wide variety of possible events and deal effectively with those events.

A traditional way to build in flexibility in bypass trust planning is to give the spouse/trustee the power not only to make income and/or principal distributions to himself or herself (limited by an ascertainable standard), but also to make HEMS distributions to the testator's descendants. In this way the surviving spouse can "spray" trust income or corpus to descendants without using up any of the surviving spouse's annual exclusion or unified credit.

Unfortunately, this spray power raises potential fiduciary problems for the spouse/trustee. Since the power is held by the spouse/trustee in his or her capacity as trustee, it carries with it a plethora of fiduciary duties -- the duty of impartiality and the duty of loyalty for starters.

1. Use of a Special Inter Vivos Power

Compare the spray power with a special inter vivos power of appointment. By giving the spouse the power to appoint trust property among descendants in his or her individual capacity as a beneficiary rather than as trustee, the spouse still has the ability to cause trust distributions to the descendants if she determines

that this is desirable. Moreover, the spouse can exercise or not exercise the special power without fear of fiduciary liability.

When coupled with a special testamentary power of appointment (discussed below), a special inter vivos power of appointment can achieve a high level of flexibility while still protecting the surviving spouse.

Of course, using a special inter vivos power is not a desirable alternative if it carries with it significant adverse tax consequences.

a. Avoiding Support Obligations

The trust instrument should include a provision prohibiting the spouse from having the power to satisfy his or her support obligations from the trust. Having the power to use trust property to satisfy a spouse's support obligations (such as a parent's duty under state law to support his or her minor children) gives the spouse a general power of appointment to the extent the trust property could have satisfied the spouse's legal obligations. I.R.C. §2041; Treas. Reg. §20.2041-1(c); Rev. Rul. 79-154, 1979-1 C.B. 301. The power to satisfy support obligations creates a general power of appointment regardless of whether the power is held by the spouse in his or her fiduciary capacity as trustee (as would be the case if the spouse had the power as trustee to make spray distributions to her minor children in satisfaction of support obligations) or by the spouse in his or her capacity as beneficiary (as would be the case if the spouse had a special inter vivos power to appoint trust property to her minor children in satisfaction of support obligations). Thus, regardless of which approach is used (spray power or special inter vivos power), the trust instrument should negate the power to make distributions to satisfy support obligations.

b. Income Tax Effects

Arguably, at least, distributions of trust income to descendants by a spouse/trustee using a spray power cause the trust income to be taxed to the descendants and not the spouse or the trust. See PLR 8939012. This may not be the result if the spouse/beneficiary instead exercised a special power of appointment to cause the same property to be distributed to the descendants. See I.R.C. §678(a)(1).

However, having the surviving spouse taxed on all of the income of the bypass trust even if he or she exercised a special power to appoint some of the trust property to her descendants is not necessarily a bad thing. It leverages the transfer tax advantages of the bypass trust in much the same way as an intentionally defective grantor trust.

c. Gift Tax Effects

Is the spouse's exercise of a special inter vivos power of appointment a taxable gift? If the trust contains an "all income to spouse" distribution provision, then the answer is pretty clearly yes. If, on the other hand, the trust contains an HEMS standard as to income and principal, then the answer should be no.

(1) Mandatory Income Distributions

In *Estate of Register v. Commissioner*, 83 T.C. 1 (1984), the Tax Court held that a taxable gift occurs when the income beneficiary exercised a special inter vivos power of appointment over a portion of the trust corpus. The court reasoned that, since the beneficiary was entitled to all of the income of the trust for life, an exercise of the special power of appointment was a taxable gift under I.R.C. § 2511. See also PLR 9419007 and PLR 8825080.

(2) HEMS Income and Principal Distribution Standard

Register was a case involving a trust with a mandatory income distribution provision. Does a taxable gift result when the beneficiary of a trust who is entitled to distributions based on an ascertainable standard (e.g., health, education, maintenance and support) exercises a special inter vivos power of appointment over the trust corpus?

In PLR 9451049, two sisters were beneficiaries of identical trusts. Each sister was entitled to HEMS distributions, and each had a special inter vivos power of appointment to appoint the property to a class of persons including the other sister. The sisters proposed exercising their special inter vivos powers of appointment in favor of each other with respect to the entire trust. (They did not like the remaindermen who would take in default of the appointment). The IRS ruled that the proposed exercise of the special powers would constitute a transfer of their right to receive HEMS distributions during their lifetimes under Treas. Reg. §25.2514-1(b)(2) and I.R.C. §2511(a). The Service said the value of the property interest to be transferred was readily ascertainable since, in theory, an ascertainable standard is (you guessed it) ascertainable.

However, in PLR 9451049, the taxpayers proposed exercising their powers of appointment with respect to *all* of the property in the trust. The author has found no case or ruling where the exercise of a special power with respect to a relatively small portion of a trust where the powerholder was an HEMS beneficiary resulted in a taxable gift.

