SETTLEMENT AGREEMENTS: CONSIDERATIONS WHEN NEGOTIATING, DRAFTING AND ENFORCING SETTLEMENT AGREEMENTS INVOLVING PROBATE, TRUST AND GUARDIANSHIP DISPUTES[1]

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CHAPTER 31

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Contested probate, trust and guardianship matters are often resolved prior to trial. A few are resolved by summary judgment, however, the majority are settled. This outline addresses various issues that should be considered when resolving probate, trust and guardianship litigation by agreement.

It is intended to provide an overview of these considerations, including estate, income and gift tax issues relating to settlement agreements reached in (i) will contests, (ii) trust disputes, and (iii) breach of fiduciary duty lawsuits. And, it includes a number of sample provisions. These provisions, however, are merely examples, and each agreement should be drafted to resolve the unique facts and issues in the particular situation. Finally, checklists and sample agreements are provided to assist when settling these matters in the early hours of the morning.

All references are to the Texas Probate Code unless otherwise noted.

II. LEGAL BASIS FOR SETTLEMENT AGREEMENTS

A. Generally

Settlement agreements are founded on both statutory and common law principals. Courts and parties often employ the fundamentals of contract law to establish, interpret and enforce settlement agreements. Rule 11 of the Texas Rules of Civil Procedure mandates the form of enforceable agreements between parties and their counsel involved in pending litigation. Section 154.071 of the Civil Practice and Remedies Code provides for enforcement of agreements realized as a result of mediation or settlement. A discussion of each of these basic tenets follows.

B. Contract Law

Compromise and settlement agreements are governed by the rules relating to the construction of contracts, including intent of the parties and offer and acceptance by the parties. *See Schlumberger Technology Corp. v. Swanson*, 959 S.W.2d 171, 178 (Tex. 1997); *Johnson v. J.M. Hubert Corp.*, 699 S.W.2d 879, 882 (Tex. App. – Amarillo 1985, writ ref'd n.r.e.) (contains release); *Stewart v. Mathes*, 528 S.W.2d 116, 118 (Tex. Civ. App. – Beaumont 1975, no writ); *TAG Resources v. Petroleum Well Services*, 791 S.W.2d 600, 605 (Tex. App. – Beaumont 1990, no writ).

A contract should generally define its essential terms "with sufficient detail to allow a court to determine the obligations of the parties." *Montanaro v. Montanaro*, 946 S.W.2d 428, 430 (Tex. App. – Corpus Christi 1997, no writ) *citing T. O. Stanley Boot Co. v. Bank of El Paso*, 847 S.W.2d 218, 221 (Tex. 1992); *see also Gannon v. Baker*, 830 S.W.2d 706, 709 (Tex. App. – Houston [1st Dist.] 1992, writ denied*); University Nat'l Bank v. Ernest & Whinney*, 773 S.W.2d 707, 710 (Tex. App. – San Antonio 1989, no writ). A party may, however, agree to certain contractual terms and leave other matters to be decided at a later time. *See Montanaro*, 946 S.W.2d at 430 *citing Scott v. Ingle Bros. Pacific*, 489 S.W.2d 554, 555 (Tex. 1972); *McCulley Fine Arts Gallery v. "X" Partners*, 860 S.W.2d 473, 477 (Tex. App. – El Paso 1993, no writ); *Magcobar North American, Inc. v. Grasso Oilfield Services, Inc.*, 736 S.W.2d 787, 795 (Tex. App. – Corpus Christi 1987, writ dism'd w.o.j.); *Frank B. Hall & Co. Inc. v. Buck*, 678 S.W.2d 612, 629 (Tex. App. – Houston [14th Dist.] 1984, writ ref'd n.r.e.), *cert. denied*, 472 U.S. 1009, 105 S.Ct. 2704, 86 L.Ed.2d 720. It is only when an essential term of a contract is left open for future negotiations that no binding contract exists. *See T. O. Stanley Boot Co.*, 847 S.W.2d at 221; *Cap Rock Elec. Co-op, Inc. v. Texas Utilities Elec. Co.*, 874 S.W.2d 92, 99 (Tex. App. – El Paso 1994, no writ); *McCulley*, 860 S.W.2d at 477.

Texas courts have indicated that what constitutes an "essential term" will be decided on a case-by-case basis. *See Charco Properties Inc. v. Law, Snakard, Garibill, P.C.*, 985 S.W.2d 262 (Tex. App. – Fort Worth 1999, n.w.h.) (time of performance not essential term); *Reppert v. Beasley*, 943 S.W.2d 172, 174 (Tex. App. – San Antonio 1997, no writ) (how agreement to be enforced was essential term); *Montanaro*, 946 S.W.2d at 431 (settlement agreement contained essential terms even though terms of required promissory did not include interest rate); *Lerer v. Lerer*, 2002 WL 31656109 (Tex.App.— Dallas 2002, pet. denied)(appellate court held that none of "(1) a specific description of the real property to be sold; (2) the expiration of the listing agreement for the sale of the real property and the appointment of brokers; (3) who controls the property during the sales; (4) who controls the proceeds from the sales of the property; (5) the date of the valuation of the properties and the terms of any sale; (6) the failure of the current trustee of the Trust to agree to the terms of the [settlement agreement], (7) the deduction of taxes and costs from sale proceeds for LRC's operations; (8) the appointment of a guardian ad litem; (9) mandatory mediation with a specified mediator; (10) payment of attorney's fees in future disputes; and (11) the terms of the mutual release" were essential and, thus, have no effect on the enforceability of the settlement agreement.).

C. Rule 11 of the Texas Rules of Civil Procedure

To the extent that a settlement agreement relates to a pending lawsuit, Rule 11 of the Texas Rules of

Civil Procedure provides the necessary requirements for enforcement of such agreements. Specifically, Rule 11 provides as follows:

> Unless otherwise provided in these rules, no agreement between attorneys or parties touching any suit pending will be *enforced* unless it be in writing, signed and filed with the papers as part of the record, or unless it be made in open court and entered of record.

TEX. R. CIV. PROC. 11 (emphasis added).

1. Writing Requirement

Rule 11 requires the agreement to be in writing to be enforced. This requirement has been relied upon by the Texas Supreme Court to deny enforcement of an oral settlement agreement. *See Kennedy v. Hyde*, 682 S.W.2d 525, 530 (Tex. 1984).

Rule 11 does not, however, prohibit oral settlement agreements made *prior* to the initiation of the litigation. *See Estate of Pollack v. McMurrey*, 858 S.W.2d 388, 393 (Tex. 1993); *Adams v. Petrade Int'l Inc.*, 754 S.W.2d 696, 714-15 (Tex. App. – Houston [1st Dist.] 1988, writ denied). Oral agreements to settle before trial are governed by contract law and Section 26.01 of the Texas Business & Commerce Code. *See Carter v. Allstate Ins. Co.*, 962 S.W.2d 268, 271 (Tex. App. – Houston [1st Dist.] 1998, writ denied); *see also Banda v. Garcia*, 955 S.W.2d 270, 272 (Tex. 1997) (Texas Supreme Court assumed oral pretrial settlement agreement was enforceable).

Rule 11 also does not prohibit the enforcement of oral offers. *See Trinity Universal Ins. Co. v. Blecker*, 944 S.W.2d 672, 675 (Tex. App. – Corpus Christi 1997) *rev'd in part on other grounds*, 966 S.W.2d 489 (Tex. 1998) (oral offers valid under contract law).

2. Multiple Documents May Constitute Rule 11 Agreement

Note that a Rule 11 may arise from one document or a series of documents, such as letters between counsel of record. One point is the Texas Supreme Court decision of *Padilla v. LaFrance*, 907 S.W.2d 454 (Tex. 1995). In *Padilla*, plaintiff's counsel made a settlement demand in a letter to defense counsel and requested the delivery of settlement documents and payment by a certain date. The defendant responded to the demand in a subsequent letter in which the defendant agreed to pay the demanded sum but inquired how a pending lien would be handled. Plaintiff's counsel responded with a third letter confirming the matter had been settled. Approximately one week after the demanded date, Defendant then proceeded to issue settlement checks, along with a formal settlement agreement. Upon receipt, plaintiff returned the checks contending that defendant did not timely accept the proposed settlement offer. Defendant then filed all three letters with the court claiming the letters constituted a valid binding settlement agreement under Rule 11. *Id.* at 458. Plaintiff responded claiming that the letters were not an enforceable settlement agreement under Rule 11, or, in the event the Court finds the letters to collectively constitute a valid Rule 11 agreement, it could not enforce the agreement because consent was withdrawn prior to the time the 'agreement' was filed with the Court. The Texas Supreme Court held that a Rule 11 agreement could be the result of multiple documents provided the documents, when construed together, reflect all material terms of the agreement. *Id.* At 460-61. The Court further held that a Rule 11 agreement is valid prior to filing and could be filed even after another party withdraws his or her consent.

3. Rule 11 Agreements Dictated to Court Reporter

It is unclear whether a settlement agreement dictated to a court reporter is an enforceable Rule 11 agreement. In *Tindall v. Bishop, Peterson & Sharp*, 961 S.W.2d 248, 249-51 (Tex. App. – Houston [1st Dist.] 1997, no writ), a settlement agreement dictated during a deposition and transcribed and signed by the court reporter, but not the parties or their lawyers, and then filed with the court was not an enforceable Rule 11 agreement. In *Kosowska v. Khar*, 929 S.W.2d 505, 507 (Tex. App. – San Antonio 1996, writ denied), however, a similar settlement agreement was enforceable as a Rule 11 agreement.

4. Rule 11 Agreements Made in Open Court

An oral settlement agreement made in open court and entered of record is enforceable. *See* TEX. R. CIV. PROC. 11; *see also Samples Exterminators v. Samples*, 640 S.W.2d 873, 875 (Tex. 1982). The noting of the agreement in the judgment or order of the court satisfies the "entered of record" requirement. *See City of Houston v. Clear Creek Basin Auth.*, 589 S.W.2d 671, 677 (Tex. 1979); *but see Tindall*, 961 S.W.2d at 251 (agreement during deposition not enforceable).

D. Texas Civil Practice and Remedies Code Section 154.071

Section 154.071 of the Texas Civil Practices and Remedies Code provides that a written settlement agreement reached in mediation and disposing of a dispute is enforceable in the same manner as any other written contract. *See* TEX. CIV. PRAC. REM. CODE § 154.071 (Vernon 2008); *see also Stevens v. Snyder*, 874 S.W.2d 241, 243 (Tex. App. – Dallas 1994, writ denied); *Martin v. Black*, 909 S.W.2d 192 (Tex. App. – Houston [14th Dist.] 1995, writ denied); *Cary v. Cary*, 894 S.W.2d 111 (Tex. App. – Houston [1st Dist.] 1995, no writ); *Hur v. City of Mesquite*; 893 S.W.2d 227, 234 (Tex. App. – Amarillo 1995, writ

denied*); Marriage of Banks*, 887 S.W.2d 160, 163 (Tex. App. – Texarkana 1994, no writ); *Marriage of Ames*, 860 S.W.2d 590, 591 (Tex. App. – Amarillo 1993, no writ).

Participants to mediation sometime draft a "term sheet" generally setting out the basic terms of a negotiated settlement. Term sheets often provide for the preparation and execution of subsequent settlement documentation satisfactory to all parties. These term sheets can be an enforceable settlement agreement or unenforceable as an agreement to agree. Enforcement is contingent on the parties' intent to be bound. *See Martin v. Black*, 909 S.W.2d 192 (Tex. App. – Houston [14th Dist.] 1995, writ denied). The court must determine whether the preparation of formal settlement documents is a condition precedent to the formation of a contract or merely a memorialization of an already enforceable contract. *Id.* at 196 *citing Foreca, S.A. v. GRD Development Co., Inc.*, 758 S.W.2d 744, 746 (Tex. 1988). A party's intent to be bound determines this issue and may be a fact issue for a jury. *Id.* at 196 (because intent disputed, question for jury). *See* discussion, *infra*.

III. STATE LAW CONSIDERATIONS

A. Why State Law Matters

In 1967, the United States Supreme Court considered whether the Internal Revenue Service could be bound by a state court adjudication of property rights when the United States was not a party. *See Comm'r v. Estate of Bosch*, 387 U.S. 456 (1967). In reaching its decision, the Court reiterated its longstanding holding that property rights are determined by state law. *See Id.* at 467("it is incumbent upon federal courts to take state law from state court decisions when federal tax consequences turn on state law"). The Court also held that when federal estate tax liability as it related to a settlement was contingent on the character of a property interest held and transferred by a decedent under state law, the Internal Revenue Service is not "conclusively bound" by a state court ruling as to a property interest. The Court formulated a new test which essentially provided that:

(i) When a state law property right has been decided by the highest court of the state, the decision should be followed and respected as the best authority for that state's law; and

(ii) When a state law property right has not been decided by the highest court of the state, federal authorities (be it the Internal Revenue Service or a tax court deciding the issue) "must apply what they find to be the state law after giving 'proper regard' to relevant rulings of other courts of the State." *Id.* at 465.

The Court recognized that its ruling will require the deciding authority to sit "as a state court." *Id.* (citing *Bernhardt v. Polygraphic Co.*, 350 U.S. 198 (1956)). Thus, a fundamental requirement of any settlement agreement is that it meets state law requirements and is based on valid rights of the parties under state law. *See* discussion *infra.*

B. Texas Law Favors Timely Settlement Agreements

It is the policy of the state of Texas to encourage resolution of disputes and the "early settlement of pending litigation through voluntary settlement procedures." TEX. CIV. PRAC. & REM. CODE ANN. § 154.002 (Vernon 2008). The Texas Supreme Court and a number of appellate courts have expressly confirmed that they continue to favor and support settlement agreements. *See Shepherd v. Ledford*, 962 S.W.2d 28 (Tex. 1998*); In Re Estate of Hodges*, 725 S.W.2d 265, 267 (Tex. App. – Amarillo 1986, writ ref'd n.r.e.); *Estate of Morris*, 577 S.W.2d 748, 755-56 (Tex. Civ. App.–Amarillo, 1979, writ ref'd n.r.e.). Encouraging settlement and compromise is in the public interest. *See Bass v. Phoenix Seadrill/78, Ltd.***,** 749, F.2d 1154, 1164 (5th Cir. 1985); *Knutson v. Morton Foods, Inc.*, 603 S.W.2d 805, 808 (Tex. 1980); *Gilliam v. Alford*, 69 Tex. 267, 6 S.W. 757, 759 (Tex. 1887).

The rationale underlying the validity of settlement agreements is explained by the Court in *Pitner v. United States* as follows:

> This approach is made possible by section 37 of the [Texas] Probate Code which provides that when a person dies leaving a will, . . . all of his estate devised or bequested by such will shall vest immediately in the devisees or legatees; . . . subject to the payment of the decedent's debts. This provision leaves the beneficiaries of an estate free to arrange among themselves for the distribution of the estate and for the payment of expenses from that estate.

388 F.2d 651, 656 (5th Cir. 1967),

Therefore, a decedent's property immediately vests in the beneficiaries named in the decedent's will, if any. This principal of immediate vesting allows beneficiaries to divide the estate, subject to any creditor claims, as they may agree and enter into a settlement agreement to that effect. The settlement agreement could result in a formal administration or provide a means to avoid it altogether. *See Estate of Hodges*, 725 S.W.2d at 267.

C. Commonly Encountered State Law Rights and Claims

While a number of state law rights and claims exist, only a few may have tax implications. A discussion of the more commonly encountered state law rights and claims follows.

1. Spousal Rights

a. Common Law or Informal Marriage

Texas is among twelve states that still recognize common-law or informal marriages. An issue as to whether a common-law or informal marriage exists between the decedent and another often arises during the estate settlement process. *See Crowson v. Wakeham*, 897 S.W.2d 779 (Tex. 1995); *Hinojosa v. Hinojosa*, 866 S.W.2d 67 (Tex. App.--El Paso 1993, no writ); *Estate of Giessel*, 734 S.W.2d 27 (Tex. App.--Houston [1st Dist.] 1987, writ ref'd n.r.e.); *Jordan v. Jordan*, 938 S.W.2d 177 (Tex. App.--Houston [1st Dist.] 1997, no writ). Once the existence of a common law or informal marriage is established, the rights and duties of a common-law spouse are equal to spouses of ceremonial marriage. *See Weaver v. State*, 855 S.W.2d 116 (Tex. App.--Houston [14th Dist.] 1993, no writ). And, the legal status of a common-law spouse is equal to that of any other married persons. *See Baker v. Mays & Mays*, 199 S.W.2d 279 (Tex. Civ. App.--Fort Worth 1946, writ dism'd). These rights include community property and other statutory rights and claims. *See e.g. Garduno v. Garduno*, 760 S.W.2d 735 (Tex. App.--Corpus Christi 1988, no writ) (informally married spouses may acquire and own community property); *Barker v. Lee*, 337 S.W.2d 637 (Tex. Civ. App.--Eastland 1960, no writ)(informally married spouses acquire homestead rights).

b. Community Property

One of the most fundamental spousal rights relates to the character of property owned at the first spouse's death. Separate property consists of:

(1) the property owned or claimed by the spouse before marriage;
(2) the property acquired by the spouse during marriage by gift, devise, or descent; and
(3) the recovery for personal injuries sustained by the spouse during marriage, except any recovery for loss of earning capacity during marriage.

TEX. FAM. CODE ANN. § 3.001 (Vernon 2006).

Community property is all property, other than separate property, acquired by either spouse during marriage. TEX. FAM. CODE ANN. § 3.002 (Vernon 1998). A presumption exists that all property acquired by either of the spouses during marriage is community property. *See* TEX. FAM. CODE ANN. § 3.003 (Vernon 2006).

If an asset is community property, it will be owned in equal undivided interests between the estate and the surviving spouse. The surviving spouse has a right to retain his or her one-half interest in all community property owned at the time of the other spouse's death. The estate also has a duty to account to the surviving spouse for post-death income from those assets in the event that community properties are in the hands of the personal representative. TEX. PROB. CODE ANN. § 378B (Vernon 2003).

The determination of whether assets are community or separate property can be an extremely complex matter and is often a source of controversy during the administration of an estate. This determination becomes even more complex when the spouses have commingled property and heirs and/or creditors are alleging that certain property is separate or community. As a result, these claims often become an issue in pending litigation and may be a legitimate basis for settlement.

c. Claims for Contribution and Reimbursement

When one spouse's marital estate benefited from expenditures made during the marriage to the exclusion of a marital estate in which the other spouse has an interest, claims for economic contribution and reimbursement arise. While originally based in equity, the Texas Legislature enacted a new statutory reimbursement governing certain claims in 1999. These statutory reimbursement were renamed claims for economic contribution in 2001. The enactment of rules regarding claims for economic contribution does not, however, completely eliminate equitable claims for reimbursement. An overview of these potential claims follows.

(i) Claim For Economic Contribution

Enacted in 1999, a surviving spouse may have a statutory claim for economic contribution. *See* TEX. FAM. CODE ANN. § 3.403 (Vernon 2006). A claim for economic contribution may be based on:

(1) the reduction of the principal amount of a debt secured by a lien on property owned before marriage, to the extent the debt existed at the time of marriage;
(2) the reduction of the principal amount of a debt secured by a lien on property received by a spouse by gift, devise, or descent during a marriage, to the extent the debt existed at the time the property was received;
(3) the reduction of the principal amount of that part of a debt, including a home equity loan:
    (A) incurred during a marriage;
    (B) secured by a lien on property; and

(C) incurred for the acquisition of, or for capital improvements to, property;

(4) the reduction of the principal amount of that part of a debt:
   (A) incurred during a marriage;
   (B) secured by a lien on property owned by a spouse;
   (C) for which the creditor agreed to look for repayment solely to the separate marital estate of the spouse on whose property the lien attached; and
   (D) incurred for the acquisition of, or for capital improvements to, property;

(5) the refinancing of the principal amount described by Subdivisions (1)-(4), to the extent the refinancing reduces that principal amount in a manner described by the appropriate subdivision; and

(6) capital improvements to property other than by incurring debt.

TEX. FAM. CODE ANN. § 3.402(a) (Vernon 2006).

But, a spouse is not entitled economic contribution based on (i) expenditures for ordinary maintenance and repairs, taxes, interest, or insurance, or (ii) the contribution by one spouse of his or her time, toil, talent, or effort during the marriage. TEX. FAM. CODE ANN. § 3.402(b) (Vernon 2006).

(ii) Claim For Reimbursement

Furthermore, a surviving spouse may also have a claim for reimbursement. TEX. FAM. CODE ANN. § 3.408 (Vernon 2006). A claim for reimbursement may be based up (i) payment during the marriage by "one marital estate of the unsecured liabilities of another marital estate" (i.e., a community debt by one spouses separate estate or vice versa); and/or (ii) inadequate compensation for the time, toil, talent, and effort of one spouse by a business under the control and direction of that spouse. TEX. FAM. CODE ANN. § 3.408(b) (Vernon 2006). As compared to the statutory formula that applies to claims for economic contribution, a claim for reimbursement is decided by the court by "using equitable principles, including the principle that claims for reimbursement may be offset against each other if the court determines it to be appropriate." TEX. FAM. CODE ANN. § 3.408(c) (Vernon 2006). Thus, the court may offset the monetary value of the spouse's use and enjoyment of property against a claim for reimbursement. TEX. FAM. CODE ANN. § 3.408(d) (Vernon 2006).

d. Homestead

A homestead right, regardless of whether the property is separate or community, may be claimed when the decedent is survived by a spouse. *See* TEX. PROB. CODE ANN. §§ 272, 282 (Vernon 2003); *Givens v. Hudson*, 64 Tex. 471 (1885); *Zwerneznann v. Von Rosenburg*, 76 Tex. 522, 13 S.W. 485 (1890); *Childers v. Henderson*, 76 Tex. 664, 13 S.W. 481 (1890); *Jenkins v. Hutchens*, 287 S.W.2d 295 (Tex. Civ. App.—Eastland 1956, writ ref'd n.r.e.). A rural homestead consists of 200 acres of land for a married decedent or 100 for a single decedent, while an urban homestead consists of a lot or lots not exceeding ten acres. *See* TEX. CONST. ART. 16, § 51; TEX. PROP. CODE ANN. § 41.001 (Vernon 2000 & Supp. 2008). As recently amended, Section 41.001 of the Texas Property Code provides that "[i]f used for the purposes of an urban home or as both an urban home and a place to exercise a calling or business, the homestead of a family or a single, adult person, not otherwise entitled to a homestead, shall consist of not more than 10 acres of land which may be in one or more contiguous lots, together with any improvements thereon." TEX. PROP. CODE ANN. § 41.001(a) (Vernon 2000& Supp. 2008).

Title to a homestead vests in the heirs of the decedent as other real property under the laws of descent and distribution upon death with a surviving spouse. *See* TEX. PROB. CODE ANN. § 283 (Vernon 2003). Thus the homestead cannot be construed as an estate asset subject to the control of the representative or court, nor is any income derived therefrom. *See* TEX. PROB. CODE ANN. § 282 (Vernon 2003); *Childers v. Henderson*, 76 Tex. 664, 13 S.W. 481 (1890); *Franklin v. Woods*, 598 S.W.2d 946 (Tex. Civ. App.—Corpus Christi 1980, no writ); *Thompson v. Thompson*, 149 Tex. 632, 236 S.W.2d 779 (1951). The homestead may not be partitioned until all superior rights of occupancy have been terminated. *See* TEX. CONST. ART. 16, § 52; TEX. PROB. CODE ANN. § 8 (Vernon 2003); *Hudgins v. Sansom*, 72 Tex. 229, 10 S.W. 104 (1888).

e. Family Allowance

Immediately upon approval of the inventory, the court shall fix a family allowance for support of the surviving spouse. Such allowance shall be sufficient for their maintenance for one year from the date of death. *See* TEX. PROB. CODE ANN. §§ 286-293 (Vernon 2003). No allowance can be made for spouses who possess sufficient separate property of their own from which they are able to provide for their own maintenance. *See* TEX. PROB. CODE ANN. § 288 (Vernon 2003); *Pace v. Eoff*, 48 S.W.2d 956 (Tex. Comm'n App. 1932, holding approved); *Kennedy v. Draper*, 575 S.W.2d 627 (Tex. Civ. App.—Waco 1978, no writ); *Noble v. Noble*, 636 S.W.2d 551 (Tex. Civ. App.—San Antonio 1982 writ ref'd n.r.e.). This allowance when proper, is a matter of right and is not construed as an advancement, thus repayment at the end of the estate is not required. *See* TEX. PROB.

CODE ANN. § 290 (Vernon 2003); *Chefflet v. Willis*, 74 Tex. 245, 11 S.W. 1105 (1889); *Stutts v. Stovall*, 544 S.W.2d 938 (Tex. Civ. App.—San Antonio 1976, writ ref'd n.r.e.). A family allowance can consist of money, property, or both, and the court may order a sale of assets to raise such allowance, including the sale of property specifically bequeathed when no other assets exist. *See* TEX. PROB. CODE ANN. §§ 292, 293 (Vernon 2003).

f. Exempt Personal Property

Surviving spouses, minors and unmarried children are entitled to have exempt personal property set aside for their use during administration. *See* TEX. PROB. CODE ANN. §§ 271, 272 (Vernon 2003); TEX. CONST. ART. 16, § 49; TEX. PROP. CODE ANN. §§ 42.001 and 42.002.

(i) Solvent Estates

In a solvent estate, exempt property may be used by persons entitled thereto during the administration. But, the right to use these assets terminates when the estate is closed. The property is then distributed to the heirs or devisees of the decedent. *See* TEX. PROB. CODE ANN. § 278 (Vernon 2003); *Kelley v. Shields*, 448 S.W.2d 135 (Tex. Civ. App.—San Antonio 1969, writ ref'd n.r.e.).

(ii) Insolvent Estates

In an insolvent estate title to the exempt personal property passes to the spouse and children free of all debts, except those debts secured by existing liens, or claims for funeral and last illness expenses presented within sixty days of the issuance of letters of administration. *See* TEX. PROB. CODE ANN. §§ 277, 279, 281, 320(a)(1) (Vernon 2003); *American Bonding Co. of Baltimore v. Logan*, 106 Tex. 306, 166 S.W. 1132 (1914) (Certified Questions Answered).

(iii) Allowance in Lieu

When a decedent's estate does not contain a homestead or exempt personal property, the surviving spouse and children may apply to the court for an allowance in lieu thereof. An allowance of up to $15,000 for the homestead and $5,000 for other exempt property is permitted. *See* TEX. PROB. CODE ANN. §§ 273, 275 (Vernon 2003); *In re: Mays' Estate*, 43 S.W.2d 306 (Tex. Civ. App.—Beaumont 1931, writ ref'd). Such allowance may be satisfied in money, property, or both, and regardless of whether it was bequeathed to another. *See* TEX. PROB. CODE ANN. § 274 (Vernon 2003). Property of the estate may be sold by court order to obtain funds necessary for the payment of such allowance. *See* TEX. PROB. CODE ANN. § 276 (Vernon 2003).

2. Tort Claims

a. Breach of Fiduciary Duty

Some claims arising at the death of an individual can take the form of tort claims for their actions (or inactions) occurring during lifetime. A common example of this type of claim relates to the failure by the executor/surviving spouse to fund the bypass trust created under the Will of the first spouse to die. As a result of this failure, all of the couple's assets are titled in the name of the surviving spouse, and the value of the surviving spouse's estate may be grossly overstated at the time of the second death, unless it is offset by the value of the claim of the bypass trust.

(i) The Constructive Trust Approach

In *Stansbury v. United States*, 543 F. Supp. 154 (N.D. Ill. 1982), aff'd by 735 F.2d 1367 (7th Cir. 1984), the court found that a decedent held property in a constructive trust for the benefit of another, and the court permitted the trust property to be excluded from the estate of the decedent. This result was based on the argument that the decedent held the property merely as a naked title holder. Thus, the decedent did not own an interest in the property at her death or possess a power of appointment over the trust property. (Note: This case did not involve a bypass trust.)

Applying the *Stansbury* rationale to the case of an unfunded bypass trust would suggest that some of the assets on hand at death of the surviving spouse belong not to the spouse, but to the bypass trust. Under Texas law, a trustee is charged with a fiduciary duty not to commingle trust property with trustee's own property. *Boettcher v. Means*, 201 S.W. 2d 255, 256 (Tex. Civ. App.—Galveston, 1947). If the trustee commingles trust property with his own property, the rights of the trust beneficiaries are not destroyed. *Pierce v. Sheldon Petroleum Co.*, 589 S.W. 2D 849 (Tex. Civ. App.--Amarillo, 1979). The trust beneficiaries have the right to recover trust property held by the trustee that can be identified as the original trust property or that can be traced as the mutations (i.e., proceeds or products) of the original trust property. *Batmanis v. Batmanis*, 600 S.W. 2D 887 (Tex. Civ. App.—Houston [14th District], 1980); *Pierce v. Sheldon Petroleum Company*, 589 S.W. 2D 849. Where the trustee in *Batmanis* had commingled trust money with his own money, it was presumed that any money expended was the trustee's own money and not the trust property. 600 S.W. 2d at 890.

This rationale suggests that any amounts consumed by the surviving spouse would be treated as have come from his or her own assets first, and not from the trust. Identifying assets as the original trust property can sometimes be done, especially with

respect to real estate. Often, if deaths are in fairly quick succession and assets were not actively traded, a number of assets on hand at the second death can be identified as having been included in the first spouse's estate. Tracing "mutations" of property is perhaps more problematic, especially if substantial time has elapsed between the dates of death. Presumably, tracing principles similar to those used to identify separate and community property in a divorce context may be employed, but most likely at considerable expense.

(ii) The Debt Approach

Section 2053(a)(3) of the Code provides that for purposes of the tax imposed by Section 2001, the value of the taxable estate shall be determined by deducting from the value of the gross estate such amounts for claims against the estate as are allowable by the laws of the jurisdiction under which the estate is being administered.

In *Bailey v. Commissioner*, 741 F.2d 801 (5th Cir. 1984), when a father died, the son inherited property, but the mother never set up a separate account for the son's benefit and did not acknowledge his inheritance rights. In administering the mother's estate, the son first became aware of his inheritance rights in his father's estate, and the son took a section 2053 deduction as a claim against the mother's estate. The son contended that the amount of this claim was the current value of the property he should have inherited from his father's estate, and that on these facts the Texas courts would impress a constructive trust in his favor. Although the Tax Court found for the government, the Fifth Circuit Court of Appeals reversed, allowing the section 2053 deduction but remanding for a determination of the current value of the son's inheritance from his father.

Applying this rationale suggests that the surviving spouse's estate would be entitled to a Section 2053 deduction for amounts owed to the bypass trust. Quantifying the debt may be problematic. It would seem that an analysis much like the constructive trust tracing-consumption-distribution approach would be required here as well.

Alternatively, as the court in *Batmanis* reminds us: "It is clearly the law in Texas that interest is allowed as damages for the failure to pay a sum due. . . . [I]nterest should be at the rate of 6% from the date due until the date of judgment." 600 S.W.2d 877, 890. For decedents dying before January 1, 2004, former Section 378B of the Texas Probate Code mandate the payment of interest on a pecuniary bequest at the statutory rate of six percent beginning one year after letters testamentary were issued. For decedents dying on or after January 1, 2004, interest accrues from the date of death. TEX. PROP. CODE ANN. § 116.051(3) (Vernon 2007). If substantial time has lapsed since the time of the first death, the IRS might argue that the statute of limitations has run, so no claim survives at the time of the death of the surviving spouse. *See* TEX CIV. PRAC. & REM. CODE ANN § 16.051 (Vernon 2008).

But when does the cause of action "accrue"? In cases involving constructive trusts, the statute does not begin to run until the beneficiary knew, or should have known, that he or she had a cause of action. *See Kelley v. Kelley*, 575 S.W.2d 612, 618 (Tex. Civ. App.—San Antonio 1978, writ ref'd n.r.e.). The beneficiary of an estate has the right to presume that the executor will carry out the provisions of the Will, and in due time will pay the bequest. Therefore, the statute of limitations will not begin to run until the executor has definitely and finally notified the beneficiary that no payment will be forthcoming under the Will. *See Savage v. Delagado*, 93 S.W.2d 480 (Tex. Civ. App.—San Antonio 1936, writ dism'd). For a discussion of these issues as well as issues relevant to the potential gift tax aspects of failure to fund, see Tracy, *Implementation of Estate Planning Strategies--Mechanics of Pecuniary Formula Bequests*, STATE BAR OF TEXAS ADVANCED STRATEGIES COURSE, 1999.

b. Wrongful Death and Personal Injury

Tort claims can create a valid deduction for a decedent's estate. One of the most significant of these claims can be claims or debts relating to the personal injury of a person by the decedent. Furthermore, the surviving spouse, children, and parents of an injured person have a separate cause of action for their own personal injuries. *See* TEX. CIV. PRAC. & REM. CODE § 71.004 (Vernon 2008)(cause of action for wrongful death exists for the "exclusive benefit of the surviving spouse, children, and parents of the deceased"). Potential claims can be made by both non-family members and family members. *See e.g.* TEX. CIV. PRAC. & REM. CODE § 72.001 (person who is related to owner or operator of motor vehicle within second degree by consanguinity or affinity and who is being transported in motor vehicle over public highway of State of Texas as a guest without payment for transportation has cause of action against owner or operator of motor vehicle for injury, death, or loss in an accident only if accident was intentional on the part of owner or operator or was caused by his heedlessness or reckless disregard of rights of others). Thus a potential beneficiary of an estate may also have a valid claim against the estate based on tort claims if the decedent causes injury to him or his child, spouse or parents.

3. Payment of Attorneys Fees

The payment of attorneys' fees and expenses is often a material term in a trust or estate settlement. If not addressed, the settling parties may be involved in additional litigation regarding their payment. Furthermore, properly structured, these payments may be of substantial tax benefit to the estate. *See* discussion *infra.*

a. Estate and Will Contests

The personal representative of an estate may recover all necessary and reasonable expenses incurred in the preservation, safekeeping, and management of the estate and all reasonable and necessary attorneys fees incurred in connection with the settlement of the estate. *See* TEX. PROB. CODE ANN. § 242 (Vernon 2003).