In order to be a taxable gift, the exercise of the power would have to be a transfer of a right or interest in property. *See* I.R.C. §2511. As illustrated in PLR 9451049, a surviving spouse's right to receive HEMS distributions during his or her lifetime is a property interest capable (in theory at least) of valuation. If after exercise of the special power there remains in the trust sufficient income and principal to provide for the HEMS beneficiary's health, education, maintenance and support, then what property interest has been transferred? The answer should be: nothing! The powerholder still gets his or her HEMS distributions for life -- the property interest he or she held prior to the exercise of the power. Even if one assumes that exercise of the power in this situation constitutes the transfer of some property interest, the interest transferred is incapable of valuation and is a gift of a present interest (qualifying for the annual gift tax exclusion under I.R.C. §2503 as well).

Consider including a provision which prohibits the exercise of the power over property needed to satisfy the HEMS standard. This may cause confusion as to what trust property is subject to the power, especially if the surviving spouse resigns as trustee, an independent trustee is appointed successor trustee, and the surviving spouse then elects to exercise the power of appointment. Nonetheless, it should further insulate the surviving spouse from a claim that the exercise of the special power was a taxable gift.

Further comfort can be drawn (at least during the estate planning process) from the fact that the taxable gift occurs, if at all, when the power is exercised. If the power exists but is never exercised, there is no taxable gift.

In summary, if a special inter vivos power of appointment is to be used as an alternative to a spray power, then:

- Prohibit the exercise of the power to satisfy the spouse's legal obligations of support;
- Consider limiting the power to property that is not necessary to satisfy the HEMS distribution standard; and
- Never, ever use the special inter vivos power with an "all income to spouse" trust.

2. When in Doubt, Don't Include a Spray Power or a Special Lifetime Power

This may be one of those places where attorneys tend to overplan their clients' estates. If the surviving spouse is trustee and the only lifetime beneficiary (with HEMS powers as to principal and income), and if the surviving spouse has a sufficiently broad special *testamentary* power at death, then both a spray power and a special lifetime power may cause more harm than good. This is especially true in families which lean in the dysfunctional direction. Just because tax law may permit you to include something does not mean you have to include it. If the surviving spouse is the only person who can get property from the bypass trust prior to his or her death, he or she loses the ability to push greater than the annual gift tax exclusion amount to his

or her descendants tax-free, but he or she also has the perfect answer to a child who comes begging for money from the trust – “Sorry, honey, but my lawyer says the trust instrument doesn’t let me give you any money.”

H. Per Stirpes Distribution at Death vs. Special Testamentary Power

In some cases, a per stirpes distribution among testator's descendants at death is required by practical considerations. For example, in a second marriage, the wife may be willing for the husband to have use and control of the bypass trust while living, but upon his death, the wife may want to assure that the children from her first marriage get what is left.

In other cases, however, a mandatory per stirpes distribution scheme may be included when the clients would be better served if they gave each other special testamentary powers of appointment. No other device is as likely to squelch the verbalization of discord among descendants as is the creative use of a special power of appointment. Once becoming aware that he or she may be completely excluded from family wealth if he or she complains, it takes a real loathing to stir up trouble.

To be used effectively, the special testamentary power of appointment must be broad enough to permit disposition of the trust outside the circle of likely troublemakers. If the spouses have two children, and the surviving spouse has the power to appoint only to either or both children, the two children can gang up on mom or dad and effectively circumvent the special power.

One way to provide the necessary flexibility is to give the surviving spouse the power to appoint not only to descendants but also to charity (either one or more specified charities or charitable organizations broadly defined). This approach involves taking a significant risk, however. The charity and/or the Texas Attorney General may be entitled to receive notice of the probate proceeding under Tex. Prob. Code Ann. §128A, Texas Trust Code §115.011 or Tex. Prop. Code Chapter 123. For persons who have yet to have experienced it, it is difficult to overstate the frustration that can arise if a charity or, worse, the attorney general decides to get involved in your matter. While a disgruntled child ultimately is likely to be willing to reach a settlement based on economic self-interest, the attorney general's office often is not.

The author has discussed informally with personnel in the charitable trust section of the attorney general's office the question of whether or not the charity and/or attorney general is entitled to notice merely because of being named in the instrument as the possible beneficiary of the exercise of a power of appointment. Suffice it to say that, in the eyes of the attorney general's office (unofficially, of course), it is still an open question.

I. Family Limited Partnerships

Family limited partnerships may be great vehicles for managing family assets and obtaining discounts for transfer tax purposes, but they can be a source of fiduciary liability for the general partner. When used for estate planning purposes, the surviving spouse often ends up as the general partner.

Does the general partner of a limited partnership owe fiduciary duties to the limited partners? The answer to that question is cloudy, but the Texas Supreme Court has characterized the duties owed by one partner to another as "a duty in the nature of a fiduciary duty." *M. R. Champion, Inc. v. Mizell*, 904 S.W.2d 617, 618 (Tex. 1995).

Where does this leave the bereaved widow or widower who finds herself or himself as the general partner of a limited partnership?