Furthermore, Texas Probate Code Section 243 allows a named personal representative or beneficiary to seek payment of their attorney's fees and expenses from the estate in a contested matter. *See* TEX. PROB. CODE ANN. § 243 (Vernon 2003); *see also Salmon v. Salmon*, 395 S.W.2d 29 (Tex. 1965) (reasonable fees mean hourly not contingent fees). A finding of good faith and just cause determine whether or not the expenses incurred in the probate of a will may be charged to the estate. It is irrelevant whether the personal representative was successful. *See* TEX. PROB. CODE ANN. § 243 (Vernon 2003). Effective September 1, 2003, awards of fees and expenses pursuant to Section 243 will be considered administration expenses and, thus, have priority over other potential creditors.

b. Trust Disputes

A trustee is statutorily entitled to reimbursement for attorneys' fees and expenses and other costs incurred in administering and protecting the trust. *See* TEX. PROP. CODE ANN. § 114.063 (Vernon 2007). Most trust agreements provide that a trustee is entitled to pay his professional advisors from the trust or to be reimbursed for such expenses.

4. Other Claims

a. Slayer's Rule

Article 1, Section 21 of the Texas Constitution provides that "[n]o conviction shall work corruption of blood, or forfeiture of estate, and the estates of those who destroy their own lives shall descend or vest as in case of natural death. Likewise, Section 41(d) of the Texas Probate Code directs that "no conviction shall work corruption of blood or forfeiture of estate" except in the case of a beneficiary of a life insurance policy under the Texas Insurance Code. *See* discussion *infra.*

Texas courts have held, however, that, in the interest of public policy, a murderer should not be able to inherit from his victim. As a result, courts may impose constructive trusts to prevent such convicted individuals from benefiting from their wrongdoing. A number of Texas cases have elaborated on the rationale of imposing a constructive trust. For example, in stating that a constructive trust prevents unjust enrichment, the court in *Pritchett v. Henry*, 287 S.W.2d 546, 550 (Tex. Civ. App.—Beaumont, 1955), added "a surviving spouse should not be permitted to keep or enjoy the property of the community since by his willful act he has made certain that he survives his deceased spouse . . .."

Nevertheless, under Texas law, it is not entirely clear which class of people should benefit from the constructive trust. In *Pope v. Garrett*, 211 S.W.2d 559 (1948), the Supreme Court noted that "equity imposes a trust on property in favor of one who is in good conscience entitled to it." The details of that case permitted the court to impose the trust in favor of a beneficiary intended to be in the decedent's Will - rather than the decedent's heirs or the contingent beneficiaries named in the Will. Furthermore, in *Pritchett*, the constructive trust was imposed in favor of an individual who was both the contingent beneficiary under the Will and the decedent's sole heir. In *Bounds v. Caudle*, 560 S.W.2d 925 (1978), the surviving spouse was convicted of negligent homicide. The court imposed a constructive trust in favor of the decedent's children to prevent the surviving spouse from taking under the Will and the life insurance policy. It is unknown whether the children or any other individuals were named as contingent beneficiaries in either the Will or the insurance policy. As a result, these cases do not provide much specific guidance on the proper beneficiaries of a constructive trust.

Gordy v. Alexander, 550 S.W.2d 146 (Tex. Civ. App.—1977) stands for the proposition that the intent of the decedent determines the proper beneficiaries of a constructive trust. In *Gordy*, the decedent was allegedly killed by her daughter; although, no criminal proceeding had yet been held. Under the decedent's Will, her property was to pass in trust to her daughter or to Jean Gordy if her daughter predeceased her. The daughter alleged that the court could not determine the proper distribution of the estate because her illegitimate daughter, the decedent's sole heir, was not a party in the suit. The court agreed because, without the heir, it could not be determined if it was the decedent's intention for Gordy to take. Thus, the court clearly stated that "the intent of the murder victim should determine who benefits from any constructive trust." Id. at 149. However, the court did

not give any guidance in determining the intent of the decedent.

There are two Texas cases that directly address the rights of the surviving spouse to the homestead and family allowance. In *Ovalle v. Ovalle*, 604 S.W.2d 526 (Tex. Civ. App.—Waco, 1980), the probate court awarded the surviving spouse a family allowance, money in lieu of exempt property, personal property, and the right to occupy the homestead. The administrator of the estate and the decedent's children (who were not children of the surviving spouse) opposed this award because the surviving spouse intentionally killed the decedent. In the criminal proceeding, the trial court found that the widow was "justified in using deadly force against her husband because she reasonably believed that such force was immediately necessary to protect herself." Id. at 527. Nevertheless, the judgment in a criminal proceeding is not binding upon the court in a civil proceeding. Id. at 528. In reversing the award granted to the surviving spouse by the probate court, the court quoted a Missouri case:

> [O]ne may qualify as a widow within the purview of the statute authorizing payment of widow's allowance from the estate of the deceased only if she has been reduced to widowhood by the ordinary and usual vicissitudes of life and not be her own felonious act which created the condition.

Id. The court, however, upheld the award of allowance in favor of the decedent's minor child.

In *Ford v. Long*, 713 S.W.2d 798 (Tex. Civ. App.—Tyler, 1986), an action was brought by the decedent's sister, the sole beneficiary of the estate, to partition the property owned jointly with the decedent's husband who had been convicted of murder and imprisoned. The husband contested the sister's suit by claiming both a homestead right in the real property and the right to use the furniture as exempt property for the remainder of his life. Nonetheless, the court ordered the sale of the property and the division of the proceeds equally between the two parties. The court reasoned that had the husband predeceased his wife, he would have no homestead interest in the land. "Since by his willful act [the husband] made certain his survival, he should be precluded from keeping and enjoying property he takes as a survivor in the community." Id. It should be noted that in each of these cases, the surviving spouse had been found to have killed the decedent prior to losing rights to the homestead and the family allowance.

Texas courts have permitted the surviving spouse to take the murdered decedent's property (without the imposition of a constructive trust) when the surviving spouse was found not guilty by reason of insanity. See *Hair v. Pennsylvania Life Insurance Co.*, 533 S.W.2d 387 (Tex. Civ. App.—Beaumont, 1975); *Simon v. Dibble*, 380 S.W.2d 898 (Tex. Civ. App.—San Antonio, 1964).

The IRS has determined that it is not possible to contract around similar state laws to take advantage of estate tax deductions unless such agreement avoids the need for judicial resolution of the matter. In Technical Advice Memorandum 9530003, a spouse accused of killing her husband and the husband's children entered into a settlement agreement before trial, attempting to resolve the parties' respective claims against the decedent's estate. Although the spouse pled not guilty, the spouse was convicted of murder. *See* Tech. Adv. Mem 9530003 (July 28, 1995). When the estate's federal estate tax return was filed, a marital deduction was claimed for the property that passed to the spouse under the settlement agreement. The IRS denied the deduction on the basis that the settlement agreement was not enforceable:

> When the settlement agreement was entered into, the issue of conviction was completely unsettled. There was a substantial amount of property riding on the determination of guilt or innocence, and neither the mother nor the children wished to be placed in an all or nothing situation based on a jury verdict. . . .The spouse's interest was ultimately to be determined by the judicial process. . .. The settlement agreement did nothing to avoid the need for further judicial proceedings.

Id.

Therefore, it appears that the IRS is willing to recognize only those settlement agreements that eliminate the need for a judicial resolution of a contested will. Nevertheless, a marital deduction will be allowed when it is unlikely that a beneficiary would ever be convicted for her role in a decedent's murder. See *Estate of Cloud v. U.S.*, 71A AFTR 2d 93-4997 (1988).

State law governs whether an estate has an interest in or right to insurance policy proceeds. See *Estate of Draper*, 64 T.C. 23 (1969). In Texas, for example, the Insurance Code states that proceeds go to the "nearest relative" rather than the estate.

b. Insurance Code Section 1103.151

Under Section 1103.151 of the Texas Insurance Code, a beneficiary who is a principal or accomplice in bringing about the death of the insured forfeits his interest in the policy. As a result, the policy proceeds are paid to the contingent beneficiaries named by the insured in the policy (assuming such contingent beneficiaries are neither principals nor accomplices). If no contingent beneficiaries are named, the proceeds

pass to the "nearest relative" of the insured. See Tex. Ins. Code § 1101.152.

There are no cases that interpret the "contingent beneficiary named by the insured" language. The prior version of the statute did not contain language which permitted contingent beneficiaries of the insurance policy to receive the proceeds of the policy; such proceeds went to the "nearest relative." However, in 1975, the Texas Supreme Court considered with issue of whether the contingent beneficiary named by the decedent in the policy could take under the statute. The court permitted the contingent beneficiary to take the proceeds, reasoning that it was the legislature's intent to "prevent the murderer from receiving such proceeds" but not to "forfeit the right of a guiltless named beneficiary." See *Deveroex v. Nelson*, 529 S.W.2d 510, 514 (Tex. 1975).

In 1987, the Texas Supreme Court again considered this issue and overruled *Deveroex*. The court reasoned that:

> [t]he fact that the legislature chose to withhold proceeds from the beneficiary/killer does not mean that the legislature intended that the nearest relative would succeed to the proceeds only upon the disqualification of all beneficiaries. . . . Rather our holding recognizes the specific direction of section 21.23 [now section 1103.152] that when a beneficiary willfully brings about the death of the insured, the proceeds succeed to the decedent's nearest relative.

See Crawford v. Coleman, 726 S.W.2d 9, 11 (Tex. 1987).

In dicta, the *Crawford* court addressed the distinction between beneficiaries named by the insured and beneficiaries pre-printed in the policy text. In the case, the life insurance policy contained pre-printed language that awarded the policy proceeds "to the insured's beneficiary, then to the insured's spouse, then to the insured's children, then to the insured's parents." The plaintiff's argued that contingent beneficiaries could only take such proceeds when they were expressly named by the insured. However, the court rejected the distinction between a pre-printed beneficiary provision and a beneficiary whose name is written into the policy, stating "in each instance the insured has selected the individual as a beneficiary even though by different means. There is no difference when an insured reads and agrees to the policy's pre-printed beneficiary designations or when the insured writes out the name of the beneficiary." Id. at 10 n.1.

The Texas Legislature subsequently amended the statute to include the current language addressing the receipt of policy proceeds by contingent beneficiaries. It is not clear that in amending the statute to address receipt of the proceeds by a contingent beneficiary, the Legislature intended to further clarify that such contingent beneficiary must be named by the insured, rather than pre-printed in the policy.

IV. OVERVIEW OF FUNDEMENTAL TAX CONSIDERATIONS

A. General Overview of Amounts Received in Settlement of Will Contest

Amounts received in settlement of a will contest are generally not subject to income and gift taxes. *See Lyeth v. Hoey*, 305 U.S. 188 (1938) (Court held settlement amount not subject to income tax under I.R.C. Section 102); *see also*, Priv. Ltr. Rul. 8902045 (Oct. 21, 1988) (bona fide settlement does not result in gift tax under I.R.C. Section 2501). But, the effect of the settlement on death taxes depends on the existence of a bona fide dispute, the transfers involved, and the existence of an enforceable right as between the settling parties.

B. Enforceable Right Under State Law

A party to a settlement should not automatically assume that the property and proceeds received or paid in settlement will automatically be deemed to have "passed" from the Decedent to a person pursuant to a settlement agreement. It is particularly important with regard to property to be received by a spouse or charity under a settlement agreement. The failure to meet the passing requirement can result in the property being subject to estate tax notwithstanding the identity of the recipient.

As discussed *supra*, the Supreme Court held in *Bosch* that the "test of 'passing' for estate tax purposes should be whether the interest reaches the spouse pursuant to state law, correctly interpreted [by the federal court]—not whether it reached the spouse as a result of a good faith adversary confrontation." *Estate of Brandon v. C.I.R*, 828 F.2d 493, 497 (8th Cir. 1987) (citing *Bosch* at 774). Thus, the availability of deductibility depends on whether the settlement payment is made pursuant to an enforceable right, i.e. as in *Brandon* whether the spouse's claims were based on an enforceable state law. *See discussion supra*.

C. Bona Fide Dispute Requirement

Likewise, a party to a settlement should not automatically assume that the property and proceeds received or paid in settlement will not be subject to income or gift tax. The Internal Revenue Service will not consider a settlement agreement to be a bona fide compromise agreement unless the parties' claims are (i) bona fide and (ii) satisfied on an economically fair basis. *See* Priv. Ltr. Rul. 8902045 (Oct. 21, 1988).

To avoid future issue, the settlement agreement should reflect that an actual bona fide dispute exists between the parties. Consider expressly setting out the basis for each person's claim in the settlement agreement. *See* discussion *infra.*

In a will contest scenario, the agreement should identify the name of each party, and their interest or standing in the proceeding, i.e., spouse, common law spouse, heir, beneficiary under prior will, etc. *See* discussion *infra.* This allows the IRS to determine from the settlement agreement the validity of each person's potential claim and possibly avoid a full tax audit.

1. Bona Fide Dispute Does Not Require Full Scale War

While truly adverse positions indicate a bona fide dispute, courts have held that a settlement in favor of the surviving spouse will qualify for the marital deduction where the disagreement is short of a full scale war. *See Citizens and Southern Nat'l Bank v. United States*, 451 F.2d 221 (5th Cir. 1971); *see also Estate of Hubert v. Comm'r*, 101 T.C. 314 (1993), *aff'd*, 63 F.3d 1083 (11th Cir. 1995) (marital deduction allowed for payments to spouse in settlement of bona fide will contest); *Estate of Dutcher v. Comm'r*, 34 T.C. 918 (1960), acq., 1961-1 C.B. 4; *Ducan v. United States*, 236 F. Supp. 747 (D. Md. 1965); *First Nat'l Bank v. United States*, 328 F. Supp. 1339 (N.D. Ala. 1971); *Estate of Barrett v. Comm'r*, 22 T.C. 606 (1954).

2. Lack of Bona Fide Dispute May Result in Transfer Being Subject to Taxes

Settlements derived from collusive or spurious suits may not qualify as a bona fide dispute. For example, property passing to a spouse under an agreement where there was not a bona fide dispute will not qualify for the marital deduction because property passing under these agreements is not deemed to have passed from the decedent, but merely by agreement of the parties. Obviously, any amounts that the surviving spouse gives up in the settlement will not qualify for the marital deduction. Treas. Reg. § 20.2056(c)-2(d)(2)

V. ESTATE TAX CONSIDERATIONS

A. Generally

The payments made pursuant to a settlement agreement and the structure of those payments can have a significant effect on the amount of estate taxes ultimately paid. The availability of marital and charitable deductions depends on the form and substance of the agreement. Furthermore, the payment of debts and administration expenses, including attorneys' fees and expenses, may be deductible for estate tax purposes.

B. The Marital Deduction

The marital deduction should be considered where there is a settlement agreement with the spouse or common law spouse.

1. I.R.C. Section 2056

Section 2056 of the Internal Revenue Code requires that the property must have passed from the decedent to his surviving spouse and that it must not be a non-deductible terminable interest in order to qualify for the marital deduction. I.R.C. § 2056. Section 2056(a) provides:

> (a) Allowance of marital deduction.--For purposes of the tax imposed by section 2001, the value of the taxable estate shall, except as limited by subsection (b), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

I.R.C. § 2056.

A potential pitfall exists in agreements where the surviving spouse agrees to reduce a fee interest in property otherwise passing to the spouse to some form of terminable interest. In such situations, the terminable interest the spouse retains will not qualify for the marital deduction. *See Estate of Thomas W. Tebb*, 27 T.C. 671, Dec. 22,212, 1967; *see also U.S. Trust Company (Estate of R.S. Davenport) v. Comm'r*, 63-2 U.S.T.C. ¶ 12177, 321 F.2d 908 (2d Cir.), *cert. denied*, 376 U.S. 937 (1963).

a. Qualified Interests

Interests that qualify for the marital deduction include:

- An outright transfer to a surviving spouse who is a U.S. citizen, so long as the spouse's interest is not conditioned upon survival for a period of more than six months.
- An interest passing to a trust for the surviving spouse that provides the spouse with the exclusive right to all income for life, and grants to the spouse a general power of appointment over the trust property at death (a so-called "life estate-power of appointment" or "LEPA" trust).
- An interest passing to a trust for the surviving spouse that provides the spouse with the exclusive right to all income for life, and for which an election is made causing the property remaining in the trust to be taxed in the spouse's estate at the time of the spouse's

later death (a so-called "qualified terminable interest property" or "QTIP" trust).

- An interest passing to a trust for the surviving spouse that provides the spouse with the exclusive right to all income for life, and provides that upon the death of the surviving spouse, the remaining trust property vests in a qualified charity (a so-called "spousal charitable remainder" trust).
- Insurance or annuity proceeds held by the insurer subject to an agreement either to pay the proceeds in installments, or to pay interest on them, during the surviving spouse's life only to the surviving spouse, so long as the installments are payable at least annually, beginning not later than 13 months after the decedent's death, and the surviving spouse has the power to appoint the amounts to the surviving spouse or his or her estate.

I.R.C. § 2056.

Each of the foregoing interests are subject to detailed addition requirements designed to ensure that the spouse receive income from the property, that no person has the ability to appoint property to anyone other than the surviving spouse during his or her lifetime and (except in the case of a QTIP trust) that the spouse has the unrestricted right to dispose of the property at death alone and in all events.

b. Passing Requirement

The principal issue in the settlement context involves the *passing* requirement. The regulations state that if an interest is assigned or surrendered to the surviving spouse as a result of a controversy, the interest will be treated as having passed from the decedent to the surviving spouse in the decedent's estate." Treas. Reg. § 20.2056(c)-2(d)(2). Specifically, Treasury Regulation 20.2056(c)-2(d)(2) provides as follows:

> If as a result of the controversy involving the decedent's will, or involving any bequest or devise thereunder, a property interest is assigned or surrendered to the surviving spouse, the interest so acquired will be regarded as having "passed from the decedent to his surviving spouse" only if the assignment or surrender was a *bona fide recognition* of *enforceable rights* of the surviving spouse in the decedent's estate. Such a bona fide recognition will be *presumed where the assignment or surrender was pursuant to a decision of a local court upon the merits in an adversary proceeding following a genuine and active contes*t. However, such a decree will be accepted only to the extent that the court passed upon the facts upon which deductibility of the property interests depends. If the assignment or surrender was pursuant to a decree rendered by consent, or pursuant to an agreement not to contest the will or not to probate the will, it will not necessarily be accepted as a bona fide evaluation of the rights of the spouse.

Treas. Reg. § 2056(c)-2(d)(2)(emphasis added); *see also Brandon*, 828 F.2d at 499; *Bel v. U.S.*, 452 F2d 683 (5th Cir. 1971); *Estate of Barrett v. Comm'r*, 34 T.C. 606 (1954).

As discussed previously, the Supreme Court has held that the test of "passing for estate tax purposes" is "whether the interest reaches the spouse pursuant to state law, correctly interpreted [by the federal court]—not whether it reached the spouse as a result of a good faith adversary confrontation." *Brandon*, 828 F.2d at 499 (citing *Bosch*, 387 U.S. at 774).

c. Enforceable Right

In order to qualify for the marital deduction, the surviving spouse must have an "enforceable right" under state law. *Brandon*, 828 F.2d at 499 (citing *Ahmanson Foundation v. United States*, 674 F.2d 761, 774 (9th Cir.1982)). In *Bosch*, the Supreme Court mandated that Internal Revenue Service was only bound by the decision of the highest state court as to a spouse's enforceable property rights. *Bosch*, 387 U.S. 465. In *Ahmanson Foundation v. United States*, 674 F.2d 761 (9th Cir. 1981), the Ninth Circuit held that property distributed to a spouse pursuant to a compromise settlement will be treated as passing from the decedent for marital deduction purposes, only if the distribution represents a good faith settlement of an enforceable claim. Relying on *Comm'r v. Estate of Bosch*, 387 U.S. 456 (1967), the court stated that:

> [E]ither a good faith settlement or a judgment of a lower state court must be based on an *enforceable right under state law properly interpreted*, in order to qualify as 'passing' pursuant to the estate tax marital deduction.

Ahmanson Foundation v. United States, 674 F.2d at 775 (emphasis added).

More recently, in Private Letter Ruling 200417030, the Internal Revenue Service stated that:

> In view of *Ahmanson*, property passing to a spouse (or charity) pursuant to the settlement of a claim will be treated as passing from the decedent, to the extent the compromise is a *bona fide settlement* of a *legally enforceable claim*. The claim must be settled pursuant to arm's length negotiations.

Priv. Ltr. Rul. 200417030 (January 16, 2004)(allowed marital deduction when either party could have prevailed at trial).

2. Interest Released by Surviving Spouse

The estate is not entitled to a marital deduction for property or other interests released, assigned or surrendered by the surviving spouse. Treas. Reg. § 2056(c)-2. Treasury Regulation 2056(c)-(d)(1) entitled will contests provides that:

> If as a result of a controversy involving the decedent's will, or involving any bequest or devise thereunder, his surviving spouse assigns or surrenders a property interest in settlement of the controversy, the interest so assigned or surrendered is not considered as having "passed from the decedent to his surviving spouse."

Treas. Reg. § 2056(c)-2(d)(1); *see also Schroeder v. United States*, 924 F.2d 1547 (10th Cir.1991).

3. Settlement Agreement Versus Judicial Determination

Payment made to a surviving spouse pursuant to a settlement agreement will be accorded the same treatment as ones made pursuant to a judicial decree. On point is the decision of *Estate of Barrett v. Comm'r*, 22 T.C. 606 (1954). In *Barrett*, a settlement was reached with a surviving spouse prior to the initiation of formal litigation regarding his forced share of the deceased spouse's estate. The Internal Revenue Service claimed that the payments made pursuant to the settlement agreement did not qualify for the marital deduction. The Tax Court, however, disagreed noting that:

> In *Lyeth v. Hoey*, the Supreme Court found too formal for substance the distinction between a payment made to an heir pursuant to judgment in a proceeding contesting a will and a payment made in compromise, in advance of trial, of the claims made in the proceeding. We think, similarly, that the distinction pressed by the respondent, on the basis of his regulations, between a payment made pursuant to an order of a local court after a fully litigated proceeding and a payment made in settlement of claims that avoids a will contest is without merit. A will contest can exist without full blown legal proceedings and we have no doubt that the executor in this case recognized the threat made on his sister's will. If the proceeding had ever come to issue and trial, the executor may well have opposed Barrett's claim, though recognizing as a danger that there was a possibility that Barrett might succeed and be awarded a substantial sum of money. If Barrett had litigated his claim and been awarded a judgment, the amount received by him would qualify as a marital deduction as an interest passing by inheritance. We find nothing in the statute or in logic that would deny similar treatment to a settlement payment made in advance of the contest where there is sufficient basis for a reasonable belief that only such payment would avoid a serious and substantial threat to the testamentary plan provided by the decedent.

Id. at 610.

More recently, the Internal Revenue Service issued Private Letter Ruling 9347003, in which it confirmed that:

> [A] settlement of a claim asserted by the surviving spouse for a share of the decedent's estate must be based on a legally enforceable claim and paid pursuant to a bona fide compromise agreement. The claim must be asserted in good faith and settled in arm's length negotiations and may be arrived at without court action. *See Estate of Barrett v. Comm'r*, 22 T.C. 606 (1954), and *Citizens and Southern National Bank v. United States*, 451 F.2d 221 (5th Cir.1971).

Priv. Ltr. Rul. 9347003 (August 5, 1993)(held amounts paid to surviving spouse to settle will contest were eligible for marital deduction, but only to extent they did not exceed value of spouse's community claim against decedent's estate under Texas law).

C. Other Claims or Payments Made To The Surviving Spouse

1. Community Property Claims

As discussed previously, the surviving spouse of a Texas resident effectively owns an undivided one-half interest in the community estate remaining at the time of the first spouse's death. *See* discussion *supra*. The decedent's gross taxable estate is only required to include the decedent's one-half interest. *See* I.R.C. § 2033. A common claim in estate litigation involves the claims of the surviving spouse as to the character of the assets that exist at the death of the first spouse.

In *Ahmanson Foundation*, the Ninth Circuit considered the availability of the marital deduction or exclusion of assets paid to a surviving spouse in settlement of her community property claims. *Ahmanson*, 674 F.2d at 773. The Internal Revenue Service argued that the marital deduction or community property exclusion was limited to the value of qualifying property that the surviving spouse had a right to receive under state law at the time of the decedent's death. *Id. at* 772. The Court stated that "the effect of the [marital deduction and community property exclusion were] the same" and that the two were "intended to play parallel and complimentary roles." *Id.*. The Court held that neither a binding non-supreme court adjudication nor a private settlement agreement were binding on the Internal Revenue Service; instead, "the test of 'passing' for estate tax

purposes should be when it reached the spouse as a result of a good faith adversary confrontation. By equating the marital deduction and community property claims, the Court suggested that the value of a spouse's claim under state law "properly applied" is not limited solely to rights under the will. *See Id.* The case was ultimately remanded by the Ninth Circuit for fact findings and a determination of California law as to the value of claim.

2. Claims for Contribution & Reimbursement

I.R.C. Section 2053(a)(3) allows a deduction from the value of the gross estate for claims against the estate provided that the claim is "allowable by the laws of the jurisdiction, . . . under which the estate is being administered." Section 20.2053-4 of the Estate Tax Regulations provides that only claims that are enforceable against the decedent's estate may be deducted under Section 2053 of the I.R.C.

As discussed *supra*, a surviving spouse (or deceased spouse) may have a claim for economic contribution against the other spouse's estate. *See* II.D.1(c) *supra.* The resulting claim may be an asset or liability of the estate of the deceased spouse.

For example, assume a surviving spouse has a $100,000 claim for economic contribution relating to the expenditure of her separate property to reduce the mortgage on a community property asset. The surviving spouse would have claim "allowable" under Texas law equal to $100,000. On the decedent's death tax return, the executor would be entitled to take a deduction equal to $50,000 (i.e., the decedent's one-half of the community debt of $100,000), assuming such amounts is timely presented and paid, on Schedule K. Assume, however, the surviving spouse claimed that community estate had a $100,000 claim for economic contribution relating to the expenditures of community property to reduce the mortgage on separate property of the decedent. In that situation, the decedent's estate would:

(i) include a $100,000 community asset on Schedule F (of which $50,000 would be included in the gross estate, i.e., the decedent's one-half community property interest), and

(ii) take a deduction equal to $100,000 assuming such amounts is timely presented and paid, on Schedule K.

3. Homestead Claims

As previously discussed, a surviving spouse generally has a right to right to occupy the resident used by him or her and the deceased spouse for as long as he or she desires. The homestead can, however, be abandoned if the surviving spouse relocates to a difference residence. Therefore, the homestead may terminate prior to the surviving spouse's death. Thus, the marital deduction is not available for a homestead right. *See* Priv. Ltr. Rul. 8736004 (1987).

The unavailability of the homestead right should be considered when structuring a settlement with a spouse. If possible and appropriate, consideration should be given to the surviving spouse receiving the property outright or, alternatively, a life estate. Both of these interests have a greater chance of meeting the requirements of Section 2056.

4. Family Allowance Claims

As previously discussed, a surviving spouse generally has a right to seek a family allowance relating to the costs of support for the first year following the deceased spouse's death. The Tax Court has held that the payment of a family allowance will not qualify for a marital deduction. *See Estate of Snider v. Comm'r*, 84 T.C. 75 (1985) (Tax Court held that family allowance under Texas law is contingent on determination by Texas Court that the spouse's separate property is inadequate for her maintenance for one year after her husband's death, and therefore not indefeasible and unconditional as of the moment of her husband's death; as a result the allowance is a nondeductible terminable interest.); *see also Jackson v. U.S.*, 376 U.S. 503 (1964), aff'g 317 F.2d 821 (9th Cir. 1963)(family allowances generally do not qualify because they are not fixed right vested at death); *but see Radel Est. v. Comm'r*., 88 T.C. 1143 (1987) (Tax Court held that family allowance under Minnesota law was not discretionary and contains no contingencies, therefore, the 'spouse allowance' was nonterminable interest under Minnesota law and qualified for marital deduction).

While not deductible, a separate tax consideration is that a spouse's right to a family allowance generally has priority over the government's priority under 31 U.S.C. 3713 as these claims generally are not debts but are charges against the property of the decedent to be deducted before payment of debts. *See* Rev. Rul. 80-112, 1980-1 C.B. 306.

D. The Charitable Deduction

The rules involving charitable deductions in the family settlement context are less complex than those involving the marital deduction.

1. I.R.C. Section 2055

Section 2055 of the Internal Revenue Code permits an unlimited deduction for qualifying bequests made to charities, and amounts passing to charities pursuant to settlement agreements are generally deductible.

2. Deductible Amount

The amount deductible is the amount the charity actually receives under the settlement agreement. *See* REV. RUL. 145, 1953-2 Cum. Bull. 273; *see also Reed v. United States*, 317 F. Supp. 1242 (D.C. Cir. 1970); *Irving Trust Company v. United States*, 221 F.2d 303 (2d Cir.), *cert. denied*, 350 U.S. 328 (1955); *Heim v. Nee*, 40 F. Supp. 594 (D.C. Ohio 1960). If the charity is to receive direct payment or specific property, recent cases and rulings support the availability of the charitable deduction. When, however, the charity will receive a split interest, for example an interest in trust, the rulings are less favorable and Internal Revenue Service appears to scrutinize these transactions more closely.

Note, where the charitable beneficiary is taking the residue of the estate, certain special, although logical, rules apply. In that circumstance, any amount paid to a non-charitable beneficiary's claim reduces the charitable deduction. *See Reed*, *supra*. If the amount the charity pays directly to the non-charitable beneficiary is paid from estate income, however, the portion attributable to estate income does not reduce the estate tax charitable deduction. *See Oldham v. Campbell*, 217 F. Supp. 819 (D.E. Tex. 1963).

Furthermore, if a charity's interest is contingent upon an event to occur, the charitable deduction is not available "unless the possibility that the charitable transfer will not become effective is so remote as to be negligible." Treas. Reg. § 20.2055.-2(b)(1).

3. Charity Must Have Bona Fide Claim

The Internal Revenue Service has stated that it will scrutinize settlement of will contests to be sure that the litigation was not collusive or instituted merely to obtain the charitable deduction. *See* REV. RUL. 89-31, 1989-9 I.R.B. 32; T.A.M. 8945004 (Aug. 4, 1989).

E. Deducting Litigation Expenses

Litigation expenses are deductible as expenses of administration under Internal Revenue Code § 2053(a)(2) if they are actually and necessarily incurred in the proper administration and settlement of a decedent's estate and are allowable under applicable state law. *See* discussion *supra.* Expenses of administration are not generally deductible, however, when incurred for the individual benefit of heirs, legatees, or devisees. *See Estate of Dutcher v. Comm'r*, 34 T.C. 918 (1960); *Estate of Landers v. Comm'r*, 38 T.C. 828 (1962); *Estate of Baldwin v. Comm'r*, 59 T.C. 654 (1973).

a. Administration Expenses

Treas. Reg. § 20.2053-3(a) provides, in part, that a decedent's gross estate is entitled to a deduction on Schedule J for administration expenses actually and necessarily incurred in the administration of the decedent's estate including the collection of assets, payment of debts, and distribution of property to the persons entitled to it. These administration expenses include attorney's fees.

b. Litigation Expenses

The Internal Revenue Code allows a will contestant's fees and expenses to be deducted, *see Sussman v. United States*, 236 F. Supp. 507 (E.D.N.Y. 1962), and the Texas Probate Code allows the attorneys fees of will contestants to be charged to the estate where the contestant is a devisee, legatee, or beneficiary of a will or an alleged will or an administrator with will annexed. *See* TEX. PROB. CODE ANN. § 243 (Vernon 2003). Such allowance is limited to good faith actions based on just cause. *Id.; see also Wick v. Fleming*, 652 S.W.2d 353 (Tex. 1983) (holding that good faith and just cause finding must be made in original proceeding); *Alldrige v. Spell*, 774 S.W.2d 707 (Tex. App. – El Paso 1989, no writ) (requiring jury finding of good faith before awarding attorney's fees); *Currie v. Drake*, 550 S.W.2d 736 (Tex. Civ. App. – Dallas 1977, writ ref'd n.r.e.).

F. Tax Apportionment

When drafting a will, the draftsman pays special attention to the apportionment of estate and inheritance taxes to ensure that the intended net after-tax benefit comports with the client's wishes. Section 322A of the Texas Probate Code provides for a mandatory method of tax apportionment, noting that it does not apply "to the extent the decedent in a written inter vivos or testamentary instrument disposing of or creating an interest in property specifically directs the manner of apportionment . . ." or grants discretionary authority in another person. *See* TEX. PROB. CODE ANN. § 322A(B)(2) (Vernon 2003 & Supp. 2008). In the context of a settlement that ignores or overrides the will, any tax apportionment language in the will may be set aside, leaving the parties with tax apportionment under Section 322A.

In advising clients about the impact of a proposed settlement, the apportionment of estate and inheritance taxes should be carefully thought through, and the "net" numbers examined. To the extent that the settlement is structured with a view toward minimizing or eliminating transfer taxes, more funds will be left on the table to be divided among the parties. Even in those circumstances, however (and perhaps especially in those circumstances), thought should be given to who will bear the tax risk if the

IRS is successful in re-characterizing some component of the transaction, and as a result, taxes are owed. In this setting, the parties may wish to negotiate an indemnity for taxes ultimately assessed, and provide notice and an opportunity to participate in the tax dispute for the party who may ultimately be charged with the tax. *See* discussion *infra.*

VI. GIFT TAX CONSIDERATIONS

A. Generally

Section 2501 of the Internal Revenue Code places a tax on property transfers by gift and Section 2512(b) provides that where a transfer of property is made for less than adequate consideration, that the amount in excess of fair consideration will be treated as a gift. Generally, a transfer of property by an individual in compromise and settlement of threatened estate litigation is a transfer for full and adequate consideration in money or money's worth and, thus, is not a gift for federal gift tax purposes. *See Irma Lampert*, T.C.M. 1184 (1956); *see also Righter v. United States*, 66-2 U.S.T.C. ¶ 1242, 258 F. Supp. 763 (8th Cir. 1966) *rev'd and remanded on other grounds* 68-2 U.S.T.C. ¶ 12554, 400 F.2d 344 (8th Cir. 1968).

B. Unintended Gifts

Where there is no adequate consideration for the settlement agreement, gift tax consequences may arise. *See Nelson v. United States*, 89-2 U.S.T.C. (CCH) ¶ 13,823 (D.N.D. 1989) (unreported). Private Letter Ruling 8902045 involved a will contest settlement and considered the issue of whether transfers pursuant to the settlement were subject to the gift tax. The ruling indicates that the Internal Revenue Service has fully adopted the *Ahmanson Foundation* reasoning. *See* discussion *supra*. In particular, the Internal Revenue Service opined that intra-family settlements should not result in shifts between the parties' economic rights, that the economic values of the parties' claims should be determined "with appropriate allowances for uncertainty," and that "differences may be justified on the basis of compromise." Priv. Ltr. Rul. 8902045.

C. Use of Surviving Spouse's Exemption Amount

In a settlement involving a surviving spouse, the overall tax effect of the settlement may be improved by having other parties agree to forego claims so that property passes to the surviving spouse in a manner that qualifies for the unlimited estate tax marital deduction. It may be easier to obtain the agreement of others to forego claims if the surviving spouse is willing to make donative transfers to those persons, perhaps utilizing his or her federal gift tax exemption. While the marital deduction may be disallowed if the IRS determines that the surviving spouse purchased an interest from the other claimants, properly structured, such a technique effectively allows the use of both the decedent's estate tax exemption and the surviving spouse's gift tax exemption to pass property without current transfer taxes to persons other than the spouse or charity.

Naturally, the surviving spouse must feel comfortable that the loss of his or her gift tax credit (and effectively, a corresponding amount of estate tax credit at a later death), will not work an undue hardship on the spouse's intended beneficiaries. There is a perception, however, that the estate tax exemption is likely to be substantially increased in future years, and younger spouses may be willing to bet that future increases to the estate tax exemption will be sufficient to avoid estate taxes for heirs, even after the current use of some or all of the gift tax exemption.

VII. INCOME TAX CONSIDERATIONS

A. Taxation of Will Contest Settlement

1. General Rule

Under the general rule of Section 102 of the Internal Revenue Code, "gross income does not include the value of property acquired by gift, devise, or inheritance." I.R.C. § 102(a). Similarly, the portion of an estate received by an heir in compromise of his will contest against the decedent's will is generally exempt from federal income tax. *See Lyeth v. Hoey*, 305 U.S. 188 (1938); *Quigly v. Comm'r*, 143 F.2d 27 (7th Cir. 1944). In *Lyeth*, the Supreme Court addressed for the first time the issue of whether property received by a person from the estate of a decedent in compromise of his claim as an heir was subject to income tax under the predecessor to I.R.C. Section 102. Because the property was received via a settlement instead of pursuant to a will or heirship statute, the Internal Revenue Service took the position that the property was subject to income tax because the then applicable state law provided that state successor taxes applied to property passing under the will as written and regardless of any subsequent settlement agreement. *Id.* at 190. The Supreme Court held that property was properly excluded from income because:

> There is no question that petitioner obtained that portion, upon the value of which he is sought to be taxed, because of his standing as an heir and of his claim in that capacity. It does not seem to be questioned that if the contest had been fought to a finish and petitioner had succeeded, the property that he would have received would have been exempt under the federal act. Nor is it questioned that if in any appropriate proceeding, instituted by him as heir, he had recovered judgment for a part of the estate, that part would

> have been acquired by inheritance within the meaning of the act. *We think that the distinction sought to be made between acquisition through such a judgment and acquisition by a compromise agreement in lieu of such a judgment is too formal to be sound, as it disregards the substance of the statutory exemption*.

Id. at 196 (emphasis added).

Furthermore, Section 663(a)(1) provides that a gift or bequest of a specific sum or property will not be taxable as follows:

> There shall not be included as amounts falling within I.R.C. Sections 661(a) or 662(a) if the amount paid, under the terms of the governing instrument, is properly paid or credited as a gift or bequest of a specific sum of money or of specific property and which is paid or credited all at once or in not more than *3 installments.*

I.R.C. § 663(a)(1)(emphasis added); *see also* Treas. Reg. § 1-102-1(d)("[a]ny amount required to be included in the gross income of a beneficiary under sections 652, 662, or 668 shall be treated for purposes of this section as a gift, bequest, devise, or inheritance of income from property. On the other hand, any amount excluded from the gross income of a beneficiary under section 663(a)(1) shall be treated for purposes of this section as property acquired by gift, bequest, devise, or inheritance").

2. Exception: Distributable Net Income

The structure of the payments or distribution may subject the beneficiary to income tax. For example, the payment of an amount from the residuary of an estate could carry out distributable net income (i.e. income) while the payment of a specific sum will not. *See* I.R.C. § 663(a)(1)(DNI does not include "[a]ny amount which, under the terms of the governing instrument, is properly paid or credited as a gift or bequest of a specific sum of money or of specific property and which is paid or credited all at once or in not more than 3 installments"). Distributable net income, commonly referred to as DNI, is a fundamental concept of income taxation of trusts, estates and their beneficiaries. It is a concept uniquely applicable to the taxation of trusts and estates and is necessary to implement the conduit principle, that is, a trust or estate is often nothing more than a conduit for property to pass to its beneficiaries. Taxable income must be modified in several respects in order to serve as an effective measure of the maximum allowable deduction to estates or trusts for distributions to beneficiaries and amounts which beneficiaries must include in their gross income. As modified, the taxable income of an estate or trust is labeled DNI.

DNI is basically the amount of trust or estate income available for distribution in a particular tax reporting year. It can be classified as a trust's gross income, excluding net capital gains allocated to principal, but including net tax exempt income, minus allowable deductions and losses. I.R.C. § 643(a). Distributable net income serves three functions. First, trust or estate DNI establishes the maximum amount that a trust or estate can deduct under I.R.C. Sections 651 and 661. Likewise, DNI determines the maximum amount that the trust or estate beneficiaries can be taxed under I.R.C. Sections 652 and 662. Finally, DNI determines the character of a distribution by a trust or estate. Specifically, it is used to characterize and divide distributions into different "classes" of income. The character of a distribution may also affect the maximum deduction allowed to the fiduciary and the maximum portion of the distribution included in gross income by the beneficiary.

Unless a specific exception applies, all estate distributions, whether in cash or in kind, carry out the estate's DNI. Generally, the amount of DNI carried out by an in-kind distribution to a beneficiary is the *lesser* of the adjusted basis of the property prior to distribution, or the fair market value of the property at the time of the distribution. I.R.C. § 643(e). The estate does not generally recognize gain or loss as a result of making a distribution to a beneficiary. This general rule is subject to some important exceptions.

a. Distributions of Assets to Fund Pecuniary Gifts

A concept related to the "discharge of obligation" notion is a distribution of assets to fund a bequest of "a specific dollar amount," including a pecuniary bequest or a formula bequest. For example, an agreement requiring an executor to distribute $400,000 worth of property, if funded with assets worth $400,000 at the time of distribution, but worth only $380,000 at the date of death, will cause the estate to recognize a $20,000 gain. The rules governing this area should not be confused with the "specific sum of money" rules that govern DNI carry outs. Unless the formula language is drawn very narrowly, most formula gifts do not constitute gifts of a "*specific sum of money*," exempt from DNI carryout, because they usually cannot be fixed exactly at the date of death (for example, most formula marital bequests must await the executor's determination of whether administration expenses will be deducted on the estate tax return or the estate's income tax return before they can be computed). Such gifts are, however, treated as bequests of "*a specific dollar amount*" for gain recognition purposes, regardless of whether they can be precisely computed at the date of death. As a result, gains or losses will be recognized

by the estate if the formula gift describes a pecuniary amount to be satisfied with date-of-distribution values, as opposed to a fractional share of the residue of the estate. *Compare* Treas. Reg. § 1.663(a)-1(b) (to qualify as bequest of specific sum of money or specific bequest of property, and thereby avoid DNI carry-out, the amount of money or the identity of property must be ascertainable under the will as of the date of death) *with* Treas. Reg. § 1.661(a)-2(f)(1) (no gain or loss recognized unless distribution is in satisfaction of a right to receive a specific dollar amount or specific property other than that distributed); *see also* Treas. Reg. § 1.1014-4(a)(3); Rev. Rul. 60-87, 1960-1 C.B. 286. For fiscal years beginning on or before August 1, 1997, estates could recognize losses in transactions with beneficiaries. Although the Taxpayer Relief Act of 1997 repealed this rule for most purposes, an estate may still recognize a loss if it distributes an asset that has declined in value in satisfaction of a pecuniary bequest. I.R.C. § 267(b)(13). Note, however, that loss recognition is denied to trusts used as estate surrogates as a result of the related party rules of Section 267(b)(6) of the Code, except for qualified revocable trusts electing to be treated as estates under Section 646 of the Code.

b. Distributions To Satisfy the Estate's Obligations

Distributions that satisfy an obligation of the estate are recognition events for the estate. The fair market value of the property is treated as being received by the estate as a result of the distribution, and the estate will recognize any gain or loss if the estate's basis in the property is different from its fair market value at the time of distribution. Rev. Rul. 74-178, 1974-1 C.B. 196. Thus, for example, if the estate agrees to pay a debt of $10,000 pursuant to a settlement agreement, and transfers an asset worth $10,000 with a basis of $8,000 in satisfaction of the debt, the estate will recognize a $2,000 gain.

c. Separate Share Rule

Section 663 of the Internal Revenue Code provides that when multiple beneficiaries have substantially separate and independent shares of a trust or estate, each beneficiary's "separate share" may be treated as separate trust or unit for the limited purpose of determining the amount of net income distributed to each beneficiary during the tax reporting period. The question of what constitutes "substantially separate and independent shares" is not resolved by the I.R.C. but is instead expressly left to be determined by the Treasury Regulations. I.R.C. § 663(c).

The separate share rule provides a certain measure of relief from the automatic application of the tier system and from the restricted nature of the gift and bequest exclusion. It can prevent one beneficiary being taxed on a corpus distribution as though that beneficiary had received income when the income, in reality, is accumulated for the benefit of another.

Prior to the passage of the Taxpayer Relief Act of 1997, the separate share rule only applied to trusts. The adoption of the separate share rule for estates results in more equitable shifting of estate income as between and among its beneficiaries. The disadvantage is that it will also lead to increased complexity when determining each beneficiary's share of estate income.

3. Exception: Bequest of Income

Section 102 also does not apply to amounts required to be paid pursuant to a settlement agreement from income. If the bequest or inheritance is the right to receive income, the amounts are taxable to the beneficiary. *See* I.R.C. § 102(b). Specifically, Section 102(b) provides that:

> (b) Income.--Subsection (a) *shall not exclude* from gross income—
>
> (1) the income from any property referred to in subsection (a); or
>
> (2) where the gift, bequest, devise, or inheritance is of income from property,
>
> the amount of such income.

I.R.C. § 102(b) (emphasis added); *see also Harte v. United States*, 252 F.2d 259 (2d Cir. 1958); *Tree v. United States*, 55 F. Supp. 438 (Ct. Cl. 1944), *cert. denied*, 324 U.S. 852 (1945).

In settlements, an issue exists whether the settlement will be characterized as a bequest of income when the original bequest was of income. When the settlement is in lieu of an income interest, the courts have generally held the settlement amount is includable in gross income under I.R.C. Section 102(b). *See Getty v. Commissioner*, 91 T.C. 160, 176 (1988), rev'd. 913 F.2d 1486, 1492 n. 7 (9th Cir.1990). In *Getty*, the court noted that:

> [W]hether a claim is resolved through litigation or settlement, the nature of the underlying action determines the tax consequences of the resolution of the claim." *Tribune Publishing Co. v. United States*, 836 F.2d 1176, 1177 (9th Cir.1988). In characterizing the settlement payment for tax purposes, we ask, " 'In lieu of what were the damages awarded?' " Id. at 1178 (quoting *Raytheon Prod. Corp. v. Commissioner*, 144 F.2d 110, 113 (1st Cir.), cert. denied, 323 U.S. 779, 65 S.Ct. 192, 89 L.Ed. 622 (1944)); *see also Spangler v. Commissioner*, 323 F.2d 913, 916 (9th Cir.1963) (question was what the taxpayer would have received had sums wrongfully withheld been paid when due); *Victor E. Gidwitz*

> *Family Trust v. Commissioner*, 61 T.C. 664, 673-74 (1974) (question was what the taxpayer would have received in a merger had the consideration for the taxpayer's shares been adequate).

Id. at 176

For example, in *Harrison v. Commissioner*, 119 F.2d 963 (7th Cir. 1941), *aff'g*. 41 B.T.A. 1217 (1940), the deceased spouse's will did not comply with a prenuptial agreement that required the decedent to establish a trust that would pay all of its income to the surviving spouse for life. The surviving spouse was entitled, under applicable state law, to renounce the will and take one-half of the estate. The surviving spouse ultimately entered into a settlement whereby she received (i) a specific sum of money, and (ii) an additional cash payment relating to the delay in funding the testamentary trust. The court held that the payment of the specific sum was exempt under Section 102 as it related to her right to renounce the will and take one-half of the estate, however, the remaining amount was subject to income tax because it related to her right to receive income from date of death forward. *See Id.* at 1124.

More recently, in *Getty v. Comm'r*, 913 F2d 1486 (9th Cir. 1990), *rev'g* 91 TC 160 (1988), the Ninth Circuit considered whether the settlement of the testator's son's suit, seeking to impose a constructive trust to enforce the testator's promise to remedy the inequality of the financial treatment of his various children during his lifetime, was excludable from gross income as being in the nature of a bequest, devise, or inheritance. Under the testator's will, the son was only entitled to nominal bequest and the son sought to impose a constructive trust on estate assets in an amount equal to the income received by the testator's other children. The son and the other beneficiaries entered into a settlement under which the son received $10,000,000 in settlement of his claims. The I.R.S argued that the son's claim was for income from property because in his complaint the son characterized the benefit he sought in enforce as a claim for income. The son's complaint alleged that the testator promised to provide for the son, in his will, an amount equal to the income received by the testator's other children prior to the testator's death. The I.R.S. argued that the settlement amount was not excluded from the son's gross income because the claimed bequest was one of income. The court, however, declined to review the son's pleadings so narrowly and instead expressly employed a broader approach in determining the true nature and basis of the son's claim. The court construed the claim to be a claim for inheritance equal to the amount of income the other children received, not of income. Because, the testator could have remedied the inequality with a bequest of property as opposed to a bequest of income, the court held the settlement amount was excludible from income as a bequest. *Id*. at 1491.

4. Exception: Bequest for Services Rendered

Bequests made to compensate for services rendered to the decedent are not excluded from income. *See Cotnam v. C.I.R.*, 263 F.2d 119 (5th Cir.1959); *see also Wolder v. Comm'r*, 493 F.2d 608 (2nd Cir., 1974), *cert. den*. 419 U.S. 828 (1974)(payment to lawyer in the form of bequest was method that parties chose to compensate lawyer for his legal services and was subject to taxation), *Davies v. C.I.R.*, 23 TC 524 (1954); *Estate of Braddock v. U.S.*, 434 F2d 631 (9th Cir. 1970); *Jones v. C.I.R.*, T.C.M. 1958- 191 (CCH) (1958); Priv. Ltr. Rul. 67-375 (1967)(distribution of property under will in satisfaction of written agreement under which taxpayers were required to perform services for testator is compensation for services includible in their gross income in the taxable year of receipt).

In *Cotnam*, the taxpayer won a contract action against the decedent's estate based on her claim that the decedent had promised Cotnam one-fifth of his estate in return for her serving him as an attendant. Cotnam was not a heir or beneficiary under a prior will. When Cotnam failed to include the judgment in her gross income, the Internal Revenue Service assessed a deficiently for the amount of the judgment. Cotnam claimed the amount of the judgment was exempt as a bequest under Section 102. The Fifth Circuit Court of Appeals disagreed finding that the judgment was not exempt as a bequest but, rather, was taxable income for services rendered to the decedent. *Id.* at 121. In finding the payments should be taxed as income, the court noted that:

> The nature of the transaction underlying the judgment, not the judgment itself, controls the tax effects. *United States v. Safety Car Heating Co.*, 1936, 297 U.S. 88, 56 S.Ct. 353, 80 L.Ed. 500; *Arcadia Refining Co. v. Comm'r*, 5 Cir., 1941, 118 F.2d 1010. The amount received is taxable or nontaxable according to what it represents. If the judgment was for an amount due under a contract for personal services, a reference in the judgment or the opinion supporting it to the sum recovered as 'in the nature of a bequest' will not change the compensation from taxable income to an exempt bequest. Thus, in order to acquire property by inheritance, a party must bring suit against the estate as an heir. He must participate in the proceeds as an heir.

Id. at 121.

The court further noted that it found "no difference between a contract to compensate for one's personal service in the form of a bequest, and one in

which the contractor agrees to pay for the services during his life." *Id.* at 123 (citing *Ex parte Simons*, 1918, 247 U.S. 231, 38 S.Ct. 497, 62 L.Ed. 1094). Only when services are not required as a condition of payment of the legacy is the property is acquired by bequest and, therefore, excluded from income. *Id.* at 123 (citing *United States v. Merriam*, 263 U.S. 179, 44 S.Ct. 69, 70, 68 L.Ed. 240 (1923)). As Cotnam had not standing as an heir or beneficiary, the judgment represented payment for services rendered. *See Id.*

In fact, Internal Revenue Service Publication 525 now states that "[I]f you receive cash or other property as a bequest for services you performed while the decedent was alive, the value is taxable compensation."

B. Taxation of Payments By Estate

1. General Rule

As a general rule, the payment of a bequest to a beneficiary is not deductible by the estate unless the bequest qualifies for the estate tax marital or charitable deduction. Therefore, characterizing a claim as taking the form of an inheritance, while preserving favorable income tax treatment for the beneficiary under Section 102 of the Internal Revenue Code, will yield no tax benefit to the estate.

2. Exception: Debts

If the payment takes the form of the payment of a debt owed by the decedent to the claimant/beneficiary, the payment of the claim may be deductible as a debt of the decedent. *See* I.R.C. § 2053. For example, in *Bailey v. Commissioner*, 741 F.2d 801 (5th Cir. 1984), when a father died, the son inherited property, but the mother never set up a separate account for the son's benefit and did not acknowledge his inheritance rights. In administering the mother's estate, the son first became aware of his inheritance rights in his father's estate, and the son took a section 2053 deduction as a claim against the mother's estate. The son contended that the amount of this claim was the current value of the property he should have inherited from his father's estate, and that on these facts the Texas courts would impress a constructive trust in his favor. Although the Tax Court found for the government, the Fifth Circuit Court of Appeals reversed, allowing the Section 2053 deduction but remanding for a determination of the current value of the son's inheritance from his father.

Generally, the amount of the deduction is the value of the claim as of the decedent's date of death. The I.R.S. may challenge a deduction based on the amount of the ultimate settlement. *See Estate of Smith v. Comm'r*, 198 F.3d (5th Cir. 1999)(evidence of settlement amount reached after death not admissible to determine date of death value of claim).

3. Exception: Payments to Employees

Section 102(c) of the Code provides that the exclusion from income for bequests does not apply to any amount transferred by or for an employer to or for the benefit of an employee. In the context of settling claims against an estate from an employee or former employee, those claims may be deductible by the estate for income tax purposes under Sections 162 or 212 of the Internal Revenue Code, or for estate tax purposes as a debt of the estate under Section 2053(a)(3). If the liability arose prior to the decedent's death, and would have been deductible by the decedent had it been paid during lifetime, it may constitute a "deduction in respect of a decedent," for which both an income and an estate tax deduction may be permitted. I.R.C. § 691(b).

4. Exception: Administration Expenses

As discussed previously, litigation expenses are commonly deducted as expenses of administration under Internal Revenue Code § 2053(a)(2) if they are actually and necessarily incurred in the proper administration and settlement of a decedent's estate and are allowable under applicable state law. Expenses of administration are not generally deductible when incurred for the individual benefit of heirs, legatees, or devisees. *See Estate of Dutcher v. Comm'r*, 34 T.C. 918 (1960); *Estate of Landers v. Comm'r*, 38 T.C. 828 (1962); *Estate of Baldwin v. Comm'r*, 59 T.C. 654 (1973). Deduction not taken on the death tax returns is generally available as an income tax deduction.

a. Estate Settlements

As previously discussed, the Internal Revenue Code allows a will contestant's fees and expenses to be deducted, *see Sussman v. United States*, 236 F. Supp. 507 (E.D.N.Y. 1962), and the Texas Probate Code allows the attorneys fees of will contestants to be charged to the estate where the contestant is a devisee, legatee, or beneficiary of a will or an alleged will or an administrator with will annexed. *See* TEX. PROB. CODE ANN. § 243 (Vernon 2003). Such allowance is limited to good faith actions based on just cause. *Id.; see also Wick v. Fleming*, 652 S.W.2d 353 (Tex. 1983) (holding that a good faith and just cause finding must be made in the original proceeding); *Alldrige v. Spell*, 774 S.W.2d 707 (Tex. App.–El Paso 1989, no writ) (requiring jury finding of good faith before awarding attorney's fees); *Currie v. Drake*, 550 S.W.2d 736 (Tex. Civ. App. – Dallas 1977, writ ref'd n.r.e.).

But a deduction is not allowed for fees incurred by a beneficiary or heir to establish his or her share of the decedent's estate. *See* I.R.C. § 212. Treasury Regulation 1.212-1(k) provides that:

> (k) Expenses paid or incurred in defending or perfecting title to property, in recovering property (other than investment property and amounts of income which, if and when recovered, must be included in gross income), or in developing or improving property, constitute a part of the cost of the property and are not deductible expenses. Attorneys' fees paid in a suit to quiet title to lands are not deductible; but if the suit is also to collect accrued rents thereon, that portion of such fees is deductible which is properly allocable to the services rendered in collecting such rents. *Expenses paid or incurred in protecting or asserting one's right to property of a decedent as heir or legatee, or as beneficiary under a testamentary trust, are not deductible.*

Treas. Reg. § 1.212-1(k)(emphasis added).

b. Trust Settlements

Depending on the facts and circumstances, a portion of the attorney fees and expenses paid by the trust may be deductible. Treasury Regulation § 1.212 provides as follows:

> (i) Reasonable amounts paid or incurred by the fiduciary of an estate or trust on account of administration expenses, including fiduciaries' fees and expenses of litigation, which are ordinary and necessary in connection with the performance of the duties of administration are deductible under section 212, notwithstanding that the estate or trust is not engaged in a trade or business, except to the extent that such expenses are allocable to the production or collection of tax-exempt income. But see section 642 (g) and the regulations thereunder for disallowance of such deductions to an estate where such items are allowed as a deduction under section 2053 or 2054 in computing the net estate subject to the estate tax.

Treas. Reg. § 1.212-1(i).

Similar to a beneficiary of an estate, expenses paid or incurred by a beneficiary of a trust to protect or assert his or her right to property as beneficiary under a testamentary trust, are not deductible. *See* Treas. Reg. § 1.212-1(k)

C. Non-Pro Rata Distributions

If an estate makes unauthorized non-pro rata distributions of property to its beneficiaries, the Internal Revenue Service has ruled that the distributions are equivalent to a pro rata distribution of undivided interests in the property, followed by an exchange of interests by the beneficiaries. This deemed exchange will presumably be taxable to both beneficiaries to the extent that values differ from basis. Rev. Rul. 69-486, 1969-2 C.B. 159. For example, suppose an estate passes equally to A and B, and contains two assets, stock and a farm. At the date of death, the stock was worth $100,000 and the farm worth $110,000. At the date of distribution, each is worth $120,000. If the executor gives the stock to A and the farm to B *and if the will fails to authorize non-pro rata distributions,* the Internal Revenue Service takes the view that A and B each received one-half of each asset from the estate. A then "sold" his interest in the farm (with a basis of $55,000) for stock worth $60,000, resulting in a $5,000 gain to A. Likewise, B "sold" his interest in the stock (with a basis of $50,000) for a one-half interest in the farm worth $60,000, resulting in a $10,000 gain to B. To avoid this result, the settlement agreement or other governing instrument should expressly authorize non-pro rata distributions.

D. Income Tax Basis In Property Received Under Settlement

1. General Rule

Most practitioners describing the impact of death upon basis use a kind of short-hand by saying that assets get a "step-up" in basis at death. In inflationary times, this oversimplification is often accurate. However, it is important to remember that the basis of an asset may be stepped up or down. For most assets, the original cost basis in the hands of the decedent is simply irrelevant. It is equally important to remember that the basis adjustment rule is subject to some important exceptions. Stated generally, a decedent's estate receives a new cost basis in its assets equal to the fair market value of the property at the appropriate valuation date. I.R.C. § 1014. In most cases, the basis is the date-of-death value of the property. However, if the alternate valuation date has been validly elected, that value fixes the cost basis of the estate's assets. I.R.C. § 1014(a)(3).

The basis adjustment rule also applies to a decedent's assets held by a revocable trust used as an estate surrogate, since they are deemed to pass from the decedent pursuant to Sections 2036 and 2038 of the Code. The adjustment to the basis of a decedent's assets occurs regardless of whether the estate is large enough to be subject to federal estate tax. Original basis is simply ignored and federal estate tax values are substituted. And, the new cost basis applies not only to the decedent's separate property but also to *both halves* of the community property owned by a married decedent. I.R.C. § 1014(b)(6).

2. Exception: Income in Respect of A Decedent

There is no specific definition of "income in respect of a decedent," commonly referred to as IRD, in the Internal Revenue Code. Essentially, it consists of income earned by a decedent before death but not recognized until after death. It may be included in the gross income of the decedent's estate or by one or more of the estate beneficiaries at the time the estate or beneficiary, respectively, collects the item of income. An estate is not entitled to an adjusted tax basis on IRD assets includible in a decedent's estate. Likewise, a beneficiary (by will or agreement) is generally not entitled to an adjusted tax basis on IRD assets to be received by the beneficiary. The following are common examples of IRD:

- Dividends declared on stock owned by a decedent that is payable to shareholders of record on a date before the decedent's death but not actually paid until after death. *Estate of Putnam v. Comm'r*, 324 U.S. 393 (1945);
- Death payments made to beneficiaries under an Individual Retirement Account or an exempt deferred compensation plan. *Hess v. Comm'r*, 271 F.2d 104 (3d Cir. 1959), rev'g 31 T.C. 165 (1958);
- Compensation for the decedent's services, including a bonus paid after death, that the employer had no obligation to pay. *Rollert Residuary Trust v. Comm'r*, 752 F.2d 1128 (6th Cir. 1985) aff'g, 80 T.C. 619; *Bausch's Estate v. Comm'r*, 186 F.2d 313 (2nd Cir. 1951); Rev. Rul. 68-124, 1968-1 C.B. 124.
- Renewal commissions owed a deceased life insurance agent. *Findlay v. Comm'r*, 332 F.2d 620 (2nd Cir. 1964); Rev. Rul. 59-162, 1959-1 C.B. 224;
- Amounts recovered by a decedent's estate as damages for the decedent's lost profits. *Estate of Carter v. Comm'r*, 35 T.C. 326 (1960), aff'd, 298 F.2d 192 (8th Cir.) cert. denied 370 U.S. 910 (1962);
- Alimony arrearages owing to a decedent at the time of his or her death and paid after death. *Estate of Narischkine v. Comm'r*, 14 T.C. 1128 (1950), aff'd, 189 F.2d 257 (2nd Cir. 1951);
- Accrued but unreported interest on United States Treasury Series E bonds owned by a decedent at the time of his or her death. *Apkin v. Comm'r*, 86 T.C. 692 (1986);
- Income realized by an estate on nonqualified or nonrestricted stock options owned by decedent at the time of his or her death. Rev. Rul. 53-196, 1953-2 CB 178;
- Insurance reimbursements of previously deducted medical expenses received after the decedent's death. Rev. Rul. 78-292, 1978-2 CB 233;
- Liquidating distributions if the decedent had the right to any liquidation proceeds. *Estate of Bickmeyer v. Comm'r*, 84 T.C. 170 (1985);
- Sales proceeds received after death if: (i) the decedent had, before his or her death, entered into a legally binding contract regarding the sale item; (ii) the decedent had performed all of the substantive acts required by the terms of the contract; (iii) on the date of the decedent's death, no economic material contingencies existed that could have disrupted the sale; (iv) the decedent, had he or she lived, received the proceeds of the sale. *Estate of Peterson v. Comm'r*, 74 T.C. 630 (1980) aff'd, 667 F.2d 675 (8th Cir. 1981).

3. Exception: No New Basis for Deathbed Transfers to Decedent

Section 1014(e) of the Code provides a special exception for appreciated property given to a decedent within one year of death, which passes from the decedent back to the donor as a result of the decedent's death. This rule is presumably designed to prevent avaricious taxpayers from transferring property to dying individuals, only to have the property bequeathed back to them with a new cost basis.

4. Considerations In Settlement of Trust Funding Claims

a. Debt Approach

The approach of including the property in the surviving spouse's gross estate and taking a Section 2053 deduction permits a second step-up in basis for all of the assets held in that spouse's name. But, if the bypass trust is funded with property that has appreciated subsequent to the surviving spouse's date of death, his estate will be satisfying a claim against the estate with appreciated property which will be a recognition event for capital gains purposes (measured, however, only by the difference in value from the second spouse's death to the date of funding). Rev. Rul. 74-178, 1974-1 C.B. 196.

b. Constructive Trust Approach

If the constructive trust approach is employed, the assets traceable to the bypass trust are really excludable from the surviving spouse's estate as belonging to the (constructive) bypass trust, they are treated as having passed from the estate of the first

spouse. Basis therefore will depend upon the fair market value at the date of the first spouse's death. I.R.C. § 1014. Since the bypass assets are not included in the estate of the surviving spouse, no second step-up (or down) in basis applies.

Note, if the executor of the surviving spouse's estate settles the claim by now funding a pecuniary bypass bequest with appreciated assets based upon their date-of-distribution value, a substantial capital gain (measured by the difference in value from the first spouse's death to the date of funding) could result. Treas. Reg. § 1.661(a)-2(f)(1).

If this approached is used, the surviving spouse's estate may be below the filing threshold. If no return is filed, but the IRS somehow later is successful in asserting that a return was due and tax owed, the executor of the surviving spouse's estate would be personally liable for estate tax, penalties, and interest until discharged from liability. I.R.C. §§ 2002 and 2204. The statute of limitations for estate and gift tax is three years from the date the return is filed. I.R.C. §6501(a). In addition, if there is an omission on an estate tax return that exceeds 25% of the gross estate, the statute of limitations is extended to six years from the date of filing of the return. I.R.C. §6501(e)(2). However, there is an exception (i.e., there is no statute of limitations) if no return is filed.

Thus, if the bypass trust is funded after the surviving spouse's death, and Form 706 is never filed for that estate, the statute of limitations never begins to run; exposure, theoretically, never ends. If no Form 706 is required because the surviving spouse's estate is less than the filing requirement, but the executor chooses to file a Form 706 anyway, would the executor succeed in tolling the statute of limitations? Would a closing letter for a return that was not required be effective?

If the surviving spouse's estate exceeds the filing threshold, even if the assets traced to the bypass trust are excluded from the estate, (or if the executor simply decides to file a return anyway), how should information about the late funding of the "constructive" bypass trust be disclosed on the Form 706? The Form 706 instructions request attachment of all instruments creating a trust for the benefit of the surviving spouse. Therefore, the first spouse's Will or revocable trust agreement creating the bypass trust should be attached. The Form 706 instructions do not request information regarding the funding of the trust, or even the value of the predeceased spouse's bypass trust at date of the second spouse's death. Obviously, if the "debt" approach is utilized, and the assets of the surviving spouse's estate exceed the filing threshold, and the amount of the debt must be listed. Full disclosure of how the "debt" is computed may be warranted, especially in view of the fact that debts owed to related parties are on the "hit" list of IRS examining attorneys. See IRS ESTATE TAX EXAMINER'S HANDBOOK § (16)33(3), (4).

E. Sale of an Expected Inheritance

In Revenue Ruling 70-60, a daughter sold a partial interest in her expected inheritance from her father, who was living at the time of sale and had made no will. The Internal Revenue Service held that "the entire amount received by the [daughter] for the relinquishment of her right to inherit the interest from her father" was includible under Section 61(a) in her gross income in the year of sale. Rev. Rul 70-60 (1970). It is notable that the Internal Revenue Service Publication 525 provides that the seller of an interest in an expected inheritance from a living person is required to report the entire amount receive in gross income in the year of sale.

F. Sale of an Remainder Interest In A Trust

One settlement technique used in controversies between the income and remainder beneficiaries of a trust involves a "sale" of the interest of one set of beneficiaries to the other. One effect of the sale is to merger the income and remainder interests in the hands of the "buyer," thereby cause the trust to terminate pursuant to 112.034(b) of the Texas Trust Code. For example, if a decedent's Will established a QTIP trust for a second spouse, with the remainder interest passing to children from a first marriage, the surviving spouse might purchase the remainder interest from the children, causing the trust to merge (subject to any spendthrift provisions) and removing the sales price from the estate of the surviving spouse.

In a Field Service Advisory issued on July 6, 1995, the Internal Revenue Service addressed a request for advice regarding the proper income tax treatment of petitioners' assignment of a remainder interest in a trust in exchange for the canceling of certain indebtedness. Specifically, the taxpayer inquired whether he was required to recognize taxable income under I.R.C. Section 61 relating to the assignment of an expectant remainder interest in a trust in exchange for the cancellation of indebtedness. The Service advised that "the transfer of the remainder interest was a taxable event resulting in income to the petitioner husband."

It should be noted that in the context of a QTIP trust, the purchase of the remainder interest may be treated as a "disposition" of that interest by the spouse pursuant to Section 2519, and as a result, the spouse may be treated as having made a taxable gift to the children equal to the value of the purchase price. Rev. Rul. 98-8, 1998-1 C.B. 541. Naturally, the gift may be sheltered by the spouse's remaining gift tax exclusion.

B. Life Insurance

1. General Rule

Generally speaking, life insurance proceeds are income tax free to the beneficiary of the policy. I.R.C. 101(a)(1). The acquisition of a policy of life insurance by one party to a dispute on the life of another will normally provide that party with tax free income upon the death of the insured.

2. Exception: Transfer For Value

When an existing policy of insurance is among the assets to be divided upon the settlement of an estate dispute, an important exception to the foregoing rule must be considered. Section 101(a)(2) of the Internal Revenue Code provides, "In the case of a transfer for a valuable consideration, by assignment or otherwise, of a life insurance contract or any interest therein, the amount excluded from gross income . . . shall not exceed an amount equal to the sum of the actual value of such consideration and the premiums and other amounts subsequently paid by the transferee." I.R.C. § 102(a)(2); *see also Tennessee Foundry & Mach. Co. v. Comm'r*, 399 F.2d 156(6th Cir. 1968)(death proceeds subject to income tax when beneficiary/employer received life insurance policy purchased with funds embezzled by employee and received in settlement of beneficiary/employer's claims of embezzlement).

The foregoing provisions do not apply in the case of a transfer to the insured, to a partner of the insured, to a partnership in which the insured is a partner, or to a corporation in which the insured is a shareholder or officer. Under this provision, the IRS might take the position that insurance transferred to a party other than the insured is a "transfer for a valuable consideration (i.e., the value of the settlement attributable to the insurance policy—presumably its then cash value), and seek to tax the beneficiary on any excess proceeds received upon the insured's death.