In his "Drafting Guide to the Family Limited Partnership," 4th Annual Advanced Drafting: Estate Planning and Probate Course, State Bar of Texas (1993), Thomas C. Baird suggests including the following language in the limited partnership agreement:

The General Partner will not owe a fiduciary duty to the Partnership or to any Partner. The General Partner will owe a duty of loyalty and a duty of care to the Partnership.

Does this language lower the duty of care imposed on the general partner even further? And is this, in effect, a game of limbo — how low can one go? It seems clear that the partnership agreement cannot eliminate fiduciary-type liabilities completely, or if it does so it creates problems for the limited partnership and its partners. For example, in TAM 9751003 a Texas limited partnership agreement went so far in relieving the general partner of fiduciary-type responsibilities that the IRS took the position that gifts of limited partnership interests did not qualify for the annual gift tax exclusion because they were future interest gifts — it would be a long time, if ever, that the limited partners could compel the general partner to give them anything. See also *Hackl v. Comm’r*, 118 T.C. No. 14 (March 27, 2002) (annual gift tax exclusion denied for gifts of interests in limited liability company where manager held too much control over entity).

As a practical matter, therefore, it doesn’t matter what fiduciary-type standard is applicable. From the surviving spouse's perspective in his or her capacity as general partner, he or she owes *some* duty "in the nature of a fiduciary duty," and this is enough of a crack in the wall to inspire a disgruntled limited partner to complain of the general partner's self-serving actions to force a jury issue on the breach. Thus, whether the standard is low or high, a standard of conduct still exists, and the faces the possibility of a lawsuit for the manner in which he or she manages the partnership. (Baird also recommends including alternative dispute resolution provisions in the limited partnership agreement, so perhaps this would play out in arbitration or mediation rather than court -- a prospect only slightly more appealing to the surviving spouse.)

Of course, just because the general partner owes duties to the limited partners is no reason to never use a family limited partnership as an estate planning device. Like all planning techniques, FLPs have their advantages and disadvantages. General partner liability is just one of the issues that has to be considered when an FLP is being discussed.

J. Standard Fiduciary Powers and Duties vs. Special Powers and Duties

A trust need not provide the same powers and duties for all trustees. It may be reasonable to provide that, at all times in which the surviving spouse is serving as trustee, the trustee has narrow powers and discretion with a broad waiver of duties and broad exculpatory language. The same trust could provide that, at all times that the surviving spouse is not serving as trustee, the trustee has broad powers and discretion with a narrow waiver of duties and narrow exculpatory language. When the spouse is serving as trustee, he or she would have only limited powers regarding distributions -- all limited by an ascertainable standard -- with a minimal duty of care. If the spouse ever resigns as trustee, the successor trustee can be given broader powers (if desired) and be held to a higher duty of care.

Special fiduciary provisions for surviving spouses serving as trustee may be particularly appropriate now that Texas has adopted the Uniform Prudent Investor Act. The increased duties of a trustee under the new law, including the duty to diversify, put the surviving spouse at risk.

Consider the following provision:

9. *Limits on Duty to Diversify Investments.* If the trustee of a trust created under this Will is my wife or any of my descendants, then that trustee is not required to diversify investments as might otherwise be required by the Texas Trust Code or other applicable law, and that trustee shall not be liable for loss due to lack of diversification of investments. Each trustee (regardless of whether or not the trustee is my wife or one of my descendants) may retain any property or interest in property which I owned prior to my death and which passed into the trust by the terms of this Will or otherwise without regard to the duty to diversify investments under the Texas Trust Code or other applicable law, and the trustee shall not be

liable for loss due to lack of diversification of investments attributable to the retention of that property or interest in property.

This lowers the bar a little for the family member trustee while holding non-family-member trustees to a higher standard.

The draftsman must not get carried away in waiving fiduciary duties, however. If the spouse/trustee has essentially *no* duties, he or she may hold a general power of appointment. For example, if all duties of loyalty (both statutory and common law) are waived, then arguably there is nothing to prevent the spouse/trustee from distributing the trust property to himself or herself. The trust instrument may not empower the spouse/trustee to transfer property to himself or herself, but if there is no recourse against the trustee for so acting, he or she may hold a general power for tax purposes and/or creditor protection purposes.

K. Exculpation Clauses

If the testator's highest priority is protecting the surviving spouse, then by all means use an exculpatory clause, at least with respect to those times during which the spouse is serving as trustee. Exculpatory clauses are valid in Texas but are strictly construed against exculpation. See *Corpus Christi National Bank v. Gerdes*, 551 S. W. 2d 521 (Tex. Civ. App. -- 1977, writ refd. n.r.e.), and *Jewett v. Capital National Bank of Austin*, 618 S.W.2d 109 (Tex. Civ. App. -- Waco 1981, writ refd. n.r.e.).