H. Taxation of Other Settlements

1. Tort Actual Damages

Prior to the enactment of the Small Business Job Protection Act of 1996 ("the 1996 Act"), Internal Revenue Code Section 104(a) provided a global exclusion of any damages received (whether by suit or agreement) on account of personal injury or sickness. *See* I.R.C. 11 U.S.C. § 104(a)(1)-(2). The exclusion from income was interpreted to include personal injuries whether or not the injury related to actual physical sickness or injury. Thus, certain courts have held that damage awards relating to injury to reputation or employment discrimination were excluded from the recipient's gross income. Additionally, the courts were split on the issue whether the exclusion applied to punitive damages awarded in a case involving personal injury related to actual physical injury or sickness. *See O'Gilvie v. U.S.*, 66 F.3d 1550 (10th Cir. 1995), aff'd 519 U.S. 79 (1996) (Supreme Court (held punitive damages received in tort suit for personal injuries were not excluded from taxable gross income).

Section 104(a), as amended and currently in effect, now provides:

> (1) Amounts received under workmen's compensation acts as compensation for personal injuries or sickness;
>
> (2) The amounts of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of *personal physical injuries or physical sickness*;
>
> . . .
>
> For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraphs (A) and (B) of Section 213(d)(1)) attributable to emotional distress.

I.R.C. § 104(a)(1)-(2) (emphasis added).

Section 104(a), as amended, applies to amounts received after the date of enactment (August 20, 1996) in taxable years ending after such date. H.R. 3448 § 1605(d)(1). The amendment does not apply to amounts received under a written binding agreement, court decree or mediation award in effect on (or issued on or before) September 13, 1995. H.R. 3448 § 1605(d)(2). Thus, any amounts received subsequent to August 20, 1996, including those resulting from a structured settlement, etc., which relate to an agreement or judgment in existence on September 13, 1995, would continue to be taxed in accordance with prior law.

a. Damages Relating to Non-Physical Injury or Sickness

Damages received on account of non-physical injuries or sickness are includible in a taxpayer's income and subject to income taxes. These include damages based on a claim of employment discrimination or injury to reputation. Further, Section 104(a) now clearly provides that an emotional distress claim made in conjunction with a claim for non-physical injuries will not be treated as a physical injury or sickness. In fact, the legislative history indicates that the amendment was predicated on the belief that these recoveries compensate the claimant

for lost wages or profits and, as such, should be includible in the claimant's taxable income.

b. Damages Relating to Physical Injury or Sickness

Section 104(a), as amended, now limits the income tax exclusion to recoveries "on account of" personal physical injury or sickness. The operative language being "on account of." The Conference Committee Report provides the following explanation:

> The bill provides that the exclusion from gross income only applies to damages received on account of a personal physical injury or physical sickness. If an action has its origin in a physical injury or physical sickness, then all damages (other than punitive damages) that flow there from are treated as payments received on account of physical injury or physical sickness whether or not the recipient of the damages is the injured party. For example, damages (other than punitive damages) received by an individual on account of a claim for loss of consortium due to physical injury or physical sickness of such individual's spouse are excludible from gross income. In addition, damages (other than punitive damages) received on account of a claim for wrongful death continue to be excludible from taxable income as under present law.

House Conference Committee Report 104-586, REVENUE OFFSETS (5) (May 20, 1996).

Note that Section 104(a), as amended, states that for the purposes of Section 104(a)(2) (relating to the exclusion of personal physical injuries or sickness), emotional distress shall not be treated as a physical injury or physical sickness. This language appears to provide that damages recovered for a claimant's emotional distress may be taxable income to the claimant. The legislative history indicates, however, that a recovery for emotional distress "on account of" a physical injury is still excluded from gross income. Specifically, the Conference Committee Report provides that:

> Because all of the damages received on account of physical injury or physical sickness are excludible from gross income, the exclusion from gross income applies to any damages received based on a claim of emotional distress that is attributable to a physical injury or physical sickness.

House Conference Committee Report 104-586, REVENUE OFFSETS (5) (May 20, 1996).

Therefore, based on the legislative history, it appears that all damages (except punitive damages) recovered in a lawsuit that arises from a physical injury or sickness will continue to be excluded from a claimant's gross income. This would include a damage recovery by a claimant who actually suffered physical injury or sickness and any person (such as a spouse, parent, child, etc.) who may recover damages "on account of" the injured claimant's physical injury or sickness. The exclusion extends to recoveries for physical injury or sickness pursuant to Texas' wrongful death and survival statutes. *See* TEX. CIV. PRAC. & REM. CODE Ann. § 71.002, -.004 (cause of action for actual injury arising from an injury that causes an individual's death) (Vernon 2008); *See Id.* § 71.021 (cause of action for personal injury to health).

2. Punitive Damages

As a general rule, any punitive damage recovery will constitute taxable income to the claimant. The legislative history evidences Congress' belief that punitive damages are intended to punish and do not compensate a claimant and are, thus, a windfall to the claimant. This includes punitive damages whether or not they arise from a claim involving physical injury or sickness. An exception is provided for punitive damages recovered in states in which the applicable law provides that *only* punitive damages may be awarded in wrongful death actions. *See* I.R.C. 11 U.S.C. § 104(a).

I. Segregation of Settlement Amounts

When damages are received pursuant to a settlement agreement, "the nature of the claim that was the actual basis for settlement controls whether such damages are excludable" under IRC Section 104(a)(2). *Amos v. C.I.R.*, T.C. Memo. 2003-329, 2003 WL 22839795, (U.S. Tax Ct. 2003)(citing *United States v. Burke*, 504 U.S. 229, 237 (1992)). A determination of the nature of the claims is factual. *See Id.* (citing *Robinson v. Commissioner*, 102 T.C. 116, 126, 1994 WL 26303 (1994), *aff'd. in part, rev'd in part, and remanded on another issue* 70 F.3d 34 (5th Cir.1995); *Seay v. Commissioner*, 58 T.C. 32, 37, 1972 WL 2542 (1972)).

When claims are settled via an agreement, the determination is usually made by reference to the settlement agreement. *See Id.* at *5(citing *Knuckles v. Commissioner*, 349 F.2d 610, 613 (10th Cir.1965), aff'g. T.C. Memo.1964-33; *Robinson v. Commissioner*, *supra*). When the settlement agreement lacks express language stating what the settlement amount was intended to settle, "the intent of the payor is critical to that determination." *Id.* (citing *Knuckles v. Commissioner*, *supra; see also Agar v. Commissioner*, 290 F.2d 283, 284 (2nd Cir. 1961), aff'g. per curiam T .C. Memo.1960-21). And, while the payee's belief may be relevant, the character of the settlement amount ultimately depends on the primary reason of the settling party making the

payment. *Id.* (*citing Agar v. Commissioner, supra; Fono v. Commissioner*, 79 T .C. 680, 696, 1982 WL 11175 (1982), aff'd. without published opinion 749 F.2d 37 (9th Cir.1984).

A determination whether a settlement amount is properly excludable from gross income under section 104(a)(2) "depends on the nature and character of the claim asserted, and not upon the validity of that claim." *Id.* (citing *Bent v. Commissioner*, 87 T.C. 236, 244, 1986 WL 22165 (1986), aff'd. 835 F.2d 67 (3rd Cir.1987); *Glynn v. Commissioner*, 76 T.C. 116, 119, 1981 WL 11320 (1981), aff'd. without published opinion 676 F.2d 682 (1st Cir.1982); *Seay v. Commissioner, supra.*).

For example, in *Amos v. C.I.R.*, the Internal Revenue Service disallowed an income tax exclusion arising from a settlement reached after Dennis Rodman kicked a photographer. The photographer pursued a claim against Rodman for his injuries. Rodman ultimately settled with the photographer and the parties entered into a settlement agreement that included a confidentiality clause and a liquidated damages provision that was equal to the settlement amount. As part of the settlement, the taxpayer agreed that he would not "(1) Defame Mr. Rodman, (2) disclose the existence or the terms of the settlement agreement, (3) publicize facts relating to the incident, or (4) assist in any criminal prosecution against Mr. Rodman with respect to the incident (collectively, the nonphysical injury provisions)." *Id.* at *7. The Internal Revenue Service asserted that all but $1 was includible in the photographer's income. While the Tax Court did not find that the liquidated damages provision to be determinative of the nature of the claims, it did consider all of the claims released and determined that $120,000 was excludable and $80,000 was includable in the photographer's gross income.

VIII. GENERATION SKIPPING TRANSFER TAX CONSIDERATIONS

A. General Application

The impact of the generation skipping transfer tax should be considered before finalizing any settlement involving potential skip persons. Just as bona fide transfers may impact the applicability of the marital or charitable deduction, such transfer may cause the imposition of the generation skipping transfer tax on any property received by a "skip person" as defined by Chapter 13 of the Internal Revenue Code.

B. Modifications May Cause Loss of Exempt Status

Any settlement which is contingent upon a modification of an existing trust that is grandfathered from generation skipping transfer tax should be entered into with great caution. Modification of the trust may cause the trust to lose its exempt status. Thus, the agreement to modify may need to be conditioned on a favorable ruling from the Internal Revenue Service that the modification will not result in a loss of the trust's grandfathered status.

The Tax Reform Act of 1986 provides that the GST tax applies to any generation-skipping transfer occurring after October 22, 1986, the date of enactment. Tax Reform Act of 1986 § 1433(a), Pub. L. No. 99 514 (1986). A special grandfathering rule applies to a trust that was irrevocable before September 26, 1985. All transfers from those trusts are exempt to the extent that distributions are not attributable to additions to the trust after September 26, 1985. Id. at § 1433(b)(2)(A). If an addition to an irrevocable trust was made after September 26, 1985, the original trust corpus will be "grandfathered." An addition to such a grandfathered trust will result in a split of the trust into a "non-Chapter 13 portion" with an inclusion ratio of zero and a "Chapter 13 portion" with an inclusion ratio of 1. Treas. Reg. § 26.2601 1(b)(1)(iv)(A). Later transfers from the trust are deemed to be proportionately distributed from each trust. Id. at (B) and (C).

On December 20, 2000, the IRS issued final regulations designed to identify whether a "modification" to a grandfathered trust will cause it to lose its grandfathered status. The regulations address modifications resulting from (1) the trustee's exercise of a discretionary power to modify the trust granted in the trust instrument; (2) court approved settlements affecting the terms of the trust; (3) judicial construction of exempt trust terms; and (4) other trust modifications. In general, the regulations provide that a court-approved settlement of a bona fide issue regarding the administration of the trust or the construction of terms of the governing instrument will not cause an exempt trust to be subject to loss of its GST exemption if: "(1) The settlement is the product of arm's length negotiations; and (2) The settlement is within the range of reasonable outcomes under the governing instrument and applicable state law addressing the issues resolved by the settlement. A settlement that results in a compromise between the positions of the litigating parties and reflects the parties' assessments of the relative strengths of their positions is a settlement that is within the range of reasonable outcomes." Treas. Reg. § 26.2601 1(b)(1)(iv)(B).

IX. GENERAL SETTLEMENT AND DRAFTING CONSIDERATIONS

A. Parties

1. Generally

Logic dictates that all persons affected by a controversy should be joined as parties in pending

litigation and a resulting settlement. Not all persons, however, have standing to intervene or object to a settlement agreement. A discussion of the parties who should be joined in and/or have standing to challenge the settlement of probate, trust and guardianship litigation follows.

2. Will Contests

a. Necessary Parties

Every person having a "pecuniary" interest in the estate should be joined as a party to the settlement agreement, if possible. This includes:

- a decedent's heirs at law, to the extent a will contest has been or may be filed which would result in the decedent dying intestate, *see Leon v. Keith*, 733 S.W.2d 372 (Tex. App. – Waco 1987, writ ref'd n.r.e.), and
- all persons who are or may be beneficiaries of the estate under a probated or alleged will, see *Manning v. Sammons*, 418 S.W.2d 362, 367 (Tex. Civ. App. – Fort Worth 1967, writ ref'd n.r.e.).

But, it is generally not necessary for beneficiaries of the estate to be made parties to the agreement if their interest will not be affected by it. *See Fore v. McFadden*, 276 S.W.2d 327 (Tex. Civ. App. – Texarkana 1925, writ dis'm). Note, the Texas Attorney General's office should be provide the required notices in any settlement of an estate involving a charity's interest. *See* TEX. PROB. CODE ANN. § 128A (Vernon 2003).

b. Proper Parties

In addition to "necessary" parties, a settling party should consider whether there are any other persons that should be joined as a party to the agreement to avoid a future challenge to the terms of the agreement or the will. Furthermore, a settling fiduciary should consider including all persons whose interest may be affected by the agreement as parties to the agreement or related proceeding to avoid claims against the fiduciary in the future.

All persons who may have a potential claim under a prior will or the heirship statutes should be joined as a party, if possible. If they are not joined as a party, the settling parties should include some mechanism in the agreement to establish the beneficiaries or heirs of the estate. For example, a will should be probate subject to the settlement agreement to preclude an excluded heir from seeking an heirship in the future. Alternatively, an heirship judgment should be entered and the probate of any alleged will denied to avoid a party moving to probate such a will at a later date.

c. No Standing to Contest Settlement

Not every person "interested" in an estate has standing to contest or object to a settlement agreement. Standing is generally contingent on the person having a "pecuniary interest" affected by the probate or defeat of a will. *See In re Estate of Hodges*, 725 S.W.2d 265 (Tex. App. – Amarillo 1986, writ ref'd n.r.e.); *Biddy v. Jones*, 475 S.W.2d 322 (Tex. Civ. App. – Amarillo 1971, no writ); *Logan v. Thomason*, 202 S.W.2d 212 (Tex. 1947). Texas courts here held that the following individuals lack standing to oppose a settlement agreement.

(i) Named Executor

The person named as executor of the estate lacks standing to object to a settlement agreement relating to administration and settlement of an estate. *See In re Estate of Hodges*, 725 S.W.2d at 268 (right to compensation as executor not pecuniary interest in estate); *Biddy*, 475 S.W.2d at 323 (agreement not to probate binding on named executor not party to agreement).

(ii) Temporary Administrator

A temporary administrator of an estate has no justiciable interest in either the admission to or denial of a will to probate. *See Aaronson v. Silver*, 304 S.W.2d 218, 220 (Tex. Civ. App. – Austin 1957, writ ref'd n.r.e.).

(iii) Creditor

A creditor lacks standing if the payment of his claim is not affected by the settlement of the contest to the admission or denial of the probate of the will. *See Logan*, 202 S.W.2d at 212. But, a creditor may have standing to contest the suitability of a proposed personal representative. *See* TEX. PROB. CODE ANN. §§ 3(r), 10 (Vernon 2003); *see also, Allison v. F.D.I.C.*, 861 S.W.2d 7, 10 (Tex.App.—El Paso 1993, writ dism'd by agreement).

3. Trust Suits

a. Necessary Parties

Section 115.011(b) of the Texas Trust Code provides that the following are necessary parties to a trust suit:

- a beneficiary on whose act or obligation the action is predicated;
- a person designated by name in the instrument creating the trust; and
- a person actually receiving distributions from the trust estate at the time the action is filed.

See TEX. PROP. CODE ANN. § 115.011(b) (Vernon 2007).

If a necessary party is a charity, notice must also be given to the Texas Attorney General's office. *Id.* at § 115.011(c). To avoid future enforcement issues, all these persons should be parties to a settlement agreement relating to a trust.

Furthermore, if the proceeding involves a declaratory judgment involving the trust, all persons who have an interest that would be affected by the outcome must be joined as a party. *See* TEX. CIV. PRAC. & REM. CODE ANN. § 37.006 (a) (Vernon 2008). This may include successor trustees and contingent beneficiaries.

b. Proper Parties

In addition to all necessary parties required by the Texas Trust Code, consideration should be given to join any other persons who may have an interest in the proceeding. Additional parties may include:

- Born or ascertainable contingent beneficiaries designed by a class (such as children or grandchildren); and
- Successor trustees.

Contingent beneficiaries designated by a class are not necessary parties to a trust suit, however, they may have standing to challenge the agreement to the extent it affects his or her contingent interest. *See* TEX. PROP. CODE ANN. § 115.011(b) (Vernon 2007) (contingent beneficiaries designated by class not necessary parties to trust suit); *see also Musick v. Reynolds*, 798 S.W.2d 626 (Tex.App.–Eastland 1990, writ denied) (trust can be modified without consent of unascertained beneficiary of trust). The decision to join contingent beneficiaries is a judgment call based on the disputed issues, effect of the agreement and the comfort level sought. Successor trustees should also be joined to avoid a future claim that they hold the claims of the trust and that a settlement with a beneficiary does not bind the successor trustee. *See* discussion *supra.*

c. Minors, Unborn or Unascertained Beneficiaries

Until September 1, 1999, it was more difficult to enter into a binding settlement with minors or unborn or unascertained beneficiaries because the doctrine of virtual representation was limited to judicial proceedings. This was necessary because the Texas Trust Code Section 115.013 of provides that unborn and unascertained beneficiaries may be virtually represented by another party having a substantially identical interest in the proceeding. *See* TEX. PROP. CODE ANN. § 115.013(c)(4) (Vernon 2007). Furthermore, an enforceable settlement with a next friend generally requires court approval. *See* TEX. R. CIV. P. 44; *see also Byrd v. Woodruff*, 891 S.W.2d 689 (Tex. App.--Dallas 1994, writ dism'd by agree.).

Thus, parties to a proposed settlement agreement involving unborn or unascertained beneficiaries were often forced to initiate a "friendly" suit (assuming a lawsuit is not currently pending) to approve the proposed settlement. *See Robinson v. Nat'l Cash Register Co.*, 808 F.2d 1119 (5th Cir. 1987) (no party may be bound by judgment if non-party's and party's interest is so closely aligned that party is non-party's "virtual representative").

Effective September 1, 1999, parties can invoke the virtual representation doctrine outside a court proceeding. Provided the agreement does not purport to modify or terminate a trust, parties can enter into out-of-court agreements, including fiduciary releases and other agreements, and bind minor, unborn or unascertained beneficiaries. Section 114.032 provides that "written agreement between a trustee and a beneficiary, including a release, consent, or other agreement relating to a trustee's duty, power, responsibility, restriction, or liability, is final and binding on the beneficiary and any person represented by a beneficiary" if:

- the instrument is signed by the beneficiary;
- the beneficiary has legal capacity to sign the instrument; and
- the beneficiary has full knowledge of the circumstances surrounding the agreement.

See TEX. PROP. CODE ANN. § 114.032 (Vernon 2007).

Furthermore, an agreement with a beneficiary who has the power to revoke the trust or a general power of appointment is final and binding on any person who takes under the power of appointment or who takes in default if the power of appointment is not executed. *See* TEX. PROP. CODE ANN. § 114.032 (Vernon 2007).

As to minors, a written agreement is final and binding when all of the following provisions are meet:

- the minor's parent, including a parent who is also a trust beneficiary, signs the instrument on behalf of the minor;
- no conflict of interest exists; and
- no guardian, including a guardian ad litem, has been appointed to act on behalf of the minor.

See TEX. PROP. CODE ANN. § 114.032 (Vernon 2007).

An agreement will be binding on an unborn or unascertained beneficiary when a beneficiary who has an interest substantially identical to the interest of the unborn or unascertained beneficiary signs the instrument; provided the unborn or unascertained beneficiary has a substantially identical interest with a trust beneficiary from whom the unborn or unascertained beneficiary descends. Therefore, these beneficiaries will only be bound if there is no conflict between the virtual representative and the beneficiary. *See* TEX. PROB. CODE ANN. § 114.032 (Vernon 2007).

d. No Standing

There are certain cases in which the named and other beneficiaries of a trust lack standing to intervene in the pending litigation or any resulting settlement. These include disputes between the trustee and a third party. On point is the decision of *Davis v. Ward*, 905 S.W.2d 446 (Tex. App. – Amarillo 1992, writ denied). In *Davis*, a trustee beneficiary attempted to intervene in litigation brought by the current trustee against the former trustee for breach of fiduciary duty, fraud and conversion. The parties ultimately entered into a settlement agreement under which the defendants would convey assets to the trust. A motion to approve settlement was filed with the court. A trust beneficiary intervened in the litigation and opposed the motion to approve settlement. The trial court held that the beneficiary had no cause of action or standing in the proceeding and the trustee alone had authority to enter into the settlement and the beneficiary is bound by the trustee's actions. *See Id.* at 448; *see also Cogdell v. Fort Worth Nat'l Bank*, 544 S.W.2d 825 (Tex. App. – Eastland 1977, writ ref'd n.r.e.) (beneficiary of testamentary trust lacks standing to oppose settlement between trustee and executor of estate).

4. Guardianships

Unlike probate and trust litigation which may involve a number of parties and interests, the only interest at issue in guardianship litigation is that of the ward or proposed ward. Thus, the only necessary parties are the ward or proposed ward and the persons who have entered an appearance in the guardianship litigation. In the event a guardian ad litem has been appointed, he or she should also be included in any negotiations and resulting settlement. With regard to a ward's attorney ad litem, they should be kept informed of any proposed settlement but should generally not be a party to it.

5. Ad Litems

When a settlement is reached in conjunction with a judicial proceeding, the parties should consider whether it would be advisable to request the appointment of an ad litem to represent the interests of a minor, an incapacitated, unborn, or unascertained person, or person whose identity or address is unknown, when such person's interest is not otherwise adequately represented. *See* TEX. PROB. CODE ANN. § 34A (Vernon 2003) (attorney ad litem can be appointed in probate proceeding); TEX. PROP. CODE ANN. § 115.014(b) (Vernon 2007) (guardian ad litem can be appointed in probate proceeding); T.R.C.P. 173 (guardian ad litem can be appointed for person without guardian in civil proceeding).

Often, the appointment is not necessary as another beneficiary can virtually represent the interest or a minor can be represented by his or her parent (provided the parent is not a beneficiary of the trust or does not have a conflict of interest). However, when a potential conflict exists, the party should move for the appointment of a guardian ad litem or attorney ad litem (depending on the type of case involved) as soon as possible and the ad litem should be a party to any settlement agreement. *See* discussion *supra.*

B. Identifying Parties In Agreement

1. Define Parties

The agreement should clearly identify the parties to the agreement. *See* discussion *supra*. This includes both (i) the parties releasing claims and (ii) those parties and/or persons being released. It is preferable to include language in the beginning of the agreement identifying and defining each party and the capacity in which the party is entering into the agreement. For example, the agreement may begin with the following provision:

> This Family Settlement and Mutual Release Agreement is entered into by and among the following: (i) A ("A"); (ii) B ("B"); (iii) C ("C"); (iv) D ("D"); (v) E, Individually, as Independent Executrix of the Estate of F, Deceased, as Trustee of the F Testamentary Trust, as Trustee of the G Irrevocable Trust and as Attorney-in-Fact for G (collectively referred to as "E"); and (vi) H, Temporary Guardian Pending Contest of the Person and Estate of G, an Alleged Incapacitated Person (collectively referred to as "H"). In this Agreement, the term "Parties" shall refer collectively to A, B, C, D, E, and H, and the term "Party" shall refer to each of them severally.

Although often subject to attack, minors or contingent beneficiaries may be represented by a parent or next friend. For example, the agreement may provide that:

> The term "Parties" shall mean A, B, C, and D, individually and as next friend of her children, X and Y, their Successors, plus those minor, unborn, unascertained, and contingent beneficiaries of Trust, who are legally and virtually represented by A, B, C, and D, individually and as next friend of X and Y, pursuant to the common law of the State of Texas and the terms of the Texas Family Code and Texas Trust Code.

2. Identify and Define Persons and Entities Releasing

Parties to litigation and non-parties involved in litigation may release claims, but must have capacity and authority to do so. *See In Interest of JTH, a child*,

630 S.W.2d 473, 477 (Tex. App.–San Antonio 1982, no writ). Defense counsel may request persons with potential causes of action to release such claims, even if such persons are not parties to the litigation and have not as yet asserted any claim. For example, in personal injury litigation, spouses could relinquish rights of recovery for loss of consortium.

If there is no spouse, one or more parties may request warranty language. For example:

> X warrants that there is no existing spouse of X with any potential claim for damages relating to the Litigation, and does hereby agree to indemnify and hold harmless the person or persons released herein from any claims for damages relating to the Litigation that might be asserted by any person claiming to be X's spouse.

3. Identify and Define Persons and Entities Being Released

Similarly, the parties may release any non-party and generally should release a party's predecessor, successors and affiliates. This precludes a settling party from bringing future litigation against related persons and entities for claims arising out of the same matter. This also prevents a party from becoming an involuntary party to a future claim for contribution by such third parties.

A release only releases and discharges those persons and/or entities clearly identified in the release instrument. *See Angus Chem. Co. v. I.M.C. Fertilizer, Inc.*, 939 S.W.2d 138, 139 (Tex. 1997) (tortfeasor's release did not include his insured). It is generally preferable to list or name each person or entity being released, but a party may be released if the instrument contains sufficient language for a "stranger" to determine such person or entity or class of persons or entities being released. *See Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414, 419 (Tex. 1994) (release of "any other corporations... responsible" in settlement involving airplane pilot did not include airplane manufacturer); *see also, Knutson v. Morton Foods, Inc.*, 603 S.W.2d 805, 806 (Tex. 1980) (release of employee did not release employer).

This can be accomplished by specifically defining and including a party's predecessors, successors and affiliates. Sample definitions for each follow:

(a) The term "Predecessor(s)" shall refer to any person or entity serving prior in time as a fiduciary to the fiduciary in question. For example, A Bank is the Predecessor to B Bank with respect to the X Trusts.

(b) The term "Successor(s)" shall refer to the heirs, devisees, descendants, legatees, executors, administrators, trustees, attorneys-in-fact, appointees under any power of appointment, guardians, conservators, personal representatives, assigns, successor trustees, successors by reason of a merger, acquisition or governmental action, and any Successors of a Successor.

(c) The term "Affiliates" of the person or entity designated shall mean such person's or entity's employees, directors, officers, shareholders, children, descendants, spouse (including a former or future spouse), assigns, agents (including, without limitation, attorneys, accountants, and investment advisors), trustees, legal representatives, and all general and limited partnerships of which the person or entity is a partner, firms or corporations or any other entities directly or indirectly controlling such entity or directly or indirectly controlled by such person or entity. It is provided, however, that M and N are deemed under this Release and Indemnity Agreement NOT to be Affiliates of Bank, its Predecessors, Successors, or Affiliates, and vice versa.

Alternatively, if a party wishes to pursue a cause of action against another party's affiliate, such as an accountant or attorney, the agreement should include language expressly excluding such person or entity from any release. For example, the agreement may provide that:

> Notwithstanding anything in this agreement to the contrary, the parties acknowledge and agree that they are not releasing CPA for services provided to X Trust and nothing in this agreement shall be deemed to constitute a release of CPA in any capacity.

C. Describe Dispute and Scope

1. Generally

The settlement document should contain language describing the dispute and the extent to which the release will apply to the parties, the dispute, and their relationship. The use of broad versus narrow language depends to some degree on whether there will be a continuing relationship. The scope of the dispute, as described, may generally be narrower if the parties have a prior relationship, fiduciary or otherwise, or intend to continue to have some type of relationship in the future.

2. Define Claims

It is recommended that all known claims be specified. *See Victoria Bank and Trust Co. v. Brady*, 811 S.W.2d 931, 938 (Tex. 1991); *Torchia v. Aetna*

Casualty & Surety Co., 814 S.W.2d 219 (Tex. App. – El Paso 1991, no writ).

Parties may also release unknown claims. The release of unknown claims will, however, be narrowly construed and can be challenged because of mutual mistake, or fraud. *See Victoria Bank & Trust Co.*, 814 S.W.2d at 938. The law of contracts controls the interpretation of the release. To avoid a future dispute regarding whether unknown claims were to be released, the draftsmen should include language to prove that the signatories knew the importance of the clause. *But see Morris v. Landoll Corp.*, 822 S.W.2d 653 (Tex. App. – Fort Worth 1991, no writ) (limited application of language purporting to release all claims which are made "the basis of the lawsuit or that could have been asserted therein").

A sample provision defining claims may provide that:

> The term "Claims" shall refer to and include any and all claims, causes of action, debts, demands, actions, costs, expenses, losses, damages, charges, challenges, contests, liabilities, promises, agreements, deceptive practice claims, claims in equity, suits, and all other obligations and liabilities of whatsoever nature KNOWN and UNKNOWN, fixed or contingent, liquidated or unliquidated, anticipated or unanticipated, at law or in equity, for any type of relief or redress, including but not limited to money damages, whether founded on contract, tort (including but not limited to tortious interference with inheritance rights, conversion, fraud, tax issues, undue influence, false representation, conscious indifference, reckless disregard, and/or malicious conduct), fiduciary duty, NEGLIGENCE, gross negligence, intentional infliction of emotional distress, reimbursement, breach of fiduciary duty to disclose material information, indebtedness, FRAUDULENT INDUCEMENT, and any other ground, whether or not asserted, which any person has, may have, or have had against the released and/or indemnified party, now existing or arising in the future, including the claims brought or which could have been brought by, between or among the Parties through the effective date of the Agreement, save and except warranties and representations under this Agreement. THE PARTIES AGREE THAT THE DEFINITION OF "CLAIMS" IS AND SHALL BE AS BROAD AS THE LAW WILL ALLOW.

3. Define Transaction

In certain cases, it is advisable to define the acts or matters being released. This is particularly useful for an executor, trustee and other fiduciaries that are concerned that the act of entering into a settlement agreement may subject them to liability. It also allows the parties to limit a release to the defined transactions. For example, a provision relating to the agreement of a trustee to voluntarily resign and allow the beneficiaries to select a successor trustee may define the transactions being released as follows:

> The term "Transactions" shall mean the following: (i) the administration of the X Trust and the X Trust Estate by Bank as trustee and its Predecessors, including but not limited to the funding, implementing, and investing of the Trust Estate; (ii) any representations by Bank and its Predecessors; (iii) all other acts, transactions, and proceedings (including any failure to act) of Bank and its Predecessor in connection with the X Trust and the X Trust Estate; (iv) the payment of all debts, fees, and expenses from the X Trust and X Trust Estate, including but not limited to the payment of legal or accounting fees relating to Bank's resignation and the appointment of a successor and Bank's administration and trustee fees, transaction charges, and expenses; (v) Bank's agreement to resign as trustee of the X Trust and to enter into this Release and Indemnity Agreement and the appointment by the X Parties of a successor trustee of the X Trust; (vi) the negotiation, execution, delivery, and performance by the parties hereto of the agreements, acts, and transactions contemplated by, described or otherwise relating to this Release and Indemnity Agreement together with all transfers, distributions, agreements, and other transactions contemplated by this Release and Indemnity Agreement; (vii) all other acts, transactions, and proceedings (including any failure to act) of Bank and its Predecessors as trustee of the X Trust or its Affiliates beginning from the inception date of each, respectively, and ending on the later to occur of the date of the appointment and qualification of the respective successor trustees of the X Trust and the complete transfer of the assets of the X Trust Estate to the successor trustee (including but not limited to the negotiation and effectuation of any and all transactions, agreements, settlements, releases, indemnities, judgments, trustee changes, court proceedings, reorganizations, and other matters relating to X Trust or the X Trust Estate which took place or takes place through the consummation of this Release and Indemnity Agreement); and (viii) the distribution by Bank to the successor trustee of the X Trust of the X Trust Estate and the records of the X Trust.

4. Define Damages if Partial Settlement

When the settlement involves a partial settlement in terms of issues or parties, the agreement should clearly provide what claims, issues, parties and damages are intended to be addressed and released in the settlement agreement.

Furthermore, the settling party should carefully consider how the settlement may effect his or her claims against any non-settling parties. Consideration of the one satisfaction rule and the potential application of settlement credits are necessary in order to structure the settlement in the most advantageous manner possible.

With regard to the right of a non-settling defendant to seek a settlement credit, he or she will have the burden to prove their right to a settlement credit and the settlement credit amount. *See Mobil Oil Corporation v. Ellender,* 968 S.W.2d 917, 927 (Tex. 1998); *Oyster Creek Financial Corporation v. Richwood Investments, II., Inc.,* 2004 WL 1794706 (Tex.App.—Houston [1st Dist.] 2004, n.p.h)(not released for publication to date). This burden can be meet by placing the settlement agreement or some evidence of the settlement agreement in the record. *See Id.* When the remaining defendant meets his or her burden, the burden shifts to the "plaintiff to tender a valid settlement agreement allocation the settlement between (1) damages for which the settling and non-settling party are jointly liable, and (2) damages for which only the settling party was liable." *Oyster Creek Financial Corporation,* 2004 WL 1794706 *15 (*citing Crown Life Ins. Co. v. Casteel*, 22 S.W.3d 378, 392 (Tex. 2000)). If the plaintiff cannot satisfy his or her burden, the non-settling defendant is entitled to a credit equal to the full settlement amount. *See Oyster Creek Financial Corporation,* 2004 WL 1794706 *15 (*citing Ellender,* 968 S.W.2d at 928; *Stewart Title Guar. Co. v. Sterling*, 822 S.W.2d 1, 8 (Tex. 1991)).

D. Consideration

1. Generally

Obviously, the settlement document should contain the important element of consideration. A mutual agreement of compromise is itself valuable consideration. *See J. Kahn & Co. v. Clark*, 178 F.2d 111, 114 (5th Cir. 1949); *see Murtagh v. University Computing Co.*, 490 F.2d 810, 815 (5th Cir. 1974) *cert. denied*, 419 U.S. 835, 95 S.Ct. 62 (1975); *Schuh v. Schuh*, 453 S.W.2d 203, 204 (Tex. Civ. App. – Dallas 1960, no writ) (the settlement of contested lawsuit is sufficient consideration to support compromise settlement agreement). Release of rights and avoidance of expense and annoyance of the suit is valid consideration.

Mere inadequacy of consideration is not sufficient to destroy the effect of a release. *See Tobbon v. State Farm Mut. Auto. Ins. Co.*, 616 S.W.2d 243, 245 (Tex. Civ. App. – San Antonio 11981, writ ref'd n.r.e.); *Slade v. Phelps*, 446 S.W.2d 931, 933 (Tex. Civ. App. – Tyler 1969, on writ); *Hayes v. Roux Laboratories, Inc.*, 443 S.W.2d 621, 622 (Tex. Civ. App. – Eastland 1969, no writ). If, however, the agreement totally lacks consideration, the court will not enforce the agreement. *See Southwestern Fire & Cas. Co. v. Atkins*, 346 S.W.2d 892, 897 (Tex. Civ. App. – Houston 1961, no writ).