The Texas Trust Code now sets the limits of exculpatory clauses in trusts. See Tex. Trust Code §114.007. The following provision attempts to exculpate family members serving as trustee to the full extent permitted by Section 114.007 while holding non-family-member trustees to the default standard:

10. **Standard of Liability.** My fiduciaries shall be held to the standards of conduct imposed on trustees by the Texas Trust Code and the applicable common law, except as otherwise provided in this Will and except as follows:

a. My wife or any descendant of mine serving as fiduciary may depart from the self-dealing rules applicable to fiduciaries without liability for profits received, so long as he or she believed the self-dealing transaction to be fair when he or she entered into it and so long as the self-dealing transaction was not entered into in bad faith or with gross negligence.

b. My wife or any descendant of mine serving as fiduciary shall not be personally liable for failing to meet these standards, so long as he or she did not act in bad faith or was not guilty of gross negligence.

L. Conflict of Interest Clauses

If protecting the surviving spouse is a priority, then at the very least a good conflict of interest clause should be included in the will or trust. This clause makes it clear that, in the event of a conflict, the conflict is resolved in favor of the surviving spouse. This type of clause can go a long way toward solving unanticipated problems in the spouse's favor. For example, it may be enough to withstand an attack against the spouse/trustee based on no spray distributions being made to descendants from the bypass trust.

Consider the following provision:

11. **Conflicts of Interest.** I realize that in the course of the administration of my estate, in the course of making distribution of estate assets, in the course of valuing any estate property, and in the course of administering any trusts

established hereunder, certain conflicts of interest may develop between my wife and my descendants or other potential beneficiaries, between the various classes of beneficiaries or between the fiduciary in the capacity of personal representative and the fiduciary in the capacity of trustee, and the beneficiaries. In the resolution of any conflict of interest, I direct each fiduciary first to make a reasonable effort to determine the overall effect of the conflict in the administration of my estate and of the trust or trusts created under the terms of this Will and then to make reasonable efforts to resolve the conflict by mutual agreement of the respective beneficiaries. In the event that mutual agreement cannot be reached after reasonable efforts, then my fiduciary shall resolve conflicts in its sole discretion based upon the following priorities:

1. My wife shall be favored at the expense of my descendants and all other classes of beneficiaries.
2. Among my descendants, my children shall be favored at the expense of more remote descendants.
3. Life tenants shall be favored at the expense of remaindermen of whatever class.

M. Tweaking Traditional Disability Planning Techniques

Of course, the estate planning attorney can reach into his or her bag of tricks for several traditional disability planning tools — durable powers of attorney for medical decisions and property management, declarations of guardianship in the event of later incapacity, directives to physicians, management trusts, etc. There are statutory forms for most of these documents,⁷ and planners should be familiar with the purposes and effects of these techniques.

This paper does not cover the basics of these techniques. Rather, it discusses factors to consider when using these devices for surviving spouses and offers suggestions on how best to utilize and modify these traditional techniques.

1. Durable Powers of Attorney for Property and Declarations of Guardian

Unless revocable management trust planning is used, the cornerstone of the disability plan for the surviving spouse will be the durable power of attorney for property. Here are some suggestions for best utilizing this device:

a. Always Back up the Durable Power of Attorney for Property with a Declaration of Guardian, and Always Designate the Same Persons Designated as Agents and Alternate Agents in the Power of Attorney as Guardians and Alternate Guardians of the Estate in the Declaration of Guardian

Appointment of a guardian of the estate for a principal revokes the power of attorney for property of that principal. Tex. Prob. Code Ann. §485. If the power of attorney is not backed up by a declaration of guardian, a family member who is not named as agent on the power of attorney may (unnecessarily) be given the incentive to seek a guardianship to displace the named agent. If the declaration of guardian names the

⁷ Tex. Prob. Code Ann. § 490 (statutory durable power of attorney form); Tex. Health & Safety Code §166.164 (medical power of attorney form); Tex. Prob. Code Ann. §679 (declaration of guardian form); Tex. Health & Safety Code §166.033 (directive to physicians and family or surrogates form). Current versions of these forms are available in WordPerfect and html (World Wide Web) formats at the author's web site (www.texasprobate.com -- click "Forms" or "Disability Planning"). There is no statutory form for a management trust.

principal's choices of guardian and alternate guardians in the same order as the agent and alternate agents on the power of attorney, a disgruntled family member may be less likely to pursue a guardianship.

Note that Tex. Prob. Code Ann. §679(d) gives a *preference* to the persons named in a declaration of guardian, but it does not require the court to appoint the designated persons. However, Tex. Prob. Code Ann. §679(b) *prohibits* the court from appointing a person who the principal says is disqualified from serving in the declaration of guardian. Therefore, if there is a really bad apple in the family, he or she (as well as his or her spouse and descendants, in most cases) should be disqualified from serving as guardian in the declaration of guardian.

Often parents are reluctant to take the step of disqualifying a child, fearing that the child may be emotionally harmed by the knowledge that his or her parent lacked confidence in him or her. While there is no way to assure that a child will not discover the existence and content of the declaration of guardian (unless, of course, it becomes necessary in a guardianship proceeding or threatened guardianship proceeding), the parent may take some comfort in the fact that the declaration of guardianship and its contents need not be disclosed to anyone prior to incapacity and need not be disclosed to the disgruntled family member after incapacity unless the agent under the power of attorney chooses to disclose it. Absent a trust arrangement, neither the parent nor the parent's agent owes any fiduciary duty to a child or other descendant of the parent — a mere expectancy of inheritance does not give rise to the existence of a right to information about the parent's estate plan. Under current Texas case law, not even a person's guardian has the right to possession of his or her will. *Bauman v. Wills*, 721 S. W. 2d 525 (Tex. App. — Corpus Christi 1986, no writ). Therefore, there is little reason to believe that a Texas court would compel the custodian of the will or other estate planning documents to deliver them (or copies of them) to family members.

Serious consideration should be given to the disqualification option. It has been the author's sad experience to represent a daughter named as agent on a power of attorney and as first choice on a declaration of guardian in a guardianship where the statutory probate court had no qualms whatsoever about throwing out the guardianship declaration and appointing the agent's sibling.⁸ The author also has had the unpleasant experience of representing the agent named in a power of attorney in a guardianship proceeding where, despite the principal's clear intent that one of her children should have nothing to do with the management of her affairs, the estate planning attorney inexplicably failed to get her to execute a declaration of guardian. These experiences make it hard for the author to overemphasize the importance of covering these issues with the client — this seemingly routine part of the estate plan cannot be glossed over.

b. In General, Co-Agents on Powers of Attorney for Property Are a Bad Idea

Parents often are reluctant to show favoritism when naming agents and ask if they can simply name two or more children as co-agents. This opens a whole new can of worms.

Do the co-agents have to act jointly on each decision, or can each act independently? In the author's experience, clients wishing to use co-agents usually want each to be able to act independently of the other. If this is the desired result, then the power of attorney should so state. Unfortunately, the statutory durable power of attorney form does not provide for co-agents, so some custom drafting is required.

What happens if the principal names co-agents but fails to specify whether they are authorized to act jointly or independently? As a legal matter, the answer is unclear. The Durable Power of Attorney Act is silent on this point. If one looks to the probate code (for estates) and the trust code (for trusts) by analogy, one gets conflicting answers. Tex. Prob. Code Ann. §240 permits each co-executor or co-administrator of

⁸ In this case, the determining factor for the court was that, while the designated agent planned to keep her mother in a nursing home near her home because job constraints prevented her from keeping her mother at home, the nondesignated sibling worked out of his home and represented to the court that his mother could live there instead of in a nursing home. While the author disagreed strenuously with the court over its readiness to disregard the proposed ward's wishes as expressed in the guardianship declaration, he does not dispute that the court was doing what it thought was best for the proposed ward.

a decedent's estate to act independently, except with respect to conveyances of real property, while Tex. Trust Code § 113.085 infers that two co-trustees must act jointly. As a practical matter, however, the answer is clear: no third party who is asked to accept the power of attorney and who is aware of the issue will accept it without the joinder of each co-agent.

The problems of requiring co-agents to act jointly are self-apparent. True, the principal may rest easy knowing that the children all must agree on an action before it is taken, but the potential for deadlock and the delay in acting is obvious.

If the co-agents may act independently, other problems may arise. Consider this hypothetical: Co-Agent A uses the power of attorney to open a checking account at a bank with the principal's funds, with herself as the only authorized signatory. Co-Agent B then goes to the same bank and seeks to withdraw the funds from the account (on which he cannot sign) using the same power of attorney. Little wonder that banks don't like to accept powers of attorney.

All of these unnecessary complications may be avoided if the principal is persuaded to name agents to serve successively rather than jointly.

c. Don't Just Use the Gift-Giving Power in the Statutory Durable Power of Attorney Form Without Considering Alternative Language

The 1997 legislative changes to the statutory durable power of attorney form now permit the principal to authorize gift-giving. To authorize gift-giving, the principal must place his or her initials at the beginning of the following sentence (on the statutory form):

I grant my agent (attorney in fact) the power to apply my property to make gifts, except that the amount of a gift to an individual may not exceed the amount of annual exclusions allowed from the federal gift tax for the calendar year of the gift.

Tex. Prob. Code Ann. §490.

Is this gift-giving provision adequate? Consider the following:

- For calendar year 2006, the annual gift tax exclusion amount is \$12,000. The exclusion amount is indexed for inflation and eventually will increase at \$1,000 increments. The gift-giving language in the statutory form will permit the gift-giving authority to grow with the inflation adjustments.
- Does the sentence in the statutory form authorize gifts to nonindividuals? For example, may the agent make gifts to charitable organizations, and are such gifts limited to \$12,000 per calendar year? May the agent make gifts to a trust (not a crummey trust, presumably, since those are, in effect, gifts to individuals), and are such gifts limited to \$12,000 per calendar year? "Individual" is not a defined term in Tex. Prob. Code Ann. § 3.

The author believes that it is unclear from the language of the statutory form whether gifts to charities and/or gifts to trusts in excess of \$12,000 per calendar year are authorized. Therefore, modification of the statutory form or use of a nonstatutory form with clearer language is recommended.