While one consideration can generally support the release of more than one claim (*Torchia v. Aetna Casualty & Surety Co.*, 804 S.W.2d 219, 223 (Tex. App. – El Paso 1991, writ denied), the release of two or more *liquidated* claims may require separate consideration for each claim. *See Hallmark v. United Fidelity Life Ins. Co.*, 286 S.W.2d 133 (Tex. 1956).

2. Consideration Underlying Settlement Agreement

Avoiding a contest is sufficient consideration. It is not necessary to show that the perceived grounds for contest would actually be effective. *See Fore v. McFadden*, 276 S.W.2d 327 (Tex. Civ. App. – Texarkana 1925, writ dism'd); *Brown v. Burke*, 26 S.W.2d 415 (Tex. Civ. App. – Waco 1930, no writ). In *Stringfellow v. Early*, 40 S.W.2d 871 (Tex. Civ. App. 1897, no writ), the court also determined that sufficient consideration exists when there is a relinquishment of the right to seek probate of the will and where the respective portions of the estate passing to each beneficiary under the will are equitable.

E. Choice of Law

Parties may contractually agree to a choice of law. For example, the agreement could provide that:

> [this] entire agreement shall be governed by, construed, and interpreted and the rights of the parties determined in accordance with the law of the state of Texas, and shall be enforced in Harris County, Texas.

See Duncan v. Cessna, 665 S.W.2d 414, 421 (Tex. 1984); *Cook v. Frazier*, 765 S.W.2d 546, 549 (Tex. App. – Fort Worth 1989, no writ).

The parties' right to choose what jurisdiction's laws will apply is not unfettered. The parties must select the law of a jurisdiction that has some relationship to the parties and the agreement. *See DeSantis v. Wackerhut Corp.*, 793 S.W.2d 670 (Tex. 1990). Thus, it is unlikely the parties could agree to interpret the will of a Texas resident according to another state's laws. In determining whether to recognize a choice of law clause, the court must determine whether a state has a more significant relationship to the parties' particular substantive issue than the state selected. *Id*. at 678; *see also Duncan v. Cessna*, 665 S.W.2d at 421. If any element of the

execution of a contract occurs in Texas, and a party to the contract is an individual Texas resident or a Texas corporation or association, or has its principal place of business in Texas, then a choice of law provision providing for application of a different state's law may not be recognized, and enforceability of the provision will be determined under Texas laws. *Id*. at 681.

F. Releases

1. Generally

The release is one of the most important aspects of a settlement agreement. The release should be carefully drafted to ensure it is neither too broad nor too narrow, depending on the facts of the case. In general, a release will only discharge those persons specifically named. *See Duncan v. Cessna*, 665 S.W.2d 414, 419 (Tex. 1984); *rev'd on other grounds*; *Smithson v. Cessna Aircraft Co*., 665 S.W.2d 439 (Tex. 1984); *McMillan v. Klingensmith*, 467 S.W.2d 193, 196 (Tex. 1971). All known and identifiable parties being released must be specifically identified. *See* discussion *supra*.

2. Defined Claims and Matters Released

When the agreement limits or previously defines the claims and matters being released, the release provisions should rely on those definitions and utilize the defined terms. For example,

> Upon full and final performance of his obligations under this Settlement Agreement, C and the then acting personal representative of the estate shall mutually release each other and discharge each other from the claims to the Decedent's Estate, save and except for the obligations under this Settlement Agreement.

Alternatively, known claims should be specifically described in the release provisions and these provisions should expressly address whether *unknown* claims are being released. *See Memorial Med. Ctr. v. Keszler*, 943 S.W.2d 433, 435 (Tex. 1997). In *Memorial*, the Texas Supreme Court held that the release of all claims "relating to [plaintiff's] relationship with" the defendant included all existing claims whether known or unknown. *Id*. at 438. The Court held that the language of the release was sufficient to include unknown claims. *Id*. Likewise, in the recent decision of *Stark v. Benckenstein*, 156 S.W.3d 112 (Tex.App.—Beaumont 2004, no pet.), the appellate court upheld a release that specifically provided for the release of unknown claims in conjunction with a disclaimer of reliance. *See* discussion *infra.*

Note that, as previously discussed, release provisions are likely to be narrowly construed and can be subject to challenge because of mutual mistake, fraud, or failure by the fiduciary to disclose. *See Victoria Bank & Trust Co. v. Brady*, 811 S.W.2d 931, 938 (Tex. 1991); *see also Stark v. Benckenstein*, 156 S.W.3d at 123.

Thus, the release terms should attempt to set out all known claims being released and specify whether unknown or future claims are intended to be included. The following is a sample release for a will contest or estate settlement:

> Upon full and final performance of the obligations to C under this Settlement Agreement, each Party, for themselves and their lineal descendants, does hereby forever release and discharge A, Individually and in all capacities, B, Individually and in all capacities, the Decedent's Estate, their respective heirs, personal representatives, executors, affiliates, officers, directors, partners, administrators, successors, agents, attorneys, and assigns [or use defined predecessors, successors, and affiliates] of and from any and any and all claims, causes of action, debts, demands, actions, costs, expenses, losses, damages, charges, challenges, contests, liabilities, promises, agreements, deceptive practice claims, claims in equity, suits, and all other obligations and liabilities of whatsoever nature KNOWN and UNKNOWN, fixed or contingent, liquidated or unliquidated, anticipated or unanticipated, at law or in equity, for any type of relief or redress, including but not limited to negligence, gross negligence, FRAUDULENT INDUCEMENT, intentional infliction of emotional distress, tortious interference with inheritance rights, tortious interference with contracts, tortious interference with business relations, physical, mental, or emotional distress, improvement of Decedent's separate property through the expenditure of separate or community funds, money or time, talent, or labor of either of them, the enhancement of Decedent's separate property, the advancement of separate or community funds to reduce separate property debt, improvements to Decedent's separate property, any gifts made by Decedent, the Decedent, unjust enrichment, the administration of Decedent's Estate, breach of fiduciary duty to disclose material information, all claims which were or could have been made in currently pending litigation, fraudulent concealment, rights of reimbursement, exempt property, fraud, fraud on the community, theft, undue influence, misappropriation, breach of fiduciary duty, family allowance, and any other statutory rights and demands and any and all other causes of action of any kind and/or character, whether KNOWN or UNKNOWN, fixed or contingent,

> liquidated or unliquidated, whether or not asserted, arising out of or any way connected with any act, omission or event related to the Decedent's Estate, and/or the parties hereto, save and except for the representations, warrants, obligations under this Settlement Agreement.

When a continuing fiduciary relationship is contemplated, the release should be narrowed to avoid releasing future rights or actions relating to the trust or estate.

3. Claims Against Counsel

The settlement agreement may also provide for the release of any potential claims relating to the handling of plaintiff's claims:

> The parties further expressly agreed that their settlement extends to all claims, demands, and causes of action, which they may have now or in the future, arising out of the manner in which [defendant] and its counsel, handled, settled, or defended any of the [plaintiff's] claims under the [applicable statute].

See Torchia, 814 S.W.2d at 222.

G. Indemnities

1. Generally

Indemnity serves as protection against liability on cross-actions, liens, and other potential claims by third parties, and is an important factor in facilitating and/or permitting a full or partial settlement of litigation. In some instances, defendants would be imprudent to settle without the protection of an indemnity agreement.

Parties drafting and relying on indemnification clauses should bear in mind that such clauses are construed strictly against an indemnitee. Failure to draft clear indemnification, duty to defend and hold harmless clauses can result in unanticipated liability for the indemnitee.

A settling party should attempt to identify and include any third parties who could bring claims against him, her or it. Indemnities are a viable option when the consenting party is economically solvent and appears likely to remain that way. In these cases, the party may be willing to rely upon a consenting or releasing party's agreement to indemnify the party for any claims brought by any other person or entity (including minor or unborn beneficiaries) against a personal representative or trustee for the act or omission. Because an indemnity is only as good as the economic worth of the party making the indemnity, and because the party may die or circumstances may change, the indemnified party may be unlikely to be willing to rely on any indemnity in circumstances in which the dollars involved are large or there is considerable risk of litigation. Nonetheless, for many common transactions (the resignation of a trustee without final settlement of accounts, the investment or retention of certain assets, entering into settlement agreements, leases, or other transactions) a common practical solution is an indemnity.

The most concerning source of third party claims is federal and state agencies. Thus, parties should attempt to include indemnification provisions to guard against claims by the Internal Revenue Service and the Environmental Protection Agency, or similar agencies.

2. Tax Indemnity

An indemnity serves as protection against liability on cross-actions, liens, and other potential claims by third parties, and is an important factor in facilitating and/or permitting a full or partial settlement of litigation. In some instances, defendants would be imprudent to settle without the protection of an indemnity agreement, particularly if the future assessment of taxes may be an issue.

The tax liability issue principally arises in settlements involving decedent's estates. A personal representative has a duty to pay death taxes when due. *See* I.R.C. § 2002. This includes taxes attributable to non-probate assets. *See* Treas. Reg. § 20.2002-1. A personal representative is also responsible for preparing and filing the death tax return, if necessary. Certain other persons may also be subjected to personal liability for the payment of any unpaid death taxes to the extent of the value of the property received. Internal Revenue Code Section 6324 imposes personal liability on a decedent's spouse, transferees, trustees, surviving tenants, holders of appointed properties, insurance beneficiaries and others who receive or hold estate assets.

Furthermore, the government has priority to be paid debts owed to it before other debts or expenses of the estate. *See* 31 U.S.C. 3713 (priority of government debts). Taxes are debts due the government. *See Price v. U.S.*, 269 U.S. 492 (1926). The obligation to pay taxes includes both known and unknown income, gift and death taxes. The distribution of a beneficiary's interest in an estate before the payment of any death or other taxes may subject the personal representative and the beneficiary to liability. *See Leuthesser v. Comm'r.*, 18 T.C. 1112 (1952); *Posey v. Comm'r.*, 10 T.C.M. 383 (1951); *but see Schwartz v. Comm'r.*, 560 F.2d 311 (8th Cir. 1977) (executor's personal liability limited to distributions made after estate became insolvent).

Thus, when distributing estate assets, both the personal representative and distributee should address such person's tax responsibilities and protections. For example, the agreement may include the following indemnity:

> A, individually and as successor personal representative of Decedent's Estate and her Successors, B, C, and D hereby agree to INDEMNIFY, DEFEND and HOLD HARMLESS E, and her Affiliates and Successors, from any and all liability, transferor, transferee or otherwise, (i) relating to her serving as personal representative of Decedent's Estate or A's appointment as the successor representative of Decedent's Estate, including any and all past, current or future federal or state income gift or death taxes, and any related interest and penalties which may be claimed, or assessed, relating to Decedent's Estate, (ii) relating to any and all past, current or future federal or state income, gift or death taxes, including any interest, and penalties, imposed by reason of the distributions provided for in this Agreement, and (iii) arising from all claims, costs, expenses, including but not limited to attorneys fees and expenses, accountant fees and expenses, experts, litigation costs and bond premiums, relating to any attempt by the Internal Revenue Service or other persons or entities to assess, collect or enforce any claims, demands, assessments or judgments against E, or her Affiliates or Successors, for past, current or future federal or state income, gift or estate taxes, and any related penalties and interest.

Parties drafting and relying on indemnification clauses should bear in mind that such clauses are construed strictly against an indemnitee. Failure to draft clear indemnification, duty to defend and hold harmless clauses can result in unanticipated liability for the indemnitee.

3. Environmental Indemnity

Courts have found that the intent to transfer Comprehensive Environmental Response Compensation and Liability Act ("CERCLA") liability and Texas Superfund equivalent liability must be explicit or clearly intended as evidenced by the language of the clause. The parties covered by the clause, the types of liabilities covered, triggering events, the form and timing of notification under the clause and the scope of any required cleanup should be expressly stated in the clause.

Although contractual indemnifications never completely eliminate the possibility of financial (and possibly personal) ruin, they can significantly minimize the risk as between the parties to a contract. One of the overriding purposes behind CERCLA is to ensure that all hazardous materials sites are remediated by the persons responsible for the contamination. Thus, CERCLA provides that indemnifications, hold harmless agreements or similar agreements between potentially responsible parties are not barred. Suits for contribution or subrogation claims also are not barred. Regardless, however, of any private contractual arrangements in this regard, there can be no agreement or conveyance to transfer liability sufficient to operate as a bar to the government's claims under CERCLA.

To be given proper interpretation and effect, the essential elements of an indemnification provision must be expressed clearly, rather than being left to the unstated or assumed intent of the parties. If a contract is silent as to environmental indemnification, it may lead to the interpretation that the parties intended common law to govern. Then, the various environmental laws, which impose the full complement of remedial actions, financial responsibilities and possible penalties, would be applied accordingly.

One cautionary note bears repeating. Regardless of the terms and conditions contracting parties may agree on among themselves, an environmental indemnification is valid only as it exists between those parties. In practice, it is only as good as the indemnitor's pocket is deep. Further, indemnification between contracting parties may not bar a suit for contribution between parties who are actual contributors to the environmental problems.

H. Future Disputes

1. Generally

While generally not held to be a material term, it is advisable to include a mechanism to resolve future disputes relating to the settlement agreement.

2. Notice of Default and Time to Cure

At a minimum, it is advisable to include a provision that requires each party to notify an alleged defaulting party of a claimed default or breach of the settlement agreement, and provide a reasonable time to cure the default. Such notice should be made a condition precedent to seeking legal fees and expenses for breach of contract. As with all notices, the agreement should provide who should receive the notice and the means of notification, i.e., certified mail, facsimile, etc.

3. Mediation

Many disputes, even post settlement, are the result of lack of communication and frustration. Just as mediation often results in the initial resolution of a dispute, so may it resolve post settlement disputes in a cost effective manner. It is suggested that the parties include a mandatory post settlement mediation provision in the settlement agreement. The agreement may provide that in the event a dispute arises between the parties relating the terms and conditions of the

settlement, they will agree to attend mediation and attempt to resolve such disputes before initiating other legal action. There should also be, however, a stipulated time frame in which the other party agrees to attend mediation or their right to enforce such a provision will deemed waived.

If possible, the parties should pre-select the mediator to avoid the usual issues involved in selecting a mediator. Also, the agreement should provide how the parties will pay for mediation: equally or agree that mediator or third party will have the power to assess costs as between the parties as the circumstances warrant.

4. Arbitration

As with any agreement, the parties can agree that any future disputes will be submitted to arbitration. Arbitration continues to be the increasing alternative forum of choice in which to settle disputes – even those relating to an existing settlement agreement. To be binding, parties must contractually agree to submit their disputes to arbitration in lieu of, or in addition to, other remedies available under Texas law.

If arbitration is desired, the arbitration provision should expressly address the matters that may be submitted to arbitration, the process of arbitration, who shall pay the arbitration fees, and whether there are any specific requirements as to the proposed arbitrators, such as board certified lawyers, etc.

For example, the following provision allowed either side to compel arbitration:

> Any disputes relating to the terms of this Agreement will be decided by Judge _____ by motion submitted by any Party and, if requested, oral argument; provided, in the interests of time any Party may request that [Name of Arbiter] arbitrate such disputes on a binding basis; provided, the non-prevailing Party (as determined by [Name of Arbiter]) shall pay [Name of Arbiter]'s fees and expenses. Any Party wishing to submit an issue to [Name of Arbiter] for arbitration shall provide written notice of the requested arbitration or request to all other Parties and [Name of Arbiter]. The written notice of arbitration shall provide a brief description of the nature of the dispute and the resolution sought by the requesting Party. The non-requesting Party shall have three business days to either agree to the resolution sought by the requesting Party or state their objection to the resolution requested. If an agreement is not reached by the Parties within three (3) business days of the submission of the non-requesting Party's response, [Name of Arbiter] shall arbitrate the dispute pursuant to the Texas Arbitration Act. The Party or Parties prevailing in an arbitration proceeding herein or in a legal proceeding brought in a court of competent jurisdiction to enforce or preserve the rights awarded pursuant to an arbitration proceeding herein, including all appeals, shall be entitled to recover from the non-prevailing Parties all costs and expenses incurred by the prevailing Parties with respect to all of the proceedings, including reasonable attorney's fees. The decision of the arbitrator shall be final as between the Parties and may be enforced or preserved upon application to any court of competent jurisdiction.

5. Waiver of Right to Jury Trial

If arbitration is not selected, another alternative to reduced future litigation costs is to insist that all parties waive his or her right to seek a jury trial on any issues relating to the settlement agreement. In *Prudential Insurance Co. of America and Four Partners L.L.C.*, 148 S.W.3d 124 (Tex. 2004), the Texas Supreme Court recently consider the issue of whether a lease provision waiving a jury in any litigation over the lease is by itself unenforceable and, if not, whether the provision is invalid in a lease.

In *Prudential*, the underlying lawsuit involved a restaurant company's lease with Prudential's agent and the restaurant owners guaranty that incorporated provisions of the lease by reference. The restaurant company and the owners sued to end the lease because of an allegedly foul odor on the premises and requested a jury trial. Prudential moved to quash their jury demand, but the trial court denied the motion. The court of appeals then denied mandamus relief. Reversing the lower courts, the Texas Supreme Court held that a jury trial-waiver clause in an agreement does not violate Texas law or public policy. Rather, public policy that permits parties to waive trial altogether does not forbid waiver of trial by jury. Thus, if the parties willingly agree to a non-jury trial, enforcing that agreement is preferable to leaving them with arbitration as their only enforceable option because in arbitration parties waive not only their right to trial by jury but their right to appeal. *See Id.*

But, unlike arbitration agreements, which Texas law highly favors, "the right to a jury trial is so strongly favored that contractual jury waivers are strictly construed and will not be lightly inferred or extended." *In re Credit Suisse First Boston Mortg. Capital, L.L.C.***,** 257 S.W.3d 486 (Tex.App.—Houston [14th Dist.] 2008, mandamus filed (citing *Prudential*, 148 S.W.3d at 132-33 n. 26). Therefore, enforcement of a jury waiver requires that the waiver be "voluntary, knowing, and intelligent act that was done with sufficient awareness of the relevant circumstances and likely consequences." *Id* (citing *Prudential, 148 at 132* citing *Brady v. United States,*

397 U.S. 742, 748, 90 S.Ct. 1463, 25 L.Ed.2d 747 (1970)).

I. Payment of Attorneys Fees

1. Generally

The payment of attorneys' fees and expenses is often a material term in a trust or estate settlement. If not addressed, the settling parties may be involved in additional litigation regarding their payment. This occurs frequently in probate matters. Texas Probate Code Section 243 allows a named personal representative or beneficiary to seek payment of their attorneys fees and expenses from the estate in a contested matter, even if not successful, upon a finding that they were in good faith and brought the proceeding with good cause. *See* TEX. PROB. CODE ANN. § 243 (Vernon 2003); *see also Salmon v. Salmon*, 395 S.W.2d 29 (Tex. 1965) (reasonable fees mean hourly not contingent fees). *See* discussion *supra.*

Similarly, a trustee is statutorily entitled to reimbursement for attorneys' fees and expenses and other costs incurred in administering and protecting the trust. *See* TEX. PROP. CODE ANN. § 114.063 (Vernon 2007). Most trust agreements also provide that a trustee is entitled to pay his professional advisors from the trust or to be reimbursed for such expenses. *See* discussion *supra.*

2. Estate Settlements

If attorneys' fees and expenses are to be paid to a party's counsel, it is preferable to provide for the estate to pay them directly rather than include these fees and expenses in the amount paid to such party. This allows the estate at least the opportunity to deduct the fees on the death tax return or estate income tax return. For example, the agreement may provide that:

> Each party's attorneys' fees and expenses relating to the administration, preservation and settlement of Decedent's estate shall be paid from Decedent's Estate as follows:
>
> (i) Decedent's Estate shall pay J, K & L law firm the sum of $_____ in settlement of A and J, K & L's claims for attorneys fees and expenses relating to Decedent's Estate and the Litigation within ___ days of the effective date of this agreement; and
>
> (ii) Decedent's Estate shall pay M, N & O law firm the sum of $_____ in settlement of B and M, N & O's claims for attorneys fees and expenses relating to Decedent's Estate and the Litigation within ___ days of the effective date of this agreement; and
>
> (iii) Decedent's Estate shall pay all fees and expenses incurred by the law firm of P, Q & R through the delivery of the remaining assets of Decedent's Estate pursuant to the terms of this Agreement; provided, however, that the total attorney fees and expenses to be paid under this subparagraph (iii) shall not exceed $_____.

If the parties anticipate a personal representative will continue to act on behalf of the estate, the agreement should clarify that the payment of his or her future fees are not capped or prohibited by the agreement. For example:

> Notwithstanding any provision in this agreement to the contrary, the personal representative of Decedent's Estate shall have the right to seek payment of his reasonable and necessary attorneys fees and expenses from the Decedent's Estate.

3. Trust Settlements

Depending on the facts and circumstances, the settlement agreement may expressly provide whether the trustee's attorney fees and expenses should be paid from the trust and, if so, the agreed amount. A beneficiary may seek such an agreement to prevent a trustee from further depleting a trust. For example, the agreement may provide that:

> A and the law firm of XYZ shall receive the sum of $_____ in full and final settlement of any claims they may have against the parties to this agreement, the X Trust or its beneficiaries relating to the payment of or the right to reimbursement for attorneys fees and expenses incurred by A as trustee of the X Trust pursuant to the trust agreement, Section 114.063 and 114.064 of the Texas Property Code, as presenting in effect, or otherwise.

4. Guardianship Settlements

A party seeking the appointment of a guardian may seek the payment of his attorneys fees and expenses pursuant to Section 665B of the Texas Probate Code. *See* TEX. PROB. CODE ANN. § 665B (Vernon 2003). The award of fees is contingent on a finding "that the applicant acted in good faith and for just cause in filing and prosecution of the application." Id.

To support such a finding, the applicant should ask all the parties to the agreement to provide that he or she was in "good faith and brought the application with just cause." The agreement may also provide for the payment of the fees from the ward's estate, subject to court approval. The approval of attorneys' fees and expenses is, however, less certain in guardianship

matters. Therefore, the agreement should expressly provide whether the payment of the requested fees and expenses is a condition precedent or essential term of the agreement. If not, it is advisable to provide that the remaining terms of the agreement are enforceable in the event the court refuses to approve some or all of the requested fees and expenses.

5. Provide for the Entry and Execution of Supporting Documentation & Judgments

It is helpful to address in any settlement documents what additional actions and/or documents may be requested or required to support the potential deductibility of the legal fees paid by the estate.

a. Judicial Findings & Judgments

When a judicial proceeding is pending, it is advisable for the attorney's fees to be incorporated in an order or judgment. The Court should find that the representative has met the applicable state law requirements for payment. For example, in a will contest the court may find as follows:

> The attorneys' fees and expenses incurred by X in the amount of $_____ are necessary and essential expenses for the proper prosecution of the probate of the Last Will and Testament of Decedent dated July 1, 20XX, and the settlement, partition and distribution of the Estate. The attorneys' fees are reasonable in amount with respect to the services performed and are necessary expenses and proper expenses relating to the probate of the Last Will and Testament of Decedent dated July 1, 20XX, and the defense of the contest to such will filed by Y. The court finds that the payment of such fees are proper under the Texas Probate Code and that such fees and expenses were required to properly administer and settle this Estate.

Likewise, in the Court may enter a judgment that provides as follows:

> ORDERED, ADJUDGED and DECREED that X acted in good faith and with just cause in seeking the probate of the Last Will and Testament dated July 1, 20XX, of Decedent, and that he shall be reimbursed from the personal representative of the Estate of Decedent the sum of $_____ for legal fees and expenses, including court costs, relating to the prosecution and defense of such Will in this cause and shown to be reasonable and necessary. It is further,

Note, however, that court approval of attorneys' fees and expenses to be paid by an estate will not preclude a challenge to their deductible as administration expenses on the Form 706 as Internal Revenue Service takes the position that it can independently determine the reasonableness of the fees.

b. Supporting Documentation

It is also advisable for the attorneys to agree to execute all necessary forms or affidavit's as may be required by Internal Revenue Service to support the deductibility of such fees and expenses. For example, the agreement may provide:

> The parties agree that to the extent requested by the Internal Revenue Service or otherwise deemed advisable by the Executor of Decedent's Estate, each such party's attorney shall complete and execute a Form 4421 (Declaration of Executor's Commissions and Attorney's Fees) and such other document as may be required at audit to document and support the deductibility of legal fees paid to such party's attorney(s).

J. Effective Date of Agreement

Settlement agreements involving guardians and administrators generally require court approval. *See* TEX. PROB. CODE ANN. §§ 234, 774 (Vernon 2003). Settlements involving corporations and other business entities may require the consent of the board of directors, managing partners, general partners, etc. If additional consents are required, the agreement should expressly provide that the agreement (even as to parties signing) is not effective and enforceable until the required consents or approvals are obtained.

Thus, a settlement agreement requiring court approval may provide that:

> This Settlement Agreement shall be effective and enforceable upon the last to occur of the following: (i) the date that the last Party executes this Settlement Agreement, or (ii) the date Probate Court Number ___ approves this Settlement Agreement. The Parties agree to seek the approval of this Settlement Agreement by Probate Court Number ___ within thirty (30) days of the date the last Party executes this Settlement Agreement. A facsimile signature for any Party may serve as an original. If Court approval is not obtained, this Settlement Agreement shall be null and void and of no effect.

K. Conditions v. Covenants

The enforceability of an agreement can be conditioned on certain events or actions. For example, court approval of a settlement agreement may be a condition precedent to its enforceability by any party. *See* discussion, *supra*. This condition is commonly included in an agreement involving a court-supervised proceeding.

Alternatively, the settlement agreement may contemplate the parties taking certain action. The

failure to do so will not, however, generally be held to be a condition precedent but, rather, a breach of an enforceable covenant of the agreement.

The issue of condition versus covenant often arises when an agreement provides for the creation and execution of additional settlement documents. The settlement agreement should clearly provide whether the execution of additional settlement documents is a condition precedent to the formation of an enforceable agreement. Without such clearly expressed language, courts have held that the subsequent documents are merely a memorialization of an already existing settlement. *See Hardman*, 2 S.W.3d at 380; *Castano v. San Felipe Agricultural Manufacturing & Irrigation Company*, 2004 WL 839693 (Tex.App.—San Antonio 2004, n.p.h)(not released for publication to date).

L. Enforcement

The agreement should provide how the agreement will be enforced. For example, the agreement may provide that it will be incorporated into a final judgment. Alternatively, it may be enforced by default as a contract. In light of the *Reppert* decision, however, it is advisable to expressly provide whether a judgment approving the settlement agreement will be self-enforcing through the trial court's contempt powers or enforceable only via a breach of contract action. *See Reppert*, 943 S.W.2d at 174 (enforcement provision essential term of agreement).

If it is decided that the agreement will be incorporated into a final judgment, consider incorporating all of the terms of the agreement into the judgment rather than select ones to avoid claims of *res judicata* or merger in the future. *See Compania Financiera Libano, S.A., v. Simmons*, 53 S.W.3d 367 (Tex. 2001)(Supreme Court reversed appellate court's finding *res judicata* and merger barred action for enforcement of terms that were not included into agreement when agreed judgment incorporated only two of four terms and judgment denied all other relief not expressly granted). The failure so do so, however, should not be a bar to enforcing all of the terms of the settlement agreement as a contract unless the agreement expressly limited enforcement rights to the final judgment. *See Id.* at 367.

X. WILL CONTEST PROVISIONS

A. Generally

Settlement agreements are frequently used in the settlement of will contests or other disputes between heirs and devisees. Drafting a settlement agreement relating to the settlement of an estate can be an emotional, time-consuming and onerous process. The drafter must balance the specific desires of his client as to which assets to receive, when to receive them, who can be involved in the transfer (i.e., I will not deal with my sister in this issue), and related issues with the technical provisions necessary to address probate and tax issues. At the end of mediation, most estate settlements involve the same basic provisions relating to the distribution of assets, waivers of claims, tax payment, release, and indemnities. In some highly litigious and emotional situations, the agreement can be an effective tool to avoid future contests or interference. A brief discussion accompanied by a number of sample provisions follows. Also, sample agreements are attached as Exhibits A and B to this outline.

B. Estate Assets

1. Disclosure of Assets

It is often advisable to include a representation among the parties that they have disclosed all known estate assets. For example, the agreement may provide as follows:

> Each Party represents to every other Party that, to the best of his or her knowledge, the existence of all of the property, real and personal, community and separate, belonging to Decedent as of her/his date of death has been disclosed as described on Exhibit A attached.

If an inventory or death tax return has been prepared, the parties may reference these documents. For example:

A and B represent to C that, to the best of their knowledge, there are no properties, real or personal, belonging to Decedent as of her/his date of death other than the assets disclosed on the inventory and list of claims filed by Administrator for the Decedent's Estate and the inventory and list of claims and the Form 706, Federal Estate Tax Return filed by A, as Independent Executor of the Estate. A and B further represent and warrant to C that, to the best of their knowledge, there are no gifts or other transfers by or on behalf of Decedent in excess of $10,000 which have not previously been disclosed in the gift tax returns filed with the Internal Revenue Service. A and B represent and warrant that they have filed all alleged testamentary instruments executed by Decedent, of which they are aware, with the Clerk of the Harris County Probate Court, prior to the date of this Settlement Agreement. Alternatively, it is suggested, although not required, that the parties expressly waive any right to disclosure.

When the surviving spouse owns separate property, and the spouse is not the sole or residuary beneficiary of the estate, the agreement should identify and confirm her/his separate estate to avoid property characterization issues. This, obviously, is particularly important in second, third, etc., marriage

situations. For example, the agreement could provide that:

> The Parties agree that A owned significant property prior to her/his marriage to Decedent and such property continued to be owned by A as her/his separate property, and Decedent's Estate has no interest in or claim against such property which is described in Exhibit B. The Parties acknowledge that the property listed on Exhibit B is A's separate property (i) free of any and all claims of Decedent, Decedent's Estate, or B, C, or D, including but not limited to those relating to the separate character of the property or the community estate, and (ii) B, as the Independent Executor of the Estate, partitions to A any community interest, if any, Decedent and/or her/his estate may have in the property listed on Exhibit B.

2. Homestead

When the decedent was married at the time of his or her death, the surviving spouse may acknowledge the couple's homestead to avoid future disputes. For example,

> A acknowledges that the property commonly known as 1000 Smith Street, Dallas, Dallas County, Texas ("Homestead"), is Decedent's separate property.

This type of clause also clearly identifies the homestead in the event the surviving spouse is waiving their homestead rights as part of the agreement. For example,

> A shall vacate the Homestead and release her/his homestead rights in the Homestead on or before April 30, 2009. In the event A fails to vacate the Homestead on or before April 30, 2009 B, as Independent Executor of the Estate, may initiate actions to take possession of the Homestead and, additionally, A shall pay Decedent's Estate the sum of $100 for each day after April 30, 2009 she/he remains in the Homestead. A represents that the condition of the Homestead is substantially the same as it was as of Decedent's date of death other than normal wear and tear. Each Party shall be responsible for obtaining and maintaining insurance on any interest such Party may have in any personal or real property, including but not limited to the Homestead, covered by this Settlement Agreement. Each Party has no obligation to insure any property of any other Party, including the Homestead. All 2008 property taxes related to the Homestead shall be paid by A and all ad valorem taxes for 2009 And subsequent years shall be paid by B and/or Decedent's Estate. A shall be allowed to deduct on his personal income tax return all ad valorem taxes paid by her/him on behalf of or relating to the Homestead.

3. Family Allowance

The agreement should also address whether the surviving spouse is waiving her/his right to seek a family allowance or to set aside exempt property. For example,

> A waives, renounces and disclaims any right she may have to seek a family allowance pursuant to Section 286, *et seq*., of the Texas Probate Code, or otherwise.

4. Conveyance Documentation

The settlement agreement effectively conveys title to the assets to the parties under the terms of the settlement agreement. The agreement should also, however, provide for additional conveyance documentation to be executed and delivered in a timely manner. The receipt of the required documentation vests clear title in the transferred assets to the beneficiary/party and avoids any future title disputes. While deeds are essential to the transfer of real property, the transfer of personal property is also facilitated by the execution of bills of sales, stock powers, etc. Thus, a standard provision may provide as follows:

> In order to effectuate the conveyance of all of Decedent's interest in the property passing to A pursuant to the terms of this Settlement Agreement and property described in Exhibit B, E, as Independent Executor of the Decedent's Estate, shall deliver to A, contemporaneously with the execution of this Settlement Agreement by all the Parties, all such requisite executed documentation, deeds, bill of sales and stock transfers as is necessary to convey to A in fee simple all of Decedent's interest including, but not limited to, an executed (i) Special Warranty Deed in the form specified as Exhibit C which shall convey all of Decedent's interest in the Ranch to A, and (ii) an assignment in the form specified, as Exhibit E which shall irrevocably assign and convey to A all of Decedent's interest in X Corp. E, as Independent Executor of the Estate, shall also assign the stock by an appropriate notation on the share certificate representing Decedent's interest in X Corp. Further, E, as Independent Executor of the Estate, shall contemporaneously with the execution of this Settlement Agreement by all Parties sign such letters, authorizations or any other documentation necessary to require Bank to deliver the entire balance of Account No. 000000 to A as his sole and separate property.

5. Waiver and Release of Other Interest

To the extent a beneficiary is settling his or her interest in exchange for specific assets, he should expressly acknowledge that he has no other interest in decedent's estate. At least one appellate court has held it is not enough to simply state that the agreement resolves all of a claimant's claims against the estate. *See Ferguson v. Ferguson*, 111 S.W.3d 589 (Tex.App.—Fort Worth 2003, pet denied).

In *Ferguson*, a wife was conveyed the residence under her husband's will. Before it was distributed to her, she filed a contest to the Inventory filed by her step-son, the executor of the estate, challenging the marital property characterization of various assets. Prior to the trial on the characterization issues, wife settled and received a monetary amount pursuant to an "agreement for the resolution of [wife's] Complaints and her claims against the estate." *Id. at 592.* After paying the agreed amount, the executor claimed that the wife had relinquished any claim to the real property bequeathed to her under the will. While the trial court agreed with the executor, the appellate court reversed finding that her "claims" were limited to the issues involving characterization of separate and community property and did not extend to assets bequeathed to her under the will. *See Id.* at 592-3. The appellate court also noted that because the house was bequeathed to the wife under the will, titled vested in her immediately and therefore it found the wife could not "reasonably be viewed as having a 'claim' against the estate . . . because she already holds equitable title to it." *Id.* at 596.

A sample provision may provide as follows:

> A shall receive no other property of Decedent's Estate or X Trust other than the property set forth in this Settlement Agreement, delivered as contemplated by the terms of this Settlement Agreement, which shall fully and unconditionally satisfy and discharge her/his rights as an heir and/or beneficiary and/or claimant of the Decedent's Estate and any interest in X Trust, created by Decedent prior to her death. Save and except for the property passing to A under this Settlement Agreement, A shall have no further interest in Decedent's Estate, X Trust and Decedent's solely-owned business or any other asset of Decedent's Estate whether bequeathed to A under any alleged will or trust of the Decedent or any property that A may claim to have a community interest in as of the time of Decedent's death.

C. Prior Gifts

Parties to a will contest often challenge prior gifts allegedly made by a decedent. These gifts are frequently made pursuant to powers of attorney and, even though taxable, the required gift tax returns are not filed. The parties should consider acknowledging the gift to avoid future disputes. The parties should consider acknowledging the gift to avoid future disputes and to provide the personal representative a good faith basis to file any necessary tax returns including 709s and the 706. For example, the agreement may provide that:

> A and C agree that the gift deed dated December 31, 2002, and recorded under Film Code No. 000-00-0000, executed by B, and conveying 1.00 acres of land to A, as a gift, is valid and they have no claim to the real property described therein and will not attempt to set aside said deed for any reason.

Furthermore, the deceased spouse's estate or the surviving spouse may attempt to challenge the other spouse's prior gifts alleging fraud in the community. The parties may agree to recognize the validity of each spouse's prior gifts and waive any right to challenge such gifts. An agreement may provide that:

> The Parties acknowledge that Decedent and/or A made gifts from their community property estate and also their respective separate property estates during their marriage. The Parties acknowledge that some gifts may have been made by (i) A without the knowledge and/or consent of Decedent, and (ii) Decedent without the knowledge and/or consent of A. In addition to the release given in Paragraph 99 of this Settlement Agreement, each of the Parties agrees that they shall waive any and all claims and causes of action, known or unknown, including but not limited to any rights or reimbursements, claims of actual or constructive fraud, misrepresentation, interference, tortious or contractual, with respect to gifts made by or on behalf of Decedent and/or A.

D. Taxes

A party to a settlement agreement should always consider the tax liabilities and consequences arising out of the settlement. These considerations are not limited to estates subject to death taxes. Rather, as previously discussed, ignoring gift and income tax issues can wreak havoc on an estate settlement. For example, agreeing to receive $40,000 from the *residuary* may result in some portion being characterized as distributable net income and, thus, subject to income tax. A provision that simply provides for the payment of $40,000, however, will generally be deemed to be a payment of a specific sum and not subject to income taxation. *See* discussion, *supra*.

1. Estate Tax Assumptions

Under the appropriate circumstances, it may be advisable to expressly state in the agreement the parties' understandings of how the payments under the agreement will be reported in any tax filings. For example, the agreement may provide as follows:

> For purposes of this Agreement the Tax Assumptions shall be as follows:
>
> (i) All of the Decedent's Estate and Property which, pursuant to this Agreement, passes to either Spouse or the QTIP Trust will qualify for the marital deduction under Section 2056(a) of the Internal Revenue Code of 1986, as amended (the "Code");
>
> (ii) No portion of the Former Spouse Marital Trust established under the Will of Former Spouse shall be liable for or bear any federal estate tax as a result of the Decedent's death; and
>
> (iii) A copy of the Agreed Judgment approving this Agreement shall be attached to the U.S. Estate Tax Return - Form 706 filed on behalf of the Estate.

2. Income Taxes Relating to Distributions

To avoid a future dispute as between the parties regarding whether a distribution under the agreement carried out income, the parties may acknowledge in their agreement that the payment is intended to constitute a specific sum and therefore does not carry out distributable net income. *See* discussion *supra.* Note, however, that this provision is not binding on the Internal Revenue Service, but will at least discourage clever probate lawyers from attempting to effectively reduce a party's interest in the estate. Such a provision may provide that:

> The Parties agree and confirm that they believe that all distributions and/or property passing to A and any other amounts passing under the terms of this Settlement Agreement should be treated for income tax purposes as a settlement of a claim and/or as a gift or bequest of *a specific sum of money or of specific property* not payable in installments and are not punitive, not for services rendered, and no portion represents income or interest relating to such specific sum of money; *i.e.*, none of the distributions will constitute distributable net income to A. _____ agrees that _he will not report any portion of this payment as distributable net income of the Estate.

3. Tax Responsibilities and Notice Requirements

Considerations should be given to including in the agreement clear procedures as to which parties are responsible for handling and tax audits or disputes. However, a party that is not directly involved in certain tax filings may be affected by an audit or any resulting adjustments. For example, estate taxes allocated to such parties share may be increased. Therefore, it is advisable to include in the settlement agreement provisions that clearly provide who is responsible for all filings and when other parties are entitled to receive notice of such filings. For example, the agreement may provide as follows:

> X shall notify Y in writing within twenty (20) days or such shorter period as may be required thereby of receipt of written notice of any pending or threatened tax examination, audit or other administrative or judicial proceedings (a "Tax Contest") that could reasonably be expected to result in an indemnification obligation for taxes, interest and penalties pursuant to the Rule 11 Agreement and failure to timely give such notice shall mean that no indemnification is due to such defaulting party. If a Tax Contest relates to any taxes for which Y could be liable hereunder, Y shall have the option to use legal counsel of her choosing and to control and handle the defense and settlement of such Tax Contest at her expense. If Y elects to control and handle the defense and settlement of such Tax Contest, X agrees not to interfere with Y's defense and settlement of such Tax Contest. If Y elects not to control the defense and settlement of such Tax Contest, any other party may elect, in writing to Y, to control and handle the defense and settlement of such Tax Contest and Y shall indemnify such party for all reasonable and necessary fees and expenses, including experts.

4. Access to Death Tax Returns

Finally, a party receiving estate assets should seek a copy of the filed death tax returns. This provides the beneficiary evidence of his or her tax basis. The beneficiary should also request a copy of the "closing letter" to evidence the release of any death tax liens. The settlement agreement can simply provide that:

> A and the then acting personal representative of Decedent's Estate shall deliver to a copy of any federal and state death tax returns and any federal and state closing letters or agreements for Decedent's Estate. A or the then acting personal representative shall deliver a copy of the returns within five (5) business days of the date they are filed and the letters within ten (10) business days of receipt.

5. Income Tax Issue Relating to Deceased and Surviving Spouse's Income Tax Returns

When the surviving spouse is not the personal representative of the deceased spouse's estate, it may

be advisable to address the deceased and surviving spouse's income tax liabilities and responsibilities. This is particularly important when the spouses have significant income or have been tax aggressive.

The agreement may provide how the final income tax return will be filed and each spouse's responsibility for any income taxes due. For example, the agreement may provide as follows:

> A shall file his 2008 income tax return as a married individual filing separately. Any taxes, interest or penalties that A may owe to the federal government for all items reported on his 2008 personal income tax return as well as all taxable periods subsequent to the date of Decedent's death shall be the sole liability and obligation of A to be satisfied and paid solely from his property, and from which A shall forever hold harmless, indemnify and defend Decedent and Decedent's Estate. If there is an audit of Decedent and A's joint 2007 personal income tax return or any prior years joint personal income tax returns, Decedent's Estate and A shall each be responsible for and shall pay one-half (1/2) of any tax due, including any penalties, interest and costs of defending the claim and A shall forever hold harmless, indemnify and defend Decedent and Decedent's Estate from his one-half (1/2) of such liability, penalties, interests and costs. All liabilities and obligations incurred by A are the sole liabilities and obligations of A, to be satisfied and/or provided for by A and from which A shall forever hold harmless, indemnify and defend Decedent and Decedent's Estate. B, as Independent Executor of the Estate, shall file, as may be due, Decedent's 2008 income tax return as a married individual filing separately. Any taxes, interest or penalties that Decedent or Decedent's Estate may owe to the federal government for all items reported on Decedent's 2008 personal income tax return as well as all taxable periods subsequent to the date of Decedent's death shall be the sole liability and obligation of Decedent's Estate, B and C, to be satisfied and paid solely from Decedent's Estate, and from which Decedent's Estate, B and C shall forever hold harmless, indemnify and defend A. If there is an audit of Decedent and A's joint 2007 personal income tax return or any prior years joint personal income tax returns, Decedent's Estate and A shall each be responsible for and shall pay one-half (1/2) of any tax due, including any penalties, interest and costs of defending the claim and Decedent and Decedent's Estate shall defend A from Decedent's one-half (1/2) of such liability, penalties, interests and costs. Except as otherwise provided by this Settlement Agreement, all liabilities and obligations incurred by Decedent or Decedent's Estate are the sole liabilities and obligations of Decedent's Estate, to be satisfied and/or provided for by Decedent's Estate and from which Decedent's Estate, B and C shall forever hold harmless, indemnify and defend A.

To facilitate the release of information necessary to prepare the respective returns, the agreement may provide that:

> B and C agree to release to A or such other persons as he may specify (i) all tax records and tax documentation regarding Decedent and A in their possession or under their control within ten (10) days of such written request by A or A's accountant if, as, and when such information is requested by A or his accountant, and (ii) all financial records of A, including but not limited to, all bank statements, credit card statements, insurance information, and real estate records in his or her possession or under either of their actual or constructive control, if any, within ten (10) days of such written request by A. Furthermore, A agrees to release to B, as Independent Executor of the Estate, or any such other person as he may specify all (i) tax records and tax information of Decedent in A's possession or under his actual or constructive control on or before April 1, 2008, which is reasonably necessary to prepare Decedent's final income tax return; and (ii) financial records of the Decedent, including but not limited to, bank statements, credit card statements, insurance information, and real estate records in his possession of under his control, if any, within ten (10) days of such written request by B.

E. Address Apportionment of Death Taxes

The parties should attempt to agree on the apportionment of any death taxes. *See* discussion *supra.* As previously discussed, the agreement when properly entered into, takes the place of the Will, if one existed. Thus, an issue exists whether any tax apportionment language in the Will is applicable to the terms and provisions of a settlement agreement unless the administrative provisions of the Will are incorporated into the agreement by reference. For example, the agreement may provide as follows:

> Wife, individually and as Successor Independent Executor of the Estate (once appointed) hereby agrees to be liable for (i) all estate, generation-skipping, gift and inheritance taxes (defined herein as "Transfer Taxes") (if any are owed), including any interest and penalties, thereon (if any) in respect of the Decedent, the Decedent's

> Estate, the Property, the devises under the Will as modified under this Agreement, and (ii) all income taxes and penalties attributable to any withdrawal or deemed withdrawal from any IRA or other account transferred or assigned to the Spouse. As between Wife and Children, Children shall not be liable, directly or indirectly (including, without limitation, any transferee liability), for any tax, including any interest and penalties, thereon (if any) imposed on Wife or the Estate, or resulting from any withdrawal or deemed withdrawal from any IRA or other account transferred or assigned to the Wife, nor shall they be liable for any income, gift or estate tax, including any interest and penalties, thereon (if any) imposed on Wife or the Estate.

In the absence of a provision addressing tax allocation, it appears that the default provisions set forth in Texas Probate Code Section 322A will apply. *See* TEX. PROB. CODE ANN. § 322A (Vernon 2003 & Supp. 2008).

F. Future Contests & Interference

An estate controversy is often between members of an immediate family, and the parties are concerned that certain parties will continue to interfere with their affairs or contest their will or other planning documents at some time in the future. While each clause should be drafted to reflect the specific concerns raised by the parties, two issues that commonly arise are future will contests and interference with business interests. Sample provisions for these two matters follows.

1. Future Will Contests

A very lengthy, but so far successful, provision that attempts to avoid future will contests is as follows:

> Except as is required to enforce the terms of this Settlement Agreement, B, Individually and as Independent Executor of the Estate, and C agree never, directly or indirectly, individually or with another, contest, initiate, or voluntarily participate in any claim or cause of action (hereinafter collectively referred to as "Prohibited Acts") relating to (i) A's estate plan, including, without limitation, any will or trust allegedly executed by A, or by intestate succession, whether related to formal court proceedings or otherwise, (ii) A's inter vivos disposition of his property, and (iii) A's testamentary disposition of his property. Such Prohibited Acts include, but are not limited to, (i) contesting the probate or validity of any Will, Trust, Power of Attorney, Living Will, Designation of Guardian, Deed, Assignment, Family Limited Partnership, or other legal instrument, created or executed by or on behalf of A, or any provision thereof, (ii) instituting or joining in (except as a party defendant) any proceeding to contest the validity of any Will, Trust, Power of Attorney, Living Will, Designation of Guardian, Deed, Assignment, Family Limited Partnership, or other legal instrument, created or executed by or on behalf of A, or preventing any provision thereof from being carried out in accordance with its terms or acquiescing thereto, (iii) in any manner questioning or disputing or making any statement or declaration which questions or disputes the validity of any Will, Trust, Power of Attorney, Living Will, Designation of Guardian, Deed, Assignment, Family Limited Partnership, or other legal instrument, created or executed by or on behalf of A, (iv) initiating, participating, or opposing in any formal court proceedings or otherwise the performance of A's fiduciary or any duty, act or discretion granted to or incumbent upon him or her under the terms of any Will, Trust, Power of Attorney, Living Will, Designation of Guardian, Deed, Assignment, Family Limited Partnership, or other legal instrument, created or executed by or on behalf of A, or by law, (v) instituting or participating in any manner (except in support of A's fiduciary) in any construction or any provision of any Will, Trust, Power of Attorney, Living Will, Designation of Guardian, Deed, Assignment, Family Limited Partnership, or other legal instrument, created or executed by or on behalf of A, by declaratory judgment or otherwise, (vi) instituting or participating in any manner in any proceeding (except in support of A's fiduciary) to contest or in any manner question any accounting prepared by or on behalf of A's fiduciary, (vii) instituting or participating in any claim or cause of action, including but not limited to, tortious interference with inheritance rights, against any person which is based in any way on the proposition that A was not of sound mind, lacked capacity (contractual or testamentary), was unduly influenced, or failed to comply with applicable law at the time that A executed any legal instrument, including but not limited to, any Will, Trust, Power of Attorney, Living Will, Designation of Guardian, Deed, Assignment, Family Limited Partnership, or other legal instrument, or (viii) aiding, assisting, or encouraging another in such Prohibited Acts.

2. Future Interference With Business Interests

A sample provision providing for non-interference with a business interest follows:

All parties other than X agree that they will not (i) interfere with the business of the Company on or after the Effective Date including, but not limited to, contacting competitors, clients, employees, former employees, creditors, and/or potential clients regarding the Company and/or X, and (ii) directly or indirectly, engage in any business activity conducted by the Company, or be the owner of more than ten percent (10%) of the outstanding capital stock of any corporation or an officer, director of, or employee of any corporation or a member or employee of a partnership or any other enterprise which conducts a business in competition with the Company for a period of three (3) years following the Effective Date. All parties other than X agree that this covenant not to compete is ancillary to this Agreement executed contemporaneously with this Agreement, and is supported by independent valuable consideration the sufficiency of which is hereby acknowledged. In the event that the provisions of this Section should ever be deemed to exceed the time or geographic limitations permitted by applicable laws, then such provisions shall be reformed to the maximum time or geographic limitations permitted by the applicable laws, pursuant to the provisions of the Covenant Not to Compete Act (TEX. BUS. & COM. CODE ANN. §§ 15.50-15.52). In the event of a breach of the provisions of this Section, the Parties agree that the Company shall be entitled to recover damages for such breach at law or equity. In addition to all other remedies at law and in equity which the Company may have for breach of a covenant set forth in this Section, it is agreed that in the event of any breach or attempted or threatened breach of any such covenant, the Company shall also have the right to obtain an injunction against any breaching party, as applicable, prohibiting such breach or attempted or threatened breach, by proving the existence of such breach, or attempted or threatened breach (by a preponderance of the evidence) and without the necessity of proving either inadequacy of legal remedy or irreparable harm, and (iii) engage in any pattern of conduct that involves the making or publishing of written or oral statements or remarks (including, but not limited to, the repetition or distribution of derogatory rumors, allegations, negative reports, or comments) which are disparaging, deleterious, or damaging to the integrity, reputation, or goodwill of the Company or of its agents, shareholders, officers, directors, affiliated entities, creditors, and all other persons, natural or corporate, in privity with the Company, and (iv) disclose the Company's business information, Company trade secrets or any confidential information to third parties, including any competitors or others in the business, including but not limited to, customer names; customer accounts and credit data; referral sources; customer programs and software; information relating to processes, formulae, plans, devices, or materials of the Company; customer comments; management, accounting and reporting systems, procedures and programs; marketing and financial analysis, plans, research, programs and related information and data; forms, agreements and legal documents; regulatory and supervisory reports; correspondence; statements; corporate books and records; and other similar information in both "hard copy" and electronic form.

XI. TRUST DISPUTE PROVISIONS

A. Generally

Settlement agreements are frequently used to resolve various trust matters, including an agreed resignation of a trustee, the judicial settlements of a trustee's accounts, and disputes between or among trustees and beneficiaries. The majority of agreements involving trusts involve the same basic definitions and provisions discussed *supra* relating to waivers of claims, release, and indemnities. However, a few addition provisions that deal trust disputes are discussed below. Also, a sample agreement is attached as Exhibit C to this outline.

B. Transfer/Distribution of Assets

When a trust is terminating or a successor trustee will be appointed, the agreement may to address the timing and manner of the deliver of assets to the proper party. For example, an agreement could provide the following:

> A shall deliver to B, as the successor trustee of Trust X, within a reasonable time, not to exceed thirty (30) days following the Effective Date of this Agreement, the trust estate of Trust X. Prior to such delivery, A shall continue to maintain, but as custodian only, the assets of Trust X, and shall not sell, transfer or purchase assets without the written direction of B.

C. Trust Records

Furthermore, it is advisable to address what party shall be entitled to possession of trust records, the period of time any party must retain such records, and a prescribed manner for other parties to access such records, if required. The statute of limitation is four (4) years for breach of fiduciary duty, but that can be extended based on alleged non-disclosure or pursuant

to the discovery rule. Furthermore, the statute of limitation for most income tax issues is six years.

Therefore, it is suggested that trust records be maintained by a trustee for at least seven years following the termination of the trust or such trustee's appointment. When minors are a potential party, however, the trustee should consider retaining these records indefinitely. During this period of time, a beneficiary may require copies of various records to establish tax basis or for another purpose. The agreement may address the ongoing obligations to make available and rights to access such records. For example, an agreement could provide the following:

> A is entitled to retain possession of the original trust records other than the original signed trust agreement. A shall deliver the original signed trust agreement to B, as successor trustee of Trust X, within ten (10) days of the Effective Date of this Agreement. Provided, however, upon written request by B, C or D, A shall produce all non-privileged documents for inspection and copying by such requesting party. Non-privileged documents must be made available within ten (10) business days of such request at A's offices. The requesting party shall pay all copy expenses or related costs.

Alternatively, the agreement may provide as follows:

> A shall deliver to B, as the successor trustee of Trust X, within a reasonable time, not to exceed thirty (30) days following the Effective Date of this Agreement, all records of Trust X now in possession or control of A other than any document that relates to any communication between A and his attorneys that are privileged by Texas law. A may retain a copy of such records at [A's expenses/the expense of Trust X].

D. No Duty to Redress

To both protect the resigning trustee and any proposed successor trustee, a settlement intended to resolve all issues involving a prior trustee should include a provision that relieves a successor trustee of any claimed duty to redress the actions and inactions of his or her predecessor. A provision may provide as follows:

> The parties agree that B, as successor trustee of Trust X, shall have not duty to redress the actions or inactions of A or any other Predecessor trustee of Trust X including but not limited to, the Claims and the Transactions, and release him of duty, if any.

XII. GUARDIANSHIP PROVISIONS

A. Generally

The mediation and settlement of guardianship disputes is becoming increasingly popular. It is an excellent means to minimize the emotional and financial costs of this type of litigation. Settlement often (i) preserves the ward's property, (ii) avoids additional litigation costs, (iii) preserves family relationships, and (iv) acts as a bridge for communication. The unusual nature of a guardianship, however, results in the drafting of some unique provisions. A discussion of some frequently encountered provisions follows.

B. Appointment of Guardian

Assuming the ward or proposed ward is incapacitated, the settlement may include the appointment of a guardian. The parties may reach an agreement as to who should be appointed, subject to court approval. As part of such an agreement, certain parties may need to waive the right to seek appointment as guardian. Others may reserve the right to seek appointment as guardian in the event a qualified guardian is not serving.

A sample provision may provide that:

> A and D shall obtain a dismissal with prejudice of their contest to B's application for appointment as permanent guardian of the person and estate of C. A and D waive forever any rights they may have to be appointed guardian of the person and/or estate of C. A and D shall have the right to apply for the appointment of a corporate fiduciary as guardian of the estate of C if B or her(his) successor is found to be acting in material breach of this Agreement by a court of competent jurisdiction. Otherwise, A and D shall never institute, join in, assist, or otherwise participate in any proceeding for the appointment of any individual or entity as guardian for the estate of C except as may be required by law. B shall be appointed permanent guardian of the person of C and will post a cash bond in the amount set by the Court; the Parties will request the Court to set the bond at $_____. B shall have and expressly reserves the right to seek appointment as guardian of the estate of C with prior written notice to A and D. If B seeks such appointment, A and D shall execute and deliver, upon request by B, such releases and/or waivers as are necessary to appoint B as the guardian of the person and/or estate of C that B may reasonably request. B agrees that if (s)he is appointed as guardian of the estate of C, (s)he shall not claim a right as guardian to the possession or control of A's sole management community property, if any. If another person or

entity is acting as guardian of the estate of C, B shall not take any position contrary to the terms of this Agreement.

In the event B ceases or becomes unable to serve as guardian of the person and/or, if and after qualifying, guardian of the estate, and/or attorney-in-fact for C, then M ("M") shall succeed to all of B's rights to serve in any of such capacities to the extent provided for, and subject to, the provisions of this Agreement. The Parties further agree that they will execute, acknowledge, and deliver upon request such releases and/or waivers as are necessary to appoint M, as successor, in any of such capacities provided M agrees to be bound by the terms of this Agreement. All provisions of this Agreement applicable to B (other than representations and warranties made by B) will apply to M, as B's successor.

If M shall fail or cease to serve or qualify as C's guardian, the Parties shall request the appointment of a bank with trust powers or a disinterested third party to be successor guardian of the person and/or estate of C, and all provisions of this Agreement shall apply to the successor guardian.

C. Medical Issues and Access to Information

Family members are sometimes more amenable to allow one person to act as guardian when they feel that they will continue to play a role in future healthcare matters. Many family members will request or demand access to a ward's physician and medical records to independently verify that the ward is receiving good care. A sample negotiated provision that grants limited involvement may provide as follows:

Each of the Parties will have access to medical records and the right to confer with healthcare providers. The Parties agree that the right to confer with health providers does not allow them to interfere with the guardian's power to make healthcare decisions or ability to obtain necessary information. B, as Guardian, will consult with the Parties with respect to the following healthcare issues as they arise: (i) all major treatment decisions; (ii) all proposed changes of residence of C; (iii) changes of physicians; and (iv) any decision involving the election to use hospice care. B shall direct the staff at any facility where C is living to send A information on events at the facility to which the family is invited, including holiday parties and meetings with healthcare providers. This notice shall be effective so long as C resides in such facility. The Parties will use all efforts to communicate with each other by designated telephone and/or pager numbers with respect to these issues. In the event (i) the Parties cannot agree with respect to the designated issues after using their best efforts to reach an agreement, or (ii) in the event B has not received input from the Parties within five (5) hours from the time B has used all reasonable efforts to communicate with the Parties, or (iii) in the event of an immediate life-threatening decision, B, as Guardian, shall have the sole power to make such decisions alone on behalf of C. B shall give reasonable advance notice to A by telephone when C visits with B outside his permanent residence. A shall have the right to check C out of his permanent residence with B's prior written approval, which shall not be unreasonably withheld. B shall have the sole power to make all decisions not described above affecting C's person.

D. Preplanning the Funeral

Funeral arrangements can be emotional hot-buttons for individuals involved in a guardianship proceeding. While this issue may seem premature, it is important to address if the ward is elderly or when death appears imminent. When a non-client will be appointed guardian, it is even more important to make your client's wishes known. Recall the guardian has the power to issue burial instructions.

A sample pre-arranged and agreed funeral provision may provide as follows:

Funeral Arrangements for C. The funeral arrangements for C will be as follows: (i) no obituary will be published in the newspaper; (ii) C will be buried at Cemetery; (iii) X will be the funeral directors and the Parties will use their best efforts to go to the funeral home together to make the funeral arrangements; (iv) a Christian service will be conducted by a minister of Church at Church; (v) a rosary will be held and the casket will be _____ [open or closed]; (vi) C will not be cremated; and (vii) the reasonable funeral expenses will be paid out of the assets of C's Estate.

Burial Plots. Title to Lot 1, Section 1, at Cemetery, Houston, Texas, is held in the name of A and C. The Parties agree A and C will be buried in the two center spaces. B shall be entitled to use the two spaces next to C, on the south, and D shall be entitled to use the two spaces next to A on the north. No spaces may be sold or assigned, and no non-family members may be buried in any of these spaces without the written consent of all the living Parties.

E. Management of Estate

Clearly, the agreement should provide how the ward's estate should be managed when the Ward is

under a guardianship. Consideration must be given to the capacitated spouse's rights to manage the community estate. Provisions regarding the management may provide that (i) a court appointed guardian of the estate will manage ward's estate, (ii) a revocable trust will be created via a power of attorney, (iii) the spouse will manage all community property pursuant to Section 883 of the Texas Probate Code, (iv) the community estate will be partitioned between the spouses and all future earnings will constitute such spouse's separate property, or (v) the estate will be managed under a valid power of attorney.

XIII. REPRESENTATIONS & DISCLOSURES

A. Generally

A settlement agreement, like any contract, is subject to a voidance on grounds of fraud or material misrepresentation. *See Williams v. Glash*, 789 S.W.2d 261 (Tex. 1990). The rationale is that a contract induced by fraud is, in effect, "no contract because there is no real assent to the agreement." *Schlumberger Technology Corp. v. Swanson*, 959 S.W.2d 171 (Tex. 1997) *citing Brown Thompson Co. v. Sawyers*, 234 S.W. 873 (Tex. 1921).

B. Representations

Parties often ask other parties to make certain express representations to verify certain facts or conditions. Representations should be used to confirm material terms, facts or claims upon which the settlement is predicated. By included such representations in the agreement, a party could later seek to void the agreement on grounds of fraud or material misrepresentation if it later determined another party's representations were untrue. Potential representations may include:

- All known assets have been disclosed;
- All known estate planning gifts have been disclosed;
- The amount and nature of prior gifts or transfers have been disclosed;
- Confirmation that the party has not assigned his interest in the estate, trust or property;
- Confirmation as to each parties attorney or waiver of right to seek counsel;
- No party is under duress or coerced into signing the agreement; and
- Each party has received all information requested or waived disclosure (if possible)

Conversely, because of the potential to void a settlement agreement based on a claim of misrepresentation, a party should attempt to limit representations to those necessary to enter into a settlement agreement.

C. Disclosures

It is well settled law that a fiduciary generally has a duty of full and fair disclosure of all its acts. This duty is not negated because the fiduciary is being sued by the beneficiary or because the beneficiary is willing to enter into a settlement agreement. For example, Section 114.032 provides that a settlement agreement between a trustee and a beneficiary is binding if, among other factors, the beneficiary had "full knowledge of the circumstances surrounding the agreement." TEX. PROP. CODE ANN. § 114.032(a)(3) (Vernon 2007). To date, no Texas decision has defined what is "full knowledge" or determined whether such disclosures can be waived by a beneficiary. Therefore, it is advisable for settling trustees to provide beneficiaries and their advisors the opportunity to review its books and records prior to any settlement and require the beneficiary to confirm such information was made available prior to completion of the settlement agreement.

Furthermore, this duty of disclosure also requires that negotiations related to settlement of claims of an estate or trust be disclosed and provided to beneficiaries so that they may have adequate knowledge of the fiduciaries acts. In a recent case of first impression, the issue of disclosure required by a fiduciary versus the obligation of full and fair disclosure was considered. In *Avary v. Bank of America*, 72 S.W. 3rd 779 (Tex. App.--Dallas 2002, pet. denied), a beneficiary filed a lawsuit against the executor of a decedent's estate arising out of a court-ordered mediation of a wrongful death and survival action related to the decedent's estate. The executor moved for summary judgment on all grounds alleging that communications made at the mediation were confidential under Section 154.973 of the Texas Civil Practice and Remedies Code. The trial court granted the executor's summary judgment after permitting limited discovery. The appellate court, however, reversed holding that a separate independent tort was alleged to have occurred during the mediation and discovery was warranted in the context of the executor's duty of full and fair disclosure to the beneficiaries of the estate. Although beneficiary accepted the settlement proceeds reached in mediation, he contended that another offer would have actually resulted in a greater recovery once estate tax considerations had been taken into consideration when then total recovery was apportioned. The appellate court further held that evidence that is discoverable independent of the alternate dispute resolution procedure is discoverable regardless of the mediation. The court noted that the executor's acceptance of an apportionment of the settlement proceeds without consideration of the estate's tax obligations and without any disclosure to the heirs of the effect of the

apportionment on the estate's remaining assets and liabilities is some evidence of a breach of fiduciary duty. The court stated that because of the fiduciary relationship, the beneficiary was entitled to question the executor fully regarding its handling of the estate and other matters regarding the estate. The executor had a duty to disclose this material information to the beneficiaries and their representative.

D. Disclaimer of Reliance

While parties may condition a release or agreement on certain representations, they can also expressly disclaim any reliance. A disclaimer of reliance generally allows parties to avoid future disputes. *See Schlumberger Technology Corp. v. Swanson*, 959 S.W.2d 171 (Tex. 1997); *Atlantic Lloyds Insurance Company v. Butler*, 137 S.W.3d 199 (Tex.App.—Houston [1st Dist.] 2004, pet. filed July 6, 2004)(disclaimer of reliance in settlement agreement conclusively negated other parties alleged reliance on any representations or lack of disclosure by other parties).

A clear cut specific disclaimer effectively negates a claim of fraudulent release in most circumstances. *Id*. At 179; *but see Prudential Ins. Co. v. Jefferson Assocs.*, 896 S.W.2d 156, 162 (Tex. 1995) (concealment or obstruction of party's investigation may negate disclaimer of reliance); *Harris v. Archer*, 134 S.W.3d 411 (Tex.App.—Amarillo 2004, pet. filed April 26, 2004)(disclaimer of reliance may on bar fraudulent inducement claim when fiduciary relationship exists between the parties).

In *Schlumberger*, the Texas Supreme Court held that the following language unequivocally disclaimed reliance:

> [E]ach of us [the parties] expressly warrants and represents and does hereby state … and represent … that no promise or agreement which is not herein expressed has been made to him or her in executing this release, and that none of us is relying upon any statement or representation of any agent of the parties being released hereby, each of us is relying on his or her judgment and each has been represented by … as legal counsel in this matter.

Id. at 180 *citing Prudential*, 896 S.W.2d at 163.

If a fiduciary relationship exists between the parties, it is advisable to disclose any material information regarding the transaction to the extent possible. Additionally, the agreement should specifically disclaim reliance on any and all statements, representations, or non-disclosure of material information by the other parties. The agreement should also expressly release claims for breach of fiduciary duty to disclose material information. *See Harris*, 134 S.W.3d at 431.

E. Tort of Negligent Misrepresentation

Until a few years ago, an attorney representing a party in settlement negotiations could proceed without concern that another party to the agreement may sue him or her for negligent misrepresentation. The 1999 Texas Supreme Court decision of *McCamish, Martin, Brown & Koeffler v. Appling Interests*, 991 S.W.2d 787 (Tex. 1999) rehearing of cause overruled (Jun. 24, 1999) rehearing overruled (Jun. 24, 1999), however, has recently established this cause of action.

In *McCamish*, an attorney and his law firm represented their client in litigation that ultimately settled before trial. The parties entered into a settlement agreement that included certain representations regarding the capacity and authority of McCamish's client to enter into a binding settlement agreement. Thus, the agreement included a provision in which both McCamish and its client made certain representations. It was subsequently determined that McCamish's client did not have the requisite authority to enter into a binding settlement agreement. *Id*. at 790. Appling then filed suit against McCamish on the basis of negligent misrepresentation. The trial court held that McCamish owed no duty to Appling and, thus, could not be liable. The court of appeals reversed finding that an attorney may owe a duty to a non-client for material misrepresentation. *Id*. at 790. On petition for review, McCamish argued it should not be held liable to a non-client for a claim arising out of its representation of a client in litigation. Appling, on the other hand, asked the Court to recognize the distinction between legal malpractice cases, which require privity, and negligent misrepresentation cases, which do not. *Id*. Agreeing with Appling, the Texas Supreme Court extended the tort of negligent misrepresentation as described in Section 522 of the Restatement (Second) of Torts to attorneys. Texas courts have previously recognized this cause of action against other professionals.

In doing so, the Court also recognized that an attorney may reduce or eliminate liability to a non-client by (i) setting forth limitations as to whom should rely on the representation, or (ii) providing disclaimers as to the scope and/or accuracy forming the basis of the representation. *Id.* at 794; *see also, Schlumberger Technology Corp.*, 959 at 179.

XIV. ENFORCEMENT

A. Generally

As previously discussed, settlement agreements are highly favored by Texas courts. *See* discussion, *supra*. A settlement agreement will not be disturbed because of ordinary mistake of law or fact, and will be upheld when all parties have the same knowledge or a means to obtain the same knowledge provided there is

no fraud, misrepresentation, concealment or other inequitable conduct. *See Crossley v. Staley*, 988 S.W.2d 791 (Tex. App. – Amarillo 1999, mand denied). Furthermore, the unilateral mistake of law of the party to a settlement agreement is not grounds to avoid the agreement. *See Crossley* at 796 *citing Atkins v. Womble*, 300 S.W.2d 688, 703 (Tex. Civ. App. – Dallas 1957, writ ref'd n.r.e.).

B. Jurisdiction To Enforce Settlement Agreement

When "the settlement dispute arises while the trial court has jurisdiction over the underlying action, a claim to enforce the settlement agreement should, if possible, be asserted in that court under the original cause number." *Mantas v. Fifth Court of Appeals*, 925 S.W.2d 656 (Tex. 1996); *see also In re General Metals Fabricating Corp.*, 2006 WL 3316877 (Tex.App.—Houston [1st Dist.] 2006, no pet)(not designated for publication)(trial court abused its discretion in failing to abate main cause and severing breach of contract claim); *Batjet, Inc. v. Jackson*, 161 S.W.3d 242, 245 (Tex.App.-Texarkana 2005, no pet.)(noting that parties properly asserted their motion for summary judgment to enforce settlement agreement in trial court under original cause number); *Citgo Ref. & Mktg. v. Garza*, 94 S.W.3d 322, 330 (Tex.App.-Corpus Christi 2002, no pet.)(noting that because settlement dispute arose while trial court still had jurisdiction, parties properly asserted claims to enforce settlement agreement under original cause number). When the dispute arises while the underlying action is on appeal, however, the party seeking enforcement must file a separate breach of contract action. *Mantas*, 925 S.W.2d at 659.