In many cases (especially where the surviving spouse has a taxable estate), gifts in excess of the annual exclusion amount should be authorized. This requires modification of the statutory form or use of a nonstatutory form.

d. *Consider Recording the Power of Attorney and Requiring Revocations to Be Recorded*

Prior to 1993 durable powers of attorney for property had to be recorded in the real property records in order to be effective. Recording the power of attorney and any revocation of the power of attorney is one way to make it relatively easy for the principal to revoke the power of attorney — he or she simply has to file a revocation instrument in the real property records, and the world is put on notice that the agent’s authority is revoked. Unfortunately, the recording requirement made powers of attorney relatively hard to use — third parties were reluctant to rely on powers without first checking the real property records, and many did not wish to go to that much trouble.

The drafters of the Durable Power of Attorney Act struggled with the easy to revoke/hard to use versus hard to revoke/easy to use issue and came down firmly in the hard to revoke/easy to use camp. Under current law, a third party is entitled to rely in good faith on the nonrevocation of a power of attorney until the third party receives actual notice of its revocation. Tex. Prob. Code Ann. §§ 487-8. Recordation of the power of attorney and/or its revocation is not required.

The hard to revoke/easy to use approach of the Durable Power of Attorney Act means that the principal may never be able to catch up with a recalcitrant agent in order to revoke a power of attorney. For example, even if the principal gives a financial institution actual notice of revocation, that notice is effective only for that financial institution and only from the date of actual notice — if the agent has pulled out funds from one institution and moved them to another institution without the principal’s knowledge, the principal is effectively precluded from revoking the power of attorney.

A principal can opt out of the hard to revoke/easy to use approach if he or she wishes by requiring the power of attorney and any revocation to be recorded in the real property records. *See* Tex. Prob. Code Ann. § 488. This may, in effect, make the power of attorney unusable, since many third parties may refuse to accept it, but it is an option which principals have and one which they should be aware of.

2. Medical Powers of Attorney and Directives to Physicians

Medical powers of attorney and directives to physicians have gained widespread use and acceptance largely due to a federal requirement that health care institutions make information about disability planning available to incoming patients as a condition to receiving federal benefits (such as Medicare and Medicaid). To meet this requirement, most hospitals and nursing homes give incoming patients medical power of attorney forms and directive to physicians forms.

The directive to physicians often is the last document discussed when meeting with a client to discuss a comprehensive estate plan. The attorney should resist the temptation to consider it merely a “throw-in” with the other planning documents. Instead, the lawyer should try to ascertain if the client really wants such an instrument. It is the author’s experience that approximately one in twenty clients do not want to leave “pull the plug” instructions — at least when first considering it. If the directive is prepared routinely, the client may sign it without thinking about it or, worse, feel pressured to sign it when it is presented with the other estate planning documents at the will signing ceremony.

3. Funeral Directives/Burial Instructions

Section 711.002 of the Texas Health & Safety Code permits a person to appoint an agent to control disposition of that person’s remains. Section 711.002 provides that the following persons, in the priority listed, have the right to control the disposition, including cremation, of the decedent’s remains *and are liable for the reasonable cost of such interment*:

- (1) the person designated in a written instrument signed by the decedent [which written instrument must be substantially in the statutory form set forth in Section 711.002];
- (2) the decedent’s surviving spouse;

- (3) any one of the decedent's surviving adult children;
- (4) either one of the decedent's surviving parents;
- (5) any one of the decedent's surviving adult siblings; or
- (6) any adult person in the next degree of kinship in the order named by law to inherit the estate of the decedent.

When someone is married, they almost always want their spouse to control the disposition of remains. Therefore, when both spouses are alive, the appointment of an agent under this section is rarely used. Even after the death of the first spouse, the surviving spouse's wishes for disposition of remains usually are obvious. For example, if the couple acquired side-by-side plots in a cemetery, it is pretty obvious that the surviving spouse wishes to be buried next to his or her former spouse.

Nevertheless, there are times when the surviving spouse's loved ones may not see eye to eye on disposition of remains. Consider the following hypothetical: Daughter Sarah lives near the family home in Diboll, Texas, while daughter Suzy lives in California. Mother spends time in both places. Mother dies while "living with" or "visiting" (depending upon one's point of view) with Suzy in California. Sarah wants mom buried in the family plot in the Diboll cemetery, while Suzy wants mom cremated with her ashes scattered on the 17th hole fairway at Pebble Beach. Under Section 711.002, both daughters have equal right — and responsibility — to control disposition of mom's remains. In this case, Mother could help eliminate the possible conflict by appointing an agent under Section 711.002.

There is one big drawback to the statutory form for appointment of an agent to control disposition of remains: the form requires the agent to sign, accepting financial responsibility for the interment. None of the other estate planning documents (except, possibly, a living trust) requires anyone other than the principal to sign. As a practical matter, this is why most estate planning attorneys do not routinely crank out these forms to go along with the wills, the powers of attorney, etc., in every estate plan.