And, in one recent case, the Dallas Court of Appeals has held that a district court lacked jurisdiction over a settlement agreement concerning the distribution of the estate when the administration was pending in a statutory probate court. *See Litoff v. Litoff*, 2009 WL 456682 (Tex. App.—Dallas, n.p.h.). In *Litoff*, the appellate court first considered whether a district court had subject matter jurisdiction. *Id. at *1 (*citing *Mapco Inc. v. Forrest*, 795 S.W.2d 700, 703 (Tex.1990) (orig. proceeding); *Tellez v. City of Socorro*, 226 S.W.3d 413, 413 (Tex. 2007)(per curiam)(subject matter jurisdiction involves court's power to hear case). The appellate court noted that Section 5 of the Texas Probate Code grants a statutory probate court original probate jurisdiction over "all application, petitions, and motions regarding probate or administrations." *Id.* at *2 (citing TEX. PROB. CODE ANN. § 5(d) (Vernon 2003 & Supp. 2008). And, it has jurisdiction over "any and all" matters "appertaining" or "incident" to an estate when a probate proceeding relating to such matter is already pending in that court and over "any cause of action in which a personal representative of an estate pending in the statutory probate court is a party." *Id.* at *2 (citing TEX. PROB. CODE ANN. §5(f), (h) (Vernon 2003 & Supp. 2008). Because the Texas Probate Code defines "appertaining" and "incident" to an estate as "generally all matters relating to the collection, settlement, partition, and distribution of estates of deceased persons" and any cause of action appertaining or incident to an estate *shall* be brought in a statutory probate court, the appellate court held that the district court erred in exercising jurisdiction over a suit to enforce the settlement agreement. *Id* at *2.

C. Legally Enforceable

The issue whether an agreement is binding or legally enforceable is a question of law. *See Montanaro*, 946 S.W.2d at 430 *citing Texaco, Inc. v. Pennzoil Co.*, 729 S.W.2d 768, 814 (Tex. App. – Houston [1st Dist.] 1987, writ ref'd n.r.e.), *cert. dism'd*, 485 U.S. 994, 108 S.Ct. 1305, 99 L.Ed.2d 686 (1988); *Huffco Petroleum Corp. v. Trunkline Gas Co.*, 769 S.W.2d 672, 674 (Tex. App. – Houston [14th Dist.] 1989, writ denied); *Southwestern States Oil & Gas Co. v. Sovereign Resources, Inc.*, 365 S.W.2d 417, 419 (Tex. Civ. App. – Dallas 1963, writ ref'd n.r.e.). Therefore, unless there is ambiguity or unless surrounding facts and circumstances demonstrate a factual issue as to the settlement agreement, the issue whether the agreement fails for lack of an essential term is a question of law to be determined by the court. *See Browning v. Holloway*, 620 S.W.2d 611, 615 (Tex. Civ. App. – Dallas 1981, writ ref'd n.r.e.). In doing so, the court may consider evidence of the facts and circumstances surrounding its execution. *See Montanaro*, 946 S.W.2d 428, 430 *citing Sun Oil Co. v. Madeley*, 626 S.W.2d 726, 731 (Tex. 1981). When the evidence shows the parties intended to enter into a settlement agreement, courts must enforce the agreement. *See Montanaro citing* TEX. CIV. PRAC. & REM. CODE ANN. §§ 154.003, 154.071 (Vernon 2008); *Matter of Ames*, 860 S.W.2d at 592. In reaching its determination, the court will decide whether all the essential terms were included in settlement agreement and all conditions precedent to the enforcement of the agreement have occurred.

If, however, the agreement is ambiguous that creates an unresolved issue of fact, the party challenging the agreement may be entitled to a jury trial on any unresolved fact issues. For example, in *Martin v. Black*, 909 S.W.2d at 196, the court considered whether a term sheet reached at mediation and signed by all parties was an enforceable settlement agreement. At issue was the final term which provided that "the parties' understandings are

subject to securing documentation satisfactory to the parties." *Id*. at 194. The court held that a question of fact existed regarding whether the parties intended the execution of formal documentation to be a condition precedent to the formation of a contract or a memorialization of an existing contract. *Id. citing Foreca, S.A. v. GRD Development Co. Inc.*, 758 S.W.2d 744, 746 (Tex. 1988). When no fact issue exists, however, the court may find as a matter of law that the agreement is enforceable notwithstanding the fact that the agreement contemplated circulation of final settlement documentation. *See Hardman v. Dault*, 2 S.W.3d 378 (Tex. App. – San Antonio 1999, no pet.) (parties' agreement not "subject to" execution of subsequent documents).

D. Breach of Contract

A party to a written settlement agreement may seek to enforce the agreement under general contract law. This right applies to both Rule 11 agreements, *see Stevens v. Snyder*, 874 S.W.2d at 243, and mediation agreements, *see Cadle Co. v. Castle*, 913 S.W.2d 627, 630 (Tex. App. – Dallas 1995, writ denied).

The party seeking to enforce the settlement agreement will typically bring suit to enforce the contract alleging breach of contract or seeking specific performance. *See Stevens*, 874 S.W.2d at 243. The original petition should contain a short statement of the cause of action sufficient to provide fair notice of the claim, including a statement regarding the contractual relationship between the parties and the substance of the settlement agreement. *See Cadle Co*, 913 S.W.2d at 631 *citing Air & Pump Co. v. Almaquer*, 609 S.W.2d 309, 313 (Tex. Civ. App. – Corpus Christi 1980, no writ); 14 TEX. JUR. 3D Contracts § 338 (1981). Defenses to a breach of contract suit may include (i) lack of capacity, (ii) denial of execution, (iii) lack of consideration, (iv) usury, (v) condition precedent, (vi) accord and satisfaction, (vii) duress, (viii) fraud, (ix) illegality, (x) satisfaction and accord and (xi) mistake. While a general denial may be sufficient to deny liability in certain cases, many defenses in a breach of contract lawsuit must be verified. *See* TEX. RUL. CIV. P. 93. And any affirmative defenses of "accord and satisfaction, duress, failure of consideration, fraud, illegality, statute of frauds, and other matters in avoidance must be affirmatively pleaded accord and satisfaction, duress, failure of consideration, fraud, illegality, statute of frauds, and other matters in avoidance must be affirmatively pleaded." *See Id. citing* TEX. RUL. CIV. P. 94.

Each party is entitled to pretrial discovery. Parties are "entitled to full, fair discovery" and to have their cases decided on the merits. *Ford Motor Co. V. Castillo,* 279 S.W.3d 656 (Tex. 2009) (citing *Able Supply Co. v. Moye*, 898 S.W.2d 766, 773 (Tex.19950 (orig. proceeding); *see State v. Lowry*, 802 S.W.2d 669, 671 (Tex.1991) ("Only in certain narrow circumstances is it appropriate to obstruct the search for truth by denying discovery."). In *Ford Motor Co.*, a defendant settled a claim when the jury sent a note to the court asking "what is the maximum amount that can be awarded. After the jury was released, the majority of the jurors told the defense lawyers that they had decided one liability question in the defendant's favor when the presiding juror sent the note without the other jurors knowledge. The defendant sought to delay settlement on the basis of potential jury influence and later sought to set aside the settlement on the grounds of mutual mistake. After the appellate court upheld the trial court's granting of a motion for summary judgment in the plaintiff's favor, Texas Supreme Court reversed and remanded the matter back to the trial court, noting that a "trial court abuses its discretion when it denies discovery going to the heart of a party's case or when that denial severely compromises a party's ability to present a viable defense." *Id.* at 663(citing *Able*, 898 S.W.2d at 772.

When no material issue of fact exists, a party is entitled to summary judgment. But, the party moving for summary judgment should make sure he has amended his pleadings to assert a breach of contract claim if filed in the original lawsuit. And, if an issue of material fact exists, a party may request a jury trial. *See Id*. at 631 *citing Trinity Universal Ins. Co. v. Ponsford Bros.*, 423 S.W.2d 571, 575 (Tex. 1968). To preserve the right to a jury trial, the litigant must timely request a jury trial and preserve his record. *See Ashmore v. Smith*, 2004 WL 1171717 (Tex.App.—Austin 2004, n.p.h.)(memorandum opinion)(party waived right to jury trial on enforcement of contract because he only sought jury trial on original underlying issues and not on validity of agreement).

At trial, the plaintiff must be prepared to prove "(1) a contract existed between the parties; (2) the contract created duties; (3) the defendant breached a material duty under the contract; and (4) the plaintiff sustained damage." *Id*. at 631 *citing Snyder v. Eanes Indep. Sch. Dist.*, 860 S.W.2d 692, 695 (Tex. App. – Austin 1993, writ denied).

E. Contempt of Court

The court may render an agreed judgment on a settlement agreement. *See* TEX. CIV. PRAC. & REM CODE ANN. § 154.071 (Vernon 2008). The entry of an enforceable agreed judgment requires the continued consent of all parties at the time the judgment is rendered, and (ii) the entry of an agreed

judgment which literally complies with the terms of the settlement agreement.

Any party may revoke their consent prior to the time the court renders judgment. *See S&A Restaurant Corp. v. Leal*, 892 S.W.2d 855 (Tex. 1995) *citing Quintero v. Jim Walter Homes, Inc.*, 654 S.W.2d 442, 444 (Tex. 1983); *Samples Exterminators v. Samples*, 640 S.W.2d 873, 874-75 (Tex. 1982). It is important to recognize the distinction between the approval of a settlement and the *rendering* of a judgment. *See S&A Restaurant*, 892 S.W.2d at 858. In *S&A Restaurant*, the Texas Supreme Court found that the approval of a settlement agreement does not constitute the entry, or rendering, of a judgment and, thus, a party to the agreement could revoke their consent and preclude the entry of an agreed judgment. *Id*. at 858; *but see Reppert*, 943 S.W.2d at 174 (oral pronouncement that court "accepted and approved" agreement and made "it a judgment of the court" render judgment). The entry of an agreed judgment after a party revokes their consent is void. *Id*. at 857 *citing Samples*, 640 S.W.2d at 875.

Further, the proposed judgment must "literally comply with the terms of the agreement." *See Tinney v. Willingham*, 897 S.W.2d 543 (Tex. App. – Fort Worth 1995, no writ) *citing Wyss v. Bookman*, 235 S.W.2d 567, 569 (Tex. Comm'n App. 1921, holding approved); *Vickery v. American Youth Camps, Inc.*, 532 S.W.2d 292 (Tex. 1976). Failure to meet this requirement renders the judgment unenforceable. *See Tinney*, 897 S.W.2d at 544 *citing Vickery*, 532 S.W.2d at 292.

F. Statute of Limitation

As a general rule, a party to a settlement agreement has four (4) years to seek to set aside the agreement, on the basis of fraud or otherwise. *See Johnston v. Barnes*, 71 S.W.2d 164, 165 (Tex. App. – Houston [14th Dist.] 1986, no writ); *see also* Helen Wils, STATUTES OF LIMITATION IN PROBATE AND TRUST LITIGATION, 23rd Adv. Est. Plan. & Prob. Course.

XV. CHECKLISTS

A. Generally

Most settlements are reached at the end of a long and grueling day of mediation. Counsel is then left with the dilemma of agreeing to exchange settlement documents at a later date (after some sleep) or drafting feverishly into the night. The first option allows for "buyers remorse" and the second often leads to later construction disputes. Both options and possible results should be explained to a client. In the end, however, most clients prefer to secure a binding agreement (that may later require construction) than leave without the basic deal. To assist the weary and malnourished lawyer, a checklist is attached to assist the drafting lawyers.

Note that the following lists are non-exclusive and are meant to be for illustration purposes only. The actual facts and circumstances of the case (which in probate and trust litigation are always unique) should dictate the actual provisions and agreements.

B. Will Contests

The following is a basic checklist for settlement of a will contest:

A. Parties
- State all names
- State all relevant capacities (i.e. executor, trustee, etc.)
- Define appropriately (make sure definition includes all capacities)

B. Recitals
- Identify decedent and date of death
- State facts giving rise to contest or dispute
- State facts evidencing each settling party's standing and validity of his or her claim
- Identify pending legal action, including court, style of case, etc.
- State settlement to avoid continued litigation and buy peace

C. Definitions and scope
- Define claims
- Define relevant entities and persons included in settlement, i.e. trusts, businesses, etc.
- State what claims or matters, if any, are excluded from agreement
- Define relevant terms – including successor, affiliates, predecessors, litigation, transactions, etc.

D. Recite consideration
- Good and valuable
- Other payments provided under terms negotiated

E. Terms of settlement
- Division of estate assets
  - ⇒ Describe property each person or party to receive
  - ⇒ Time to deliver
  - ⇒ Manner to divide – bid, lots, etc.
  - ⇒ Whether appraiser must be obtained and, if so, who is responsible
  - ⇒ Who pays shipping and delivery costs

- ⇒ Who pays/responsible for storage and insurance pending distribution
- ⇒ Should a bill of sale be prepared and, if so, who prepares
- ⇒ Who prepares deeds for real property
- ⇒ How disputes should be settled
- ⇒ Disclaimers or assignments
- ⇒ Method to divide unknown, undisclosed or lost assets

- Continued administration of estate
  - ⇒ Who will be appointed or continue to serve as the personal representative of the estate
  - ⇒ Limitation on personal representative's powers, if any
  - ⇒ Reporting requirements to parties or third parties
  - ⇒ Time period to close estate
  - ⇒ Payment of fees and expenses
  - ⇒ Right to compensation
  - ⇒ Responsibility to execute conveyance documents
- Waiver of statutory rights
  - ⇒ Homestead
  - ⇒ Family allowance
  - ⇒ Exempt property

F. Taxes and debts
- Who is responsible for preparing and filing last income tax return, any gift tax returns and death tax returns
- Surviving spouse's responsibility to pay income taxes for period prior to spouse's death
- Who is responsible for payment of taxes, penalties and interest
- How and when debts and administration expenses will be paid
- Who is responsible for payment of debts and administration expenses
- Disclosures as to known debts and taxes due
- Tax apportionment – residuary, Section 322A, otherwise
- Will parties be entitled to request copy of death and income tax return
- Right to access tax records and, if so, periods to be provided
- Indemnity for income, death, and gift taxes and related penalties and interest
- Payments do not constitute distributable net income to recipient
- How will court costs and appointee fees be paid

G. Representations
- Capacity of parties
- Disclosure of assets
- Authority to act in stated capacity
- Party has not assigned, pledged or disclaimed interest
- Discharge any reliance on statement by any other party's attorney or advisor
- Include disclaimer of reliance other than expressly stated in written settlement agreement

H. Release and indemnities
- Release claims
- Limitations in release of parties and/or attorney or other advisors if desired
- Exclude obligations under settlement agreement from release
- Verify all required parties are releasing and being released in all desired capacities
- Verify successor, affiliates and predecessor are released, if desired
- Verify all agents, heirs, etc. are bound
- Indemnities for taxes, third party claims, tenant claims, environmental claims, alleged spouses, etc.

I. Disposition of litigation
- Dismissal with prejudice
- Consent judgment
- Time to dispose
- Who is responsible for preparation of paperwork
- Rights of counsel to review
- Whether parties must attend hearing

J. Remedies in default
- Settlement agreement enforced as contract
- Settlement agreement to be incorporated in judgment and enforced accordingly
- Specific performance
- Right to attorneys fees and expenses

K. Miscellaneous
- Agreement supersedes any oral or prior agreements (exclude any agreements to remain in effect)
- Agreement must be modified in writing
- Choice of law
- Incorporate exhibits
- Advice of own counsel
- Whether agreement can be executed in multiple counterparts
- Whether facsimile signature same as original

- Where future notices should be sent
- Confidentiality agreement
- Heading and titles are for descriptive purposes only
- Agreement to mediate/arbitrate future disputes
- Statement that parties and counsel in good faith and just cause
- Effective date
- Court approvals

C. Trust Suits

The following is a basic checklist relating to a lawsuit involving the administration, modification, or termination of a trust:

A. Parties
- State all names
- State all relevant capacities
- Define appropriately
- State how minors and unknown beneficiaries are bound
- State any ad litems joining as parties

B. Recitals
- Identify trust or trusts at issue
- Identify trustees
- State facts giving rise to contest or dispute
- State facts evidencing each settling party's standing and validity of his or her claim
- Identify pending legal action, including court, style of case, etc.
- State settlement to avoid continued litigation and buy peace

C. Definitions and scope
- Define claims
- Define relevant entities and persons included in settlement, i.e. other trusts, partnerships, businesses, etc.
- State what claims or matters, if any, are excluded from agreement
- Define relevant terms – including successor, affiliates, predecessors, litigation, transactions, etc.

D. Recite consideration
- Good and valuable
- Other payments provided under terms negotiated

E. Terms of settlement
- Resignation of Trustee
  - ⇒ Basis for resignation
  - ⇒ Time for resignation
  - ⇒ Any contingent events or actions
  - ⇒ Appoint successor trustee
  - ⇒ Means to qualify
  - ⇒ Who must bring suit to seek appointment, if necessary
- Distribution standard issues
  - ⇒ How future distributions will be determined
  - ⇒ Documentation beneficiaries must submit to support future distributions
  - ⇒ Property to be distributed in settlement of claims for failure to distribute sufficient amounts in past
  - ⇒ Whether payments are from income or principal
  - ⇒ How past, current and future payments will be accounted for
- Disclosure, discharge and redress
  - ⇒ Disclosures of Books, Records and Accounts
  - ⇒ Successor trustee has no duty to redress
  - ⇒ Judicial accounting
  - ⇒ Indemnify successor trustee from claims of unknown or minor beneficiary or third parties
  - ⇒ Time and place books and records will be made available
- Breach of fiduciary duty
  - ⇒ Payment from fiduciary to trust and/or beneficiary
  - ⇒ Return of trustee fees and expenses paid by trust
  - ⇒ Return of compensation by trustee
  - ⇒ Whether payment to trustee and property taken by trustee will constitute income to trustee
  - ⇒ Note or other means to secure payments
- Continued administration of trust
  - ⇒ Who will be appointed or continue to serve as the trustee of the trust
  - ⇒ Future reporting requirements to parties or third parties
  - ⇒ Payment of trustee's fees and expenses
  - ⇒ Right to compensation

F. Termination or modification of trust
- Termination
  - ⇒ Basis for termination
  - ⇒ Means to terminate – agreement or by court
  - ⇒ Who prepares paperwork and pleadings
  - ⇒ Payment of any debt, obligations and taxes

- ⇒ How pending debts, notes, leases, contracts or other obligations will be handled
- ⇒ Tax effects of termination – income and GST

- Modification
  - ⇒ Provision to be modified
  - ⇒ Basis for modification
  - ⇒ Means to modification – agreement or by court
  - ⇒ Who prepares paperwork and pleadings
  - ⇒ Tax implications
  - ⇒ GST considerations

G. Tax matters
- Consider tax implications
- Obtain tax opinions
- Request private letter rulings
- Who is responsible for filing tax returns
- Whether distributions will take into account the amount of taxes the beneficiary must pay
- Will settlement result in loss of GST "grandfathered" status

H. Representations
- Capacity of parties
- Disclosure of assets
- Authority to act in stated capacity
- Party has not assigned, pledged or disclaimed interest
- Discharge any reliance on statement by any other party's attorney or advisor
- Include disclaimer of reliance other than expressly stated in written settlement agreement

I. Release and indemnities
- Release claims
- Limitations in release of parties and/or attorney or other advisors
- Exclude from release obligations under settlement agreement
- Verify all required parties release and are released in all desired capacities
- Verify successor, affiliates and predecessor are released, if desired
- Verify all agents, heirs, etc. are bound
- Indemnities for taxes, third party claims, tenant claims, environmental claims, alleged spouses, etc.

J. Disposition of litigation
- Dismissal with prejudice
- Consent judgment
- Time to dispose
- Who is responsible for preparation of paperwork
- Rights of counsel to review
- Whether parties must attend hearing

K. Remedies in default
- Settlement agreement enforced as contract
- Settlement agreement to be incorporated in judgment and enforced accordingly
- Specific performance
- Right to attorneys fees and expenses

L. Miscellaneous
- Agreement supersedes any oral or prior agreements (exclude any agreements to remain in effect)
- Agreement must be modified in writing
- Choice of law
- Incorporate exhibits
- Advise of own counsel
- Whether agreement can be executed in multiple counterparts
- Whether facsimile signature same as original
- Where future notices should be sent
- Confidentiality agreement
- Heading and titles are for descriptive purposes only
- Agreement to mediate/arbitrate future disputes
- Effective date
- Court approvals, if any

D. Guardianship Suits

The following is a basic checklist for settlement of a guardianship contest:

A. Parties
- State all names
- State all relevant capacities
- Define appropriately
- State any ad litems joining as parties

B. Recitals
- Identify guardianship matters at issue
- State facts giving rise to contest or dispute
- State facts evidencing each settling party's standing
- Identify pending legal action, including court, style of case, etc.
- State settlement to avoid continued litigation and buy peace

C. Definitions and scope
- Define claims
- Define any released entities and persons included in settlement, i.e. other trusts, partnerships, businesses, etc.
- State what claims or matters, if any, are excluded from agreement
- Define relevant terms – including successor, affiliates, predecessors, litigation, transactions, etc.

D. Recite consideration
- Good and valuable

E. Appointment of guardian
- General issues
  - ⇒ Will guardian be appointed – person and/or estate
  - ⇒ If not, ward competent or less restrictive means
  - ⇒ Validity of POA, trust, etc., HCPOA
  - ⇒ If guardian appointed, who will be appointed guardian – person and/or estate
  - ⇒ Hearing and who will attend
  - ⇒ Waiver by anyone with priority to serve permanent/limited
  - ⇒ Who serves as representative payee for social security
  - ⇒ Provision to appoint future guardians
  - ⇒ Notice of future appointments
  - ⇒ Bond requirements
  - ⇒ Guardian's compensation
  - ⇒ Continued appointment of ad litem(s)
  - ⇒ Who prepares paperwork and time frame to do so
  - ⇒ Parties' right to be involved in future hearings
  - ⇒ Living arrangements
  - ⇒ Funeral arrangements – right to plan
- Property issues
  - ⇒ Agreements as to ward's community or separate property
  - ⇒ Rights of spouse to manage community property - 883 or otherwise
  - ⇒ Partition or exchange agreement
  - ⇒ Guardian's authority to manage community estate
  - ⇒ Annual gifting – allowed and notice requirements
  - ⇒ Notice of sales or significant transfers
  - ⇒ Guardian's compensation
  - ⇒ Payment of fees and expenses
  - ⇒ Coordination with any trusts or other entities
  - ⇒ Rights of parties to access and audit guardian's books and records
  - ⇒ Expenses to be paid by guardian versus wife, trustee or other third party
  - ⇒ Right to divorce ward
  - ⇒ Homestead rights
  - ⇒ Who pays ad litem and applicant's fees and expenses

F. Termination or modification of guardianship
- Termination
  - ⇒ Basis for termination
  - ⇒ Who prepares paperwork and pleadings
  - ⇒ Payment of any debt, obligations and taxes
  - ⇒ Ad litem's consents
  - ⇒ Doctor's letter or other medical opinion
- Modification
  - ⇒ How guardianship will be modified
  - ⇒ Basis for modification
  - ⇒ Doctor's letter or other medical opinion
  - ⇒ Who prepares paperwork and pleadings
  - ⇒ What powers will ward have
  - ⇒ What powers will guardian have

G. Representations
- Capacity of parties
- Disclosure of assets
- Authority to act in stated capacity
- Discharge any reliance on statement by any other party's attorney or advisor
- Include disclaimer of reliance other than expressly stated in written settlement agreement

H. Release and indemnities
- Release claims
- Limitations in release of parties and/or attorney or other advisors
- Exclude release for obligations under settlement agreement
- Verify all required parties release and are released in all desired capacities
- Verify successor, affiliates and predecessor are released, if desired
- Verify all agents, heirs, etc. are bound
- Indemnities for third party claims

I. Disposition of litigation
- Dismissal with or without prejudice
- Time to dispose
- Who is responsible for preparation of paperwork
- Who must execute written waivers

- Who must withdraw/dismiss contests
- Rights of counsel to review
- Whether parties must attend hearing

J. Remedies in default

- Settlement agreement enforced as contract
- Settlement agreement to be incorporated in judgment and enforce accordingly
- Right to attorneys fees and expenses

K. Miscellaneous

- Agreement supersedes any oral or prior agreements (exclude any agreements to remain in effect)
- Applicant for guardianship was in good faith and just cause
- Agreement must be modified in writing
- Choice of law
- Incorporate exhibits
- Advise of own counsel
- Whether agreement can be executed in multiple counterparts
- Whether facsimile signature same as original
- Where future notices should be sent
- Heading and titles are for descriptive purposes only
- Agreement to mediate/arbitrate future disputes
- Effective date
- Court approvals, if any

XVI. SAMPLE SETTLEMENT AGREEMENTS

(See Attached Exhibits)

EXHIBIT A

RULE 11 & SETTLEMENT AGREEMENT

THE STATE OF TEXAS §
§
COUNTY OF HARRIS §

THIS SETTLEMENT AGREEMENT ("this Agreement") is entered into by and among _____, _____, _____, and the respective heirs, personal representatives, executors, directors, officers, partners, affiliates, administrators, successors, agents, attorneys and assigns of each of them, as evidenced by their signatures affixed hereto. The preceding persons are sometimes collectively referred to herein as "the Parties" and individually referred to as "a Party." The term "Decedent's Estate" shall refer to all probate and non-probate property in which _____had an ownership interest in or claim to as of the date of her death.

W I T N E S E T H :

WHEREAS, _____("Decedent") died on _____, in Houston, Texas;

WHEREAS, Decedent was a resident of Houston, Harris County, Texas, at the time of his death;

WHEREAS, Decedent had two children: _____ and _____;

WHEREAS, on _____, _____ filed an Application for Probate and Issuance of Letters Testamentary seeking to admit the purported Will of Decedent dated _____;

WHEREAS, on _____, _____filed a Petition in Intervention for the purpose of opposing the probate of the alleged Last Will & Testament of the Decedent dated _____and claiming to be the Decedent's surviving spouse;.

WHEREAS, on _____, _____ filed a Petition in Intervention for the purpose of opposing the probate of the alleged Last Will & Testament of the Decedent dated _____.

WHEREAS, _____, _____ and _____survived the Decedent by the statutory period and are Parties to this agreement;

WHEREAS, Decedent executed a prior will dated _____;

WHEREAS, a dispute exists between the Parties and as to the validity of the testamentary instruments executed by Decedent;

WHEREAS, the Parties wish to resolve all differences and disputes between them in order to avoid further litigation and expense and to make peace; and

WHEREAS, by executing this Agreement no Party hereto concedes any legal or factual contentions of any other Party or makes any admissions but, rather, each Party denies any contrary contention made by any other Party and enters into this Agreement solely to terminate and settle their differences in an effort to minimize costs, expenses, and ongoing attorney's fees.

NOW, THEREFORE, FOR GOOD AND VALUABLE CONSIDERATION, including the mutual agreements, understandings, stipulations, representations, and releases set forth herein, the sufficiency of such consideration being hereby acknowledged and confessed by each of the Parties hereto, make the following representations and agreements:

1. Decedent's Testamentary Instruments. Each Party represents to every other Party that he or she is not aware of any testamentary instruments executed or alleged to have been executed by Decedent that remained in existence and effective at the time of her death other than the Will and the Codicil.
2. Decedent's Estate. Each Party represents to each other Party, to the best of his or her knowledge, there are no properties, real or personal, belonging to Decedent as of her date of death other than the assets disclosed on Exhibit A attached to this agreement.
3. Probate of Decedent's Will and Codicil. The Parties agree that _____ shall be admitted to probate.
4. Appointment of Personal Representative of Decedent's Estate. _____ shall be appointed as the sole Independent Executor of the Estate of the Decedent. The other Parties agree to execute and return immediately any necessary documents indicating their consent to _____'s appointment as the Independent Executor or personal representative of Decedent's probate estate.
5. Distribution of Estate Assets. The Parties agree that all of Decedent's property, being all real and personal property the Decedent had an interest in or claim to at time of her death including, but not

limited to the property listed on Exhibit A, shall pass subject to the terms of this Agreement. The Property shall be distributed as follows:

a. _____ shall receive the total sum of _____ in cash and _____. _____ shall receive such assets in full and final settlement of their interest in the Decedent's Estate. The Parties agree that the _____ shall deliver a check payable jointly to _____ and his counsel in accordance with the terms of this Agreement.

b. _____ shall receive the total sum of _____ in cash and _____. _____ shall receive such assets in full and final settlement of their interest in the Decedent's Estate. The Parties agree that the _____ shall deliver a check payable jointly to _____ and his counsel in accordance with the terms of this Agreement. _____ waives, renounces and disclaims any right she may have to seek a family allowance pursuant to Section 286, et seq., of the Texas Probate Code, or otherwise.

c. _____ shall receive the rest and remainder of Decedent's estate (being all assets other than the total sums passing to _____ and _____ under the this Agreement.

d. _____ shall pay and deliver to _____ and _____, the property and checks in payment of the amount and assets due them under this Agreement contemporaneously with the receipt of a court order authorizing this agreement (or authorizing the issuance of a check in accordance with this Agreement). The delivery of the assets shall be in full and final settlement of _____ and _____ interest in the Decedent's estate.

e. The Parties agree and confirm that all distributions and/or property passing to _____ and _____ and any other amounts passing to _____ and _____under the terms of this Settlement Agreement shall be treated for income tax purposes as a settlement of a claim and/or as a gift or bequest of "a specific sum of money or of specific property" not payable in installments and are not punitive, not for services rendered, and no portion represents income or interest relating to such specific sum of money; *i.e.*, none of the distributions will constitute distributable net income to _____ and _____.

8. Conveyance Documents. In order to effectuate the conveyance of all of Decedent's interest in the property passing pursuant to the terms of this Agreement (described in Exhibit A or otherwise), the parties shall deliver to any other parties all such requisite executed documentation, deeds, bill of sales and stock transfers as may be necessary complete the division of the Decedent's estate in compliance with this Agreement. All the Parties shall also shall also cooperate with each other to facilitate the delivery of any assets to any other party under the terms of this Agreement.

9. Administration of Decedent's Estate. _____, as the personal representative of Decedent's estate, will have sole authority over and responsibility for the administration of the Decedent's estate including, but not limited to, the preparation and filing of any of Decedent's income and gift tax returns, all death tax returns and all fiduciary income tax returns, as may be due, and the distribution of estate assets to himself as the sole beneficiary of the Decedent's estate. _____ represents that he will properly file all returns and provide for the payment of any related taxes. _____ does h hereby INDEMNIFY, DEFEND and HOLD HARMLESS _____and _____, from any and all liability, transferor, transferee or otherwise, (i) relating to ___ serving as personal representative of Decedent's Estate, including any and all past, current or future federal or state income gift or death taxes, and any related interest and penalties which may be claimed, or assessed, relating to Decedent's Estate, (ii) relating to any and all past, current or future federal or state income, gift or death taxes, including any interest, and penalties, imposed by reason of the distributions provided for in this Agreement, and (iii) arising from all claims, costs, expenses, including but not limited to attorneys fees and expenses, accountant fees and expenses, experts, litigation costs and bond premiums, relating to any attempt by the Internal Revenue Service or other persons or entities to assess, collect or enforce any claims, demands, assessments or judgments against _____ or _____, for past, current or future federal or state income, gift or estate taxes, and any related penalties and interest.

10. Release. Each Party, for themselves and their lineal heirs, beneficiaries, assigns, representative, agents and descendants, hereby forever release and discharge each other Party, individually, and in all capacities, and their respective heirs, personal representatives, executors, affiliates, officers, directors, partners, administrators, successors, agents, attorneys, and assigns of and from any and all liabilities, claims, and causes of action including, but not limited to, tortious interference with inheritance rights, tortious interference with contracts, tortious interference with business relations, physical, mental, or emotional distress, any gifts made by Decedent, will contests, claims of conflict of interest, claims against attorneys, accountants, fiduciaries or agents, unjust enrichment, the administration of the estate or the guardianship of the Decedent, all claims which were or could have been made in currently pending litigation, fraudulent concealment, rights of reimbursement, exempt property, fraud, fraud on the community, theft, undue influences, misappropriation, breach of fiduciary duty, and any other statutory rights and demands and causes of action of any kind and/or character, whether **known or unknown**, fixed or contingent, liquidated or unliquidated, whether or not asserted, arising out of or any way connected with any act, omission or event related to any Party and/or the Decedent's Estate, the guardianship of the Decedent, and the Revocable Trust, save and except for the representations, warranties, obligations under this Agreement.
11. Party's Attorneys Fees and Expenses. Each Party hereby agrees to be responsible for his or her own respective attorney's fees, costs, and expenses through the date of this Agreement, including their respective attorney's fees, costs, and expenses necessary and/or incurred in the effectuation of this Agreement. The Parties further agree that if it becomes necessary to assert any claim to enforce or defend the provisions of this Agreement, the prevailing Party shall be entitled to recover reasonable attorney's fees and other related litigation expenses from the non-prevailing Party.
12. Representations. Each Party makes the following representations to each other Party:
    a. The representing Party is legally competent to execute this Agreement and that this Agreement is valid, binding and enforceable.
    b. The representing Party believes that Decedent did not properly execute any right of survivorship or pay on death agreements or other agreements relating to the creation of non-probate assets and that any such agreements or contracts are void and of no effect and that any non-probate assets are an assets of Decedent's probate estate and pass pursuant to the terms of this Agreement.
    c. The representing Party owns the claims released herein and has not assigned, released, waived, relinquished, pledged or in any manner whatsoever, sold or transferred, his or her interest, right, and/or claims to or against the Decedent, Decedent's estate, except to his or her attorneys.
    d. **Each party confirms and agrees that such party (i) has relied on his or her own judgment and has not been induced to sign or execute this Agreement by promises, agreements or representations not expressly stated herein, (ii) has freely and willingly executed this Agreement and hereby expressly disclaims reliance on any fact, promise, undertaking or representation made by the other party, save and except for the express agreements and representations contained in this Agreement, (iii) waives any right to additional information regarding the matters governed and effected by this Agreement, (iv) was not in a significantly disparate bargaining position with the other party. and (v) has been represented by legal counsel in this matter.**
13. Entire Agreement. The provisions of this Agreement constitute the entire Agreement between the Parties, and supersede all previous negotiations and documents. No oral modification shall be binding upon either Party. The terms hereof are contractual in nature and are not mere recitals, and shall be binding upon the heirs, spouses, descendants, executors, administrators, successors, representatives, and assigns of the Parties hereto, upon complete execution by the Parties.
14. Construction. All Parties acknowledge and agree that all the Parties have participated in the drafting of this Agreement and no one Party shall be considered the drafter of this Agreement and, therefore, no presumptions shall be made for or against any other Party on the basis that any one Party was the drafter of this Agreement.
15. Multiple Counterparts. This Agreement may be executed in multiple counterparts, each of which shall be deemed an original for all purposes.
16. Effective Date. This Agreement shall be effective as of the last to occur of the following the date that

the last Party executes this Agreement.

17. Choice of Laws. This Agreement shall be construed and interpreted in accordance with the laws of the State of Texas.

EXECUTED on _____, 200__.

_____

_____, Individually, and in all capacities

_____

_____, Individually, and in all capacities

[*add jurat/acknowledgement*]

EXHIBIT "A"

LISTING OF ASSETS

EXHIBIT B

BENEFICIARY DISTRIBUTION AGREEMENT

THE STATE OF TEXAS §
§
COUNTY OF HARRIS §

THIS AGREEMENT ("this Agreement") is entered into by and among _____ ("_____"), _____ ("_____"), _____ ("_____"), _____ ("_____") and _____ ("_____"), and the respective heirs, personal representatives, executors, administrators, successors, agents, attorneys and assigns of each of them, as evidenced by their signatures affixed hereto. The preceding persons are sometimes collectively referred to herein as "the Parties" and individually referred to as "a Party." The term "Decedent" shall refer to _____ and the term "Decedent's Estate" shall refer to all probate and non-probate property in which _____ had an ownership interest in or claim to as of the date of his/her death.

W I T N E S S E T H :

WHEREAS, the Decedent died on _____, in _____ County, Texas;

WHEREAS, Decedent's wife/husband, _____ ("_____"), died on _____;

WHEREAS, prior to his/her death, Decedent arranged for _____'s Will to be admitted to probate;

WHEREAS, Decedent left a valid Last Will and Testament ("Will") that has been admitted to probate in the above-referenced proceeding. A copy of the Will is attached as Exhibit A to this Agreement;

WHEREAS, Decedent's Will provides that each of the Parties is entitled to _____ of Decedent's estate subject to probate administration;

WHEREAS, it has been determined that _____ is or was in possession of assets of the Decedent's Estate that have not been delivered to the Administrator to date, and he/she acknowledges that such assets should be treated as an advance toward his/her interest in the Decedent's Estate;

WHEREAS, it has been determined that _____ has received _____ without Administrator's permission, and he/she acknowledges that such amounts should be treated as an advance toward his/her interest in the Decedent's Estate;

WHEREAS, the Parties agree that all assets of the Decedent's Estate that were in the possession of any Party and that have not been delivered to the Administrator to date shall be treated as an advance toward his or her interest in the Decedent's Estate;

WHEREAS, the Parties survived the Decedent by the statutory period and are Parties to this agreement;

WHEREAS, issues exist between the Parties regarding the amounts and/or assets due the Decedent's Estate from some of the Parties and, thus, the remaining interest of each Party in the Decedent's Estate after taking into account advancements and assets retained by such Party;

WHEREAS, the Parties wish to resolve all differences and disputes between them in order to avoid further litigation and expense and to make peace; and

WHEREAS, by executing this Agreement no Party hereto concedes any legal or factual contentions of any other Party or makes any admissions but, rather, each Party denies any contrary contention made by any other Party and enters into this Agreement solely to terminate and settle their differences in an effort to minimize costs, expenses, and ongoing attorney's fees.

NOW, THEREFORE, FOR GOOD AND VALUABLE CONSIDERATION, including the mutual agreements, understandings, stipulations, and representations set forth herein, the sufficiency of such consideration being hereby acknowledged and confessed by each of the Parties hereto, make the following representations and agreements:

1. Decedent's Testamentary Instruments. Each Party represents to every other Party that he or she is not aware of any testamentary instruments executed or alleged to have been

executed by Decedent that remained in existence and effective at the time of her death other than the Will attached as Exhibit A to this Agreement.

2. Decedent's Estate. Each Party represents to each other Party that to the best of his or her knowledge, there are no properties, real or personal, belonging to Decedent as of her date of death other than the assets disclosed on Exhibit B attached to this agreement.
3. Agreed Advancements. The Parties acknowledge that the Decedent's Estate shall be distributed to each of the Parties as set forth in the Will but enter into this agreement to settle all disputes regarding assets of the Decedent's Estate that have been advanced to or retained by one or more of the Parties to this Agreement. Therefore, the Parties agree that certain assets have been distributed to some of the Parties to date and that such distribution and/or receipt shall be treated as an advancement of such stated Party's _____ interest in the Decedent's Estate as follows:
   (a) *: The Parties acknowledge and agree that * has received the following assets as an advancement of his/her interest in the Decedent's Estate and such assets/amounts shall reduce his _____ share of the Decedent's Estate:
      i) * has received cash in the total amount of $_____. A reconciliation of the cash received by * and the debts and other offsets is attached as Exhibit C to this Agreement;
      ii) * has received the Decedent's _____ with an agreed value of $_____;
      iii) * has received the Decedent's ◊ with an agreed value of $_____;
      iv) * has received the Decedent's ◊◊ with an agreed value of $_____;
      v) * has received the Decedent's ◊◊◊ with an agreed value of $_____;
      vi) * has received a court-approved advancement of $_____ in cash from the Administrator;
   (b) **: The Parties acknowledge and agree that ** has received the following assets of the Decedent's Estate and such assets/amounts shall reduce his/her one-_____ share of the Decedent's Estate:
      i) ** has received the Decedent's _____ with an agreed value of $_____;
      ii) ** has received a court-approved advancement of $_____ in cash from the Administrator;
   (c) ***: The Parties acknowledge and agree that *** has received the following assets of the Decedent's Estate and such assets/amounts shall reduce his/her _____ share of the Decedent's Estate:
      i) *** has received a court-approved advancement of $_____ in cash from the Administrator;
   (d) ****: The Parties acknowledge and agree that **** has received the following assets of the Decedent's Estate and such assets/amounts shall reduce his/her _____ share of the Decedent's Estate:
      i) **** has received cash in the total amount of $_____ via the pay-off of a loan due by **** and paid off after the Decedent's death with cash on deposit at _____ in the Decedent's accounts;
      ii) **** has received a court-approved advancement of $_____ in cash from the Administrator;
   (e) *****: The Parties acknowledge and agree that ***** has received the following assets as an advancement of his/her interest in the Decedent's Estate and such assets/amounts shall reduce his/her _____ share of the Decedent's Estate:
      i) ***** has received a court-approved advancement of $_____ in cash from the Administrator;
4. Agreements as to Distribution of the Real Properties. The Parties acknowledge that the Decedent's Estate includes real estate and that they would prefer for such real property to be distributed as they may agree among themselves. The Parties agree that (i) the real properties have been appraised by a court appointed real estate appraiser, (ii) he or she has received a copy of the appraisal from Administrator, and (iii) such appraised values shall

be used for purposes of determining each property's distribution value. The Parties further agree that the real property shall be distributed as between the Parties as follows:

(a) All of the Decedent's interest in the real property, including improvements, commonly known as _____, _____, Texas, having an appraised value of $_____, shall be distributed to ** as a part of his/her one-_____ interest in the Decedent's Estate;

(b) All of the Decedent's interest in the real property, including improvements, commonly known as _____, _____, Texas, having an appraised value of $_____, shall be distributed to ** as a part of his/her one-_____ interest in the Decedent's Estate;

(c) All of the Decedent's interest in the real property, including improvements, commonly known as _____, _____, Texas, having an appraised value of $_____, shall be distributed to ** as a part of his/her one-_____ interest in the Decedent's Estate;

(d) All of the Decedent's interest in the real property, including improvements, commonly known as _____, _____, Texas, having an appraised value of $_____, shall be distributed to **** as a part of his/her one-_____interest in the Decedent's Estate;

5. Distribution of Remaining Assets. The Parties acknowledge that the Administrator will distribute the remaining assets of the Decedent's Estate, after payment of all remaining debts, administration expenses, legal and accounting fees, in a manner that equalizes each Party's _____ interest in the Decedent's Estate, taking into account the agreed advancements and distributions set forth in Paragraphs 3 and 4 of this Agreement. The value of such remaining assets shall be as of date of distribution. The Parties further agree that they will agree as among themselves the division of any remaining household furnishings and personal effects. The Parties agree that Administrator shall have no further obligation to pursue assets in any of the Parties possession and control and that this Agreement is intended to settle all claims of each Party relating to assets of the Decedent's Estate in any other Party's possession and/or control, including claims of property due the Decedent's Estate and for return of assets.

6. Conveyance Documents. In order to effectuate the conveyance of all of Decedent's interest in the property passing pursuant to the terms of this Agreement (described in Exhibit B or otherwise), the Parties shall deliver to any other Parties all such requisite executed documentation, deeds, bill of sales and stock transfers as may be necessary to complete the division of the Decedent's estate in compliance with this Agreement. All the Parties shall also cooperate with each other and Administrator to facilitate the delivery of any assets to any other Party under the terms of this Agreement.

7. Release of Administrator. The Parties acknowledge that they have entered into this Agreement to resolve all pending issues regarding each of the Parties interest in the Decedent's Estate and the assets taken, stolen, and/or received by certain Parties but not others. The Parties request that Administrator rely on this Agreement in settling Decedent's Estate and distributing Decedent's assets as provided herein. The Parties further release and discharge Administrator from any claims relating to her compliance with this Agreement, including but not limited to ceasing collection efforts regarding property that may be due the Decedent's Estate, the determination of the assets in any Party's possession or control, and the distribution values determined for Estate assets.

8. Party's Attorneys Fees and Expenses. With regard to each Parties' legal fees and expenses:

(a) _____ agrees to be responsible for any and all of his/her attorney's fees, costs, and expenses through the date of this Agreement, including his/her attorney's fees, costs, and expenses necessary and/or incurred in the effectuation of this Agreement and hereby waives any right to seek further reimbursement from Decedent's Estate, Administrator or any other Party.

(b) Administrator shall be entitled to reimbursement of his/her legal fees from Decedent's Estate but waives any right to seek reimbursement from any other Party.

(c) The Parties further agree that if it becomes necessary to assert any claim to enforce or defend the provisions of this Agreement, the prevailing Party shall be entitled to recover reasonable attorney's fees and other related litigation expenses from the non-prevailing Party.

9. Representations. The Parties to this Agreement make the following representations to such other Parties:
   (a) Each Party represents to the other Parties that he or she is not aware of any assets of the Decedent's Estate other than those assets listed on Exhibit B to this Agreement;
   (b) Each Party represents to the other Parties that he/she is not aware of any cash, dividend, rents, or other assets of the Decedent's estate than is not accounted for on Exhibit C;
   (c) The representing Party is legally competent to execute this Agreement and that this Agreement is valid, binding and enforceable;
   (d) The representing Party believes that Decedent did not properly execute any right of survivorship or pay on death agreements or other agreements relating to the creation of non-probate assets and that any such agreements or contracts are void and of no effect and that any non-probate assets are an assets of Decedent's probate estate and pass pursuant to the terms of this Agreement;
   (e) The representing Party owns the claims released herein and has not assigned, released, waived, relinquished, pledged or in any manner whatsoever, sold or transferred, his or her interest, right, and/or claims to or against the Decedent, Decedent's estate, except to his or her attorneys;
   (f) **Each Party confirms and agrees that such Party (i) has relied on his or her own judgment and has not been induced to sign or execute this Agreement by promises, agreements or representations not expressly stated herein, (ii) has freely and willingly executed this Agreement and hereby expressly disclaims reliance on any fact, promise, undertaking or representation made by any other Party or Administrator, save and except for the express agreements and representations contained in this Agreement, (iii) waives any right to additional information regarding the matters governed and effected by this Agreement, (iv) was not in a significantly disparate bargaining position with the other party. and (v) has been represented by legal counsel in this matter or has voluntarily waived such right; and**
   (g) Each Party confirms and agrees _____, and the law firm of _____, solely represent A and B and do not and have never represented any other Party and have not provided any other Party legal advice or services, or made any representation to any other Party;
   (h) Each Party confirms and agrees _____, and the law firm of _____, solely represent C and do not and have never represented any other Party and have not provided any other Party legal advice or services, or made any representation to any other Party;
   (i) Each of the Parties acknowledge and understand that the Administrator does not request his or her interest in matters relating to the Decedent's Estate, has not provided them legal advice and has not made any representations to him or her. Each Party further acknowledges that (i) Administrator has suggested that he or she retain counsel if they have any questions regarding the terms or effect of this Agreement, and (ii) each Party is relying on his or her own judgment in entering into this Agreement.

10. Entire Agreement. The provisions of this Agreement constitute the entire Agreement between the Parties, and supersede all previous negotiations and documents. No oral modification shall be binding upon either Party. The terms hereof are contractual in nature and are not mere recitals, and shall be binding upon the heirs, spouses, descendants, executors, administrators, successors, representatives, and assigns of the Parties hereto, upon complete execution by the Parties.

11. Construction. All Parties acknowledge and agree that all the Parties have participated in the drafting of this Agreement and no one Party or the Administrator shall be considered

the drafter of this Agreement and, therefore, no presumptions shall be made for or against any other Party on the basis that any one Party was the drafter of this Agreement.

12. Multiple Counterparts. This Agreement may be executed in multiple counterparts, each of which shall be deemed an original for all purposes.
13. Effective Date. This Agreement shall be effective as of the last to occur of the following the date that the last Party executes this Agreement.
14. Choice of Laws. This Agreement shall be construed and interpreted in accordance with the laws of the State of Texas.

EXECUTED on _____ day of _____, 20___.

_____
*
_____
_____

_____
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_____
****
_____
_____

_____
*****
_____
_____

[*add jurat/acknowledgement*]

EXHIBIT C

SAMPLE TRUST SETTLEMENT AGREEMENT

THIS SETTLEMENT AGREEMENT ("this Agreement") is made and entered into by and among (i) *, individually and in the fiduciary capacities described below, (ii) **, individually and in the fiduciary capacities discussed below; (iii) ***; (iv) ****; and (v) *****.

Article I: Definitions

1.1 The Parties to this Settlement Agreement are defined as follows:

a. The term "Mr./Ms. *" shall mean *, individually, as a beneficiary of and as trustee of the testamentary trusts created under the Last Will and Testament of ******, Deceased, and as the virtual representative of his issue.

b. The term "Mr./Ms. **" shall mean **, individually, as a contingent beneficiary, and as a co-trustee of the testamentary trusts created under the Last Will and Testament of ******, Deceased, and as the virtual representative of his/her issue.

c. The term "Mr./Ms. *****" shall mean *****, individually, as a beneficiary of the testamentary trusts created under the Last Will and Testament of ******, Deceased, and as the virtual representative of all persons and entities who may take under a power of appointment created under the Last Will and Testament of ******, Deceased, or who may take in default if the power of appointment is not executed.

d. The term "Mr./Ms. ****" shall mean ****, individually, as a beneficiary of the testamentary trusts created under the Last Will and Testament of ******, Deceased, and as the virtual representative of his/her issue.

e. The term "Mr./Ms. ***" shall mean ***, individually, as contingent beneficiary and successor trustee of the testamentary trusts created under the Last Will and Testament of ******, and as the virtual representative of his/her issue.

1.2 The terms "Affiliate" or "Affiliates" of the person or entity designated shall mean such person's or entity's spouse (including a former or future spouse), assigns, trustees, employees, attorneys (except as otherwise expressly provided herein), and accountants. It is expressly provided, however, that a reference to an Affiliate shall not include _____.

1.3 The term "this Agreement" or "the Agreement" shall refer to this Settlement Agreement, including all Exhibits attached hereto.

1.4 The term "******" shall refer to ******, the deceased husband of Mr./Ms. ***** and the testator with regard to Last Will and Testament of ******, Deceased.

1.5 The term "Claims" shall refer to and include any and all claims, including breach of fiduciary duty, negligence, gross negligence and any other ground, causes of action, and all other obligations and liabilities, which any Party or Parties have, may have, or have had against the released Party, including the claims brought or which could have been brought by, between or among the Parties through the effective date of the Agreement relating to the testamentary trusts created under the Last Will and Testament of ******, Deceased, including the Transactions. [It is expressly provided, however, that the definition of Claims shall not include any and all claims, including breach of fiduciary duty, negligence, gross negligence, causes of action, and all other obligations and liabilities, which any Party or Parties have, may have, or have had against _____.]

1.6 The term "Corporate Trustee" shall mean _____ as the duly appointed successor corporate trustee of Trust A and Trust B pursuant to the terms of this Agreement.

1.7 The term "Effective Date" means the date the last Party signs this Agreement.

1.8 The terms "the Parties" or "the Parties hereto" shall collectively refer to Mr./Ms. *, Mr./Ms. *****, Mr./Ms. **, Mr./Ms. **** and Mr./Ms. ***.

1.9 The term a "Party" shall refer to any one of Mr./Ms. *, Mr./Ms. *****, Mr./Ms. **, Mr./Ms. **** and Mr./Ms. ***.

1.10 The terms "Predecessor" or "Predecessors" shall refer to any person or entity serving prior in time as a fiduciary to the fiduciary in question.

1.11 The terms "Successor" or "Successors" shall refer to the heirs, devisees, descendants, legatees, executors, appointees under any power of appointment, personal representatives, successor trustees, and any successors of a Successor or Successors.

1.12 The term "Transactions" shall mean the following events:

(i) the resignation of Mr./Ms. * and Mr./Ms. **, as the co-trustees of Trust A and Trust B,

(ii) the written waiver of right by, and declination to serve of, Mr./Ms. ***, as a successor trustee of Trust A and Trust B,

(iii) the appointment of Corporate Trustee as successor trustee of Trust A and Trust B;

(iv) the distribution by the Trustees of the assets of Trust A and Trust B to Corporate Trustee;

(v) all other acts, transactions, and proceedings (including any failure to act) of any of the Trustees of Trust A and/or Trust B on or before the Effective Date; and

(vi) the negotiation and consummation of this Agreement.

It is expressly provided, however, that the definition of Transactions shall not include any and all actions or inactions, transactions or events of any nature, type, or description that has given rise to or could give rise at anytime to a claim by a Party against _____.

1.13 The term "Trust A" shall refer to the testamentary trust created under and commonly referred to as _____ in the Last Will and Testament of ******, Deceased.

1.14 The term "Trust B" shall refer to the testamentary trust created under and commonly referred to as _____ in the Last Will and Testament of ******, Deceased.

1.15 The terms "Trustee" or "Trustees," shall mean the Mr./Ms. * and Mr./Ms. ** as the currently appointed and duly acting co-trustees of Trust A and Trust B under the Last Will and Testament of ******, Deceased, and the Modification Judgment.

1.16 The term "trust estate" shall refer include all properties, real or personal, however and whenever acquired, and any income there from, which may belong, respectively, to (i) Trust A, and (ii) Trust B.

1.17 The term "Will" shall refer to the Last Will and Testament of ******, Deceased, and the First Codicil, attached as Exhibits A and B, respectively, to this Agreement, and incorporated by this reference.

Article II: Recitals

WHEREAS, ****** died on _____;

WHEREAS, Mr./Ms. *****, is the surviving spouse of ******;

WHEREAS, the Will directed the creation of Trust A and Trust B;

WHEREAS, Mr./Ms. *****, Mr./Ms. * and _____ were named as the original co-trustees of the Trust A and Trust B;

WHEREAS, Mr./Ms. ***** and Mr./Ms. * served as co-trustees of the Trusts until _____;

WHEREAS, Mr./Ms. * and Mr./Ms. ** currently serve as Trustees of Trust A and Trust B pursuant to the Modification Judgment;

WHEREAS, Mr./Ms. * has the power to appoint a corporate fiduciary as successor trustee of Trust A and Trust B, pursuant to the terms and conditions of the Modification Judgment;

WHEREAS, Mr./Ms. ***** has a general power of appointment over the assets remaining in Trust A at the time of his/her death;

WHEREAS, the named remainder beneficiaries of Trust B are Mr./Ms. *, _____ and Mr./Ms. ****;

WHEREAS, _____ died in _____ without any surviving issue;

WHEREAS, Mr./Ms. * and Mr./Ms. **** are the current remainder beneficiaries of Trust B;

WHEREAS, certain differences, controversies, and Claims have arisen by and between Mr./Ms. ***** and the Trustees regarding the administration of Trust A and Trust B;

WHEREAS, this Agreement is made to completely settle and compromise all differences, controversies, and Claims between some of the Parties;

WHEREAS, the Parties have determined that it is in their respective best interests to settle and terminate all Claims between them relating to the Trustees, Trust A, Trust B and/or the Transactions;

WHEREAS, the Parties wish to compromise any and all potential Claims they have between them relating to the Trustees, Trust A and Trust B and of the administrations of Trust A and Trust B through the Effective Date of this Agreement;

WHEREAS, Mr./Ms. *** and Mr./Ms. **** have agreed to join in this Agreement to indicate their consent to its terms and their agreement to be bound by its terms as set forth below;

WHEREAS, by executing this Agreement, no Party hereto concedes any legal or factual contentions of the other Party, but specifically denies same and enters into this Agreement solely to terminate and settle the Claims between themselves in an effort to minimize costs, expenses, attorneys' fees, and, most of all, to buy peace.

Article III: Agreements

For and in consideration of the premises, the mutual covenants and the terms hereunder, the sufficiency of which consideration is hereby mutually acknowledged, the Parties to this Agreement hereby agree as follows:

3.1 **Agreements With Respect To Trusts**

a. Trust A.

i) Trust A is defined as to its present contents and trust estate as the stocks, bonds, and other securities generally listed and described on Exhibits D and E to this Agreement, the same showing an estimated fair market values as of _____, of $_____.

ii) Delivery. Mr./Ms. * and Mr./Ms. ** agree to deliver to the Corporate Trustee of Trust A, within a reasonable time, not to exceed thirty (30) days following the Effective Date, the trust estate of Trust A. Mr./Ms. * and Mr./Ms. ** agree that any records of Trust A now in possession or control of either of them belong to Trust A and further agree to deliver all such records to Corporate Trustee within thirty (30) days from the Effective Date. Mr./Ms. * and Mr./Ms. ** may retain a copy of such records.

iii) Temporary Custody. Mr./Ms. * and Mr./Ms. ** agree to continue to maintain, but as custodian only, the assets of Trust A for up to thirty (30) days after the Effective Date, during which time they agree to arrange delivery of all of the assets of Trust A to Corporate Trustee as trustee of Trust A.

iv) Resignation of Trustee. In consideration for the agreements of the Parties in this Agreement, Mr./Ms. * and Mr./Ms. ** hereby agree to resign as the current Trustees of Trust A, such resignations to become irrevocable and effective as of the Effective Date; and upon the appointment of Corporate Trustee of Trust A. In the event that Corporate Trustee declines to serve as Corporate Trustee of Trust A, or after having been appointed, Corporate Trustee thereafter for any reason fails or ceases to serve as such Corporate Trustee, the successor corporate trustee of Trust A shall be selected jointly by Mr./Ms. * and Mr./Ms. *****. The successor corporate trustee of Trust A shall be a corporate trustee as defined by the Modification Judgment.

v) Waivers of Compensation. Mr./Ms. * and Mr./Ms. ** hereby waive all fees and commissions for serving as Trustees of Trust A.

vi) Rights of Reimbursement. Except for the payment of attorneys fees and expenses provided in this Agreement, Mr./Ms. * and Mr./Ms. ** hereby waive any claims from reimbursement from the assets of Trust A.

vii) Waiver of Right to and Declination to Serve. In consideration for the Agreement herein, Mr./Ms. *** agrees that he/she hereby irrevocably waives her right to be named or appointed as a trustee of Trust A throughout the remaining term of Trust A and any post-term of Trust A until the trust estate of Trust A, remaining at the death of Mr./Ms. *****, has been delivered to any person who takes pursuant to the exercise of the power of appointment, or, if the power is not exercised, pursuant to the terms of the Will.

viii) Beneficiaries of Trust A. The Parties hereto agree that Mr./Ms. ***** will continue to be the sole beneficiary of Trust A pursuant to the terms of the Will.

b. Trust B.

i) Trust B is defined as to its present contents and trust estate as the stocks, bonds, and other securities generally listed and described on Exhibits F and G to this Agreement,

the same showing an estimated fair market values as of _____, of $_____.

ii) Delivery. Mr./Ms. * and Mr./Ms. ** agree to deliver to the Corporate Trustee of Trust B, within a reasonable time, not to exceed ten (10) days following the Effective Date, the trust estate of Trust B. Mr./Ms. * and Mr./Ms. ** agree that any records of Trust B now in possession or control of either of them belong to Trust B and further agree to deliver all such records to Corporate Trustee within ten (10) days from the Effective Date. Mr./Ms. * and Mr./Ms. ** may retain a copy of such records.

iii) Temporary Custody. Mr./Ms. * and Mr./Ms. ** agree to continue to maintain, but as custodian only, the assets of Trust B for up to ten (10) days after the Effective Date, during which time they agree to arrange delivery of all of the assets of Trust B to Corporate Trustee as trustee of Trust B.

iv) Resignation of Trustee. In consideration for the agreements of the Parties in this Agreement, Mr./Ms. * and Mr./Ms. ** hereby agree to resign as the current Trustees of Trust B, such resignations to become irrevocable and effective as of the Effective Date; and upon the appointment of Corporate Trustee of Trust B. In the event that Corporate Trustee declines to serve as Corporate Trustee of Trust B, or after having been appointed, Corporate Trustee thereafter for any reason fails or ceases to serve as such Corporate Trustee, the successor corporate trustee of Trust B shall be selected jointly by Mr./Ms. * and Mr./Ms. *****. The successor corporate trustee of Trust B shall be a corporate trustee as defined by the Modification Judgment.

v) Waivers of Compensation. Mr./Ms. * and Mr./Ms. ** hereby waive all fees and commissions for serving as Trustees of Trust B.

vi) Rights of Reimbursement. Except for the payment of attorneys fees and expenses provided in this Agreement, Mr./Ms. * and Mr./Ms. ** hereby waive any claims from reimbursement from the assets of Trust B.

vii) Waiver of Right to and Declination to Serve. In consideration for the Agreement herein, Mr./Ms. *** agrees that he/she hereby irrevocably waives his/her right to be named or appointed as a trustee of Trust B throughout the remaining term of Trust B and any post-term of Trust B until the trust estate of Trust B, remaining at the death of Mr./Ms. *****, has been delivered to the remainder beneficiary or beneficiaries.

viii) Beneficiaries of Trust A. The Parties hereto agree that Mr./Ms. ***** will continue to be the sole current beneficiary of Trust B during his/her lifetime pursuant to the terms of the Will.

c. Miscellaneous. The Parties understand and agree to the terms and conditions of this Agreement;

i) That no Party shall pursue a claim or suit against another Party, individually, or in any fiduciary capacity, for any Claims arising out of matters set forth above in this Agreement, save and except for any claims relating to any breaches of warranties, representations, or obligations set forth in this Agreement.

ii) That each Party specifically waives any right to demand an accounting or audit of Trust A or Trust B.

iii) That the Corporate Trustee shall have not duty to redress the actions or inactions of any Predecessor trustee of either Trust A or Trust B including but not limited to, the Claims and the Transactions.

iv) That attorneys fees and expenses incurred through the Effective Date of this Agreement by Mr./Ms. *****, individually, and Mr./Ms. * and Mr./Ms. **, as Trustees of Trust A and Trust B, shall be reimbursement from the principal of the respective trusts as follows: (i) twenty percent (20%) shall be paid from the assets of Trust A and (ii) eighty percent (80%) shall be paid from the assets of Trust B. It is expressly agreed, however, that Mr./Ms. *****'s total attorneys fees and expenses to be paid from the trust estates shall not exceed $10,000. It is also expressly agreed that the total attorneys fees and expenses of Mr./Ms. * and Mr./Ms. **, as Trustees of Trust A and Trust B, to be paid from the trust estates shall not exceed $_____.

3.3 **Release Of Claims**

a. Each Party, individually and on behalf of his or her Affiliates and Successors, does hereby forever release and discharge all other Parties, and each of their Successors and Affiliates of and from any and all Claims including, but not limited to any Claims relating to the Transactions.

b. Notwithstanding the foregoing, no release under this Agreement shall be held to include:

i) a release of any obligation owed or representation made pursuant to the terms of this Agreement by any Party to any other Party hereto, or

ii) a release of _____.

3.4 **Representations And Warranties**

a. Each Party hereby stipulates, represents and warrants to each of the other Parties, as follows:

i) That he or she is the current legal and beneficial owner of all of the Claims released hereby, as well as the Claims asserted by him or her orally or in written form with respect to any litigation he or she could have brought with respect to matters covered by this Agreement, including the Claims and Transactions;

ii) That he or she has not assigned, pledged or contracted to assign or pledge to any other person or entity any interest he or she may have in Trust A or Trust B or under the Will;

iii) That the terms and provisions of this Agreement are valid, binding and enforceable as against himself or herself, any such Party's Successors and Affiliates;

iv) That he or she is adequately represented by competent counsel of his or her choosing in connection with the execution and delivery of this Agreement and in any and all matters relating thereto, or has voluntarily waived such right to seek the advice of a legal advisor;

v) That he or she is not under any form of legal disability or incapacity at the time he or she executes this Agreement;

vi) That _____, and the law firm of _____, solely represent Mr./Ms. ***** and do not and have never represented any other Party and have not provided any other Party legal advice or services, or made any representation to any other Party;

vii) That _____, and the law firm of _____, solely represent Mr./Ms. * and Mr./Ms. ** and do not and have never represented any other Party and have not provided any other Party legal advice or services or made any representations to any other Party;

viii) That in executing this Agreement, each Party has relied upon his or her own judgment and the advice of his or her own attorneys, and further, that he or she has not been induced to sign or execute this Agreement by promises, agreements or representations not expressly stated herein, and he or she has freely and willingly executed this Agreement and expressly disclaims reliance upon any facts, promises, undertakings, or representations made by any other Party, or by such Party's Affiliates;

ix) That the consent of such Party to this Agreement was not procured, obtained or induced by improper conduct, undue influence or duress;

x) That such Party either (1) has knowledge of all relevant and material information and facts and has been fully informed, including by advice of counsel, concerning the existence of potential Claims or any other Party including other additional affirmative or defensive Claims arising from all matters known to him or her and arising during the period of negotiations leading to and culminating in the execution by him or her of this Agreement, in order for him or her to make an informed and considered decision to enter into this Agreement, and/or (2) specifically and after advice of counsel is waiving (a) any right to obtain or demand, and (b) any obligation of any other Party;

xi) That he or she is not in a significantly disparate bargaining position with regard to any other Party.

b. Each Party understands and agrees that each other Party has relied upon these representations and warranties in entering into this Agreement.

3.5 **Miscellaneous Provisions**

a. Parties Bound. This Agreement shall be binding upon and shall inure to the benefit of the Parties hereto and their respective Affiliates and Successors.

b. Party's Attorney's Fees and Expenses Incurred to Date. Except as otherwise provided in this Agreement, each Party hereby agrees to be responsible for his or her own respective attorney's fees, costs, and expenses through the date of this Agreement, including their respective attorney's fees, costs, and expenses necessary and/or incurred in the effectuation of this Agreement.

c. Attorney's Fees and Expenses for Breach of Agreement. The Parties agree that if it becomes necessary to assert any claim to enforce or defend the provisions of this Agreement, the prevailing Party shall be entitled to recover reasonable attorney's fees and other related litigation expenses from the non-prevailing Party. Notwithstanding any provision to the contrary, the Corporate Trustee of Trust A and Trust B shall have the right to seek payment of its reasonable and necessary attorney's fees and expenses from the respective trust estate in accordance with the Will.

d. No Oral Modification. No amendment, modification, waiver, or consent with respect to, any provision of any of this Agreement shall be effective unless the same shall be in writing and signed by the Party or Parties hereto against whom enforcement of the amendment, modification, waiver or consent is sought.

e. Counterparts. This Agreement may be executed simultaneously in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute a single instrument. This Agreement shall only be binding when one or more counterparts hereof, individually or taken together, shall bear all signatures of the Parties hereto reflected hereon as signatories.

f. Choice of Law. This Agreement shall be governed pursuant to the laws of the State of Texas.

g. Choice of Venue. _____ County, Texas shall be the appropriate and exclusive venue for any suit arising out of this Agreement.

h. Assignment. This Agreement and the rights and obligations of the Parties hereto shall not be assigned or delegated by any Party hereto without the prior written consent of the other Parties hereof.

i. Incorporation. All Exhibits attached hereto are hereby incorporated by reference in this Agreement for the purposes set forth above.

j. Headings. The paragraph headings and sub-headings used herein are for descriptive purposes only. The headings have no substantive meaning and the terms of this Agreement shall not be affected by such headings.

THIS WRITTEN AGREEMENT REPRESENTS THE FINAL AGREEMENT AMONG THE PARTIES HERETO AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS, OR SUBSEQUENT ORAL OR WRITTEN AGREEMENTS BETWEEN OR AMONG ONE OR MORE OF THE PARTIES HERETO.

PARTIES:

_____

*, Individually and as Co-Trustee of Trust A and Trust B created under the Last Will & Testament of ******, Deceased, and Virtual Representative of his/her Issue

_____

, Individually and as Co-Trustee of Trust A and Trust B created under the Last Will & Testament of ****, Deceased, Individually, as a contingent beneficiary of any trust created under the Last Will & Testament of ******, Deceased, and Virtual Representative of his/her Issue

_____

, as the successor named Trustee of Trust A and Trust B created under the Last Will & Testament of ***, Deceased, Individually, as contingent beneficiary of any trust created under the Last Will & Testament of ******, Deceased, and Virtual Representative of his/her Issue

_____

*****, Individually, as a beneficiary of any trust created under the Last Will & Testament of ******, Deceased, and as the virtual representative of all persons and entities who may take under a power of appointment created under the Last Will and Testament of ******, Deceased, or who may take in default if the power of appointment is not executed

_____

****, Individually, as a beneficiary of any trust created under the Last Will & Testament of ******, Deceased, and Virtual Representative of his/her Issue

[*add jurat/acknowledgement*]