N. Privacy Issues

One way to protect the privacy of the surviving spouse is to use a revocable management trust as the primary wealth transfer device rather than a will. See "Privacy Issues" at page 16 above. Of course, privacy is only one of many issues which must be evaluated when determining whether a client should have a will-based plan or a living trust-based plan.

Another way to preserve the privacy of the surviving spouse is to use effective disability planning techniques. Perhaps the worst invasion of one's privacy occurs when he or she is subjected to a guardianship proceeding. A public examination of his or her possible incapacity is only the beginning of the loss of privacy. Right on the heels of the incapacity determination is the filing of a guardianship inventory, applications for changes to his or her property or personal life, etc. This humiliation is best avoided by using powers of attorney for property and health that are properly backed up by a declaration of guardian.

While it may seem ironic, another way to preserve a client's privacy is the use of a corporate fiduciary rather than a family member fiduciary. While the use of a corporate trustee is not appropriate in every case, occasionally the biggest threat to one's privacy is within one's own family. A particularly private person may wish to maintain this privacy by hiring a professional trustee to assist with property management rather than relying on children or other family members.

VI. CONCLUSION

Where does all this leave poor Mrs. Brady? And where does it leave you and your malpractice carrier? Like most other unpleasant things in life, it leaves you older and wiser and hopefully in a position to avoid this mess the next time a Mr. and Mrs. Brady walks into your office.

By the way, by all reliable accounts the stars who played the Brady children all grew up to be fine, upstanding citizens. My hypothetical was just a way to focus attention on these issues and is not a reflection on those actors.

Protecting the Surviving Spouse -- And Protecting Yourself After *Belt v. Oppenheimer*

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The Friday Afternoon Cliff Notes Version

- Use your brain when planning for married couples
 - Family dynamics often are more important than theoretical tax savings
 - Care and protection of the surviving spouse usually is the highest priority
 - Don't do something for tax reasons just because you can
 - Belt v. Oppenheimer*** increases planners' risks but does not leave them defenseless
 - Ethics 101 – Who is your client and to whom do you owe duties?
 - Client communications are the key
 - Paper and speech include suggestions for engagement letters, other client communications
-

Attorney Liability for Mistakes in Estate Planning (page 5)

- Barcelo v. Elliott***
 - Privity is a defense, period.
 - Beneficiaries can't recover from estate planning attorney
 - Vinson & Elkins v. Moran***
 - But who's your client?
 - McCamish, Martin***
 - Negligent misrepresentation
-

Attorney Liability for Mistakes in Estate Planning (page 6)

- Belt v. Oppenheimer***
 - Personal representative of deceased client's estate stands in client's shoes
 - ***Barcelo*** public policy issues don't apply
 - Balancing public policy considerations permit personal representatives to sue, but not beneficiaries
 - "estate" is damaged, not who gets what
-

Helpful Client Communications (page 6)

You, and you alone, are my clients. I owe no duty to your family members or to your potential estate beneficiaries.

Helpful Client Communications (page 7)

You, and you alone, are my clients. I owe no duty to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate.

Helpful Client Communications (page 7)

You, and you alone, are my clients. I owe no duty to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate, and you waive any such duty or liability to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate.

Helpful Client Communications (page 7)

You, and you alone, are my clients. In representing you in preparing your estate plan, I want it to be clear that I have your intentions and interests at heart and that I will not be distracted by worrying about what your family members, your potential beneficiaries, or the personal representatives of your estate may think could have been done or ought to have been done. To assure my undivided loyalty to you, this will confirm our understanding that I owe no duty to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate, that you waive any such duty or liability to your family members, to your potential estate beneficiaries, to your estate or to the personal representatives of your estate, and that such persons are barred from suing me after your death.

Helpful Client Communications (page 8)

This will confirm that, while we presented you with other estate planning options, you decided not to pursue other options.

Helpful Client Communications (page 8)

Based on the information you provided to me, it is possible that the estate of the surviving spouse will be subject to estate tax. This tax could be eliminated or reduced by employing one or more tax planning strategies. We discussed some of these strategies, including the use of a credit shelter, or "bypass," trust, but you decided not to use any of these options because you preferred the simplicity and greater control of the plan described above.

Helpful Client Communications (page 8)

In helping you with your estate plan, my objective will be planning for the death or disability of either or both of you; I will not be considering the effects of a possible divorce. Either or both of you may be adversely affected by your estate plan in the event your marriage ends in divorce. If you have any questions about how this plan may affect you in the event of a divorce, please consult with an attorney experienced in family law matters.

Helpful Client Communications (page 9)

7. *My representation of you.* Please read through the enclosed documents carefully over the next two weeks. If I have made any mistakes, or if there is something you do not like or understand, please call me, and I will clear things up. If I have not heard from you within two weeks, I will assume everything is the way you want it, and my representation of you in this matter will cease.

In this matter, you and you alone have been my client. I owe no duty to any of your family members or other possible beneficiaries. I have no continuing duty to update your plan or otherwise represent you. Of course, I look forward to working with you again in the future should you wish to hire me to help you with revising your estate plan or with another matter.

Protect the Surviving Spouse From What? (pages 10 – 14)

- Fiduciary claims of descendants and remaindermen
 - Claims of creditors
 - Incompetent management of assets
 - Problems arising as a result of disclaimers
 - Problems involving disability and incapacity and
 - Invasion of privacy
-

Protecting the Spouse Using Common Planning Techniques

- Outright bequests to the surviving spouse eliminate all potential fiduciary claims against the surviving spouse (page 12)**
 - Bypass trust is *not* “just like owning it outright”
-

Protecting the Spouse Using Common Planning Techniques

- Will-based vs. revocable trust-based plans (pages 15 - 17)**
 - Will/trust contests
 - No fiduciary duties while revocable
 - Family allowance, exempt property
 - Incapacity
 - Consider prohibiting guardian from revoking trust
 - Privacy issues
-

Protecting the Spouse Using Common Planning Techniques

- Funding bypass gift with formula clause vs. disclaimer (page 17)**
 - Certainty vs. postponing decision
 - Loss of special testamentary power of appointment with disclaimer method
-

Protecting the Spouse Using Common Planning Techniques

- Spouse as trustee vs. neutral trustee (page 20)**
 - Fiduciary duties are greater with recent statutory changes, including Uniform Prudent Investor Act
 - Give spouse power to remove and replace corporate trustee
-

Protecting the Spouse Using Common Planning Techniques

- HEMS as to income vs. all income to spouse (page 20)**
 - Failure to exercise discretion can be breach of fiduciary duty
 - All income trust offers less flexibility, more safety
 - Unitrust (page 21)**
-

Protecting the Spouse Using Common Planning Techniques

I hate “spray” powers (page 21)

- Spouse/trustee with power to “spray” HEMS distributions to descendants is subject to risk and pressure
 - Better alternative: inter vivos special power of appointment
 - Tricky tax rules, though
 - Kids can still pressure Mom
 - Best alternative: No spray or special inter vivos power
 - No pressure, reduced liability
-

Protecting the Spouse Using Common Planning Techniques

I love special testamentary powers of appointment (page 24)

- Ability to steer remainder interest away from disruptive descendant is the single biggest protection the spouse/trustee has
 - Make sure the class of permissible appointees is large enough
 - Good idea to throw in charity
-

Protecting the Spouse Using Common Planning Techniques

FLPs (page 24)

- May add tax savings
 - May leave the surviving spouse (or other family members) in the lurch
 - Fiduciary issues
 - Control issues
-

Special provisions for spouse/trustees (page 25)

9. ***Limits on Duty to Diversify Investments.*** If the trustee of a trust created under this Will is my wife or any of my descendants, then that trustee is not required to diversify investments as might otherwise be required by the Texas Trust Code or other applicable law, and that trustee shall not be liable for loss due to lack of diversification of investments. Each trustee (regardless of whether or not the trustee is my wife or one of my descendants) may retain any property or interest in property which I owned prior to my death and which passed into the trust by the terms of this Will or otherwise without regard to the duty to diversify investments under the Texas Trust Code or other applicable law, and the trustee shall not be liable for loss due to lack of diversification of investments attributable to the retention of that property or interest in property.

Special provisions for spouse/trustees (page 26)

10. **Standard of Liability.** My fiduciaries shall be held to the standards of conduct imposed on trustees by the Texas Trust Code and the applicable common law, except as otherwise provided in this Will and except as follows:

a) My wife or any descendant of mine serving as fiduciary may depart from the self-dealing rules applicable to fiduciaries without liability for profits received, so long as he or she believed the self-dealing transaction to be fair when he or she entered into it and so long as the self-dealing transaction was not entered into in bad faith or with gross negligence.

b) My wife or any descendant of mine serving as fiduciary shall not be personally liable for failing to meet these standards, so long as he or she did not act in bad faith or was not guilty of gross negligence.

Special provisions for spouse/trustees (page 26)

11. **Conflicts of Interest.** I realize that in the course of the administration of my estate, in the course of making distribution of estate assets, in the course of valuing any estate property, and in the course of administering any trusts established hereunder, certain conflicts of interest may develop between my wife and my descendants or other potential beneficiaries, between the various classes of beneficiaries or between the fiduciary in the capacity of personal representative and the fiduciary in the capacity of trustee, and the beneficiaries. In the resolution of any conflict of interest, I direct each fiduciary first to make a reasonable effort to determine the overall effect of the conflict in the administration of my estate and of the trust or trusts created under the terms of this Will and then to make reasonable efforts to resolve the conflict by mutual agreement of the respective beneficiaries. In the event that mutual agreement cannot be reached after reasonable efforts, then my fiduciary shall resolve conflicts in its sole discretion based upon the following priorities:

a) My wife shall be favored at the expense of my descendants and all other classes of beneficiaries.

b) Among my descendants, my children shall be favored at the expense of more remote descendants.

c) Life tenants shall be favored at the expense of remaindermen of whatever class.

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