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Challenging the Validity of the Revocable Trust -

The revocable trust continues to be touted as a worthy Will substitute. Unscrupulous planners will insure the hapless client that the trust will save estate taxes, leaving the, albeit unspoken, implication, that a last Will and Testament cannot accomplish the same goal.

Other arguments for the preference of the revocable trust are the avoidance of probate and its attendant cost; its administration outside the supervision of the court secrecy- and, finally, the avoidance of having to notify distributees of the decedent's plan of asset distribution upon his death. The last reason is to accomplish two goals: 1) one need not worry about serving a citation upon distributees who are hard to find and 2) those overlooked by decedent's largesse cannot object.

Emphatically, a Will can accomplish the same estate tax saving as a revocable trust. The usual revocable trust is created by the grantor for his own life-time benefit. With the abolishment of the merger doctrine in New York', the grantor may serve as sole trustee as well as sole income beneficiary, provided one or more other persons hold a beneficial interest in the trust. The grantor will reserve the right to amend and revoke the instrument, which power, if not released during his lifetime, will cause the entire trust property to be part of his taxable estate upon death'. Accordingly, from an estate tax viewpoint, the grantor of a revocable trust is in the same situation as if he had created a last Will and Testament.

It is true that the cost of probate will usually exceed that for the winding up of a decedent's revocable trust, but attorney's fees for the creation of the trust and the cost of conveyance of the assets into the trust, as well as the trust's administration during the

grantor's life time, should be kept in mind.

Nevertheless, there are circumstances which properly may cause counsel to recommend the creation of a revocable trust, rather than a last Will and Testament. If the client owns real property in more than one state, ancillary probate proceedings can be avoided. Furthermore, we have all encountered the client who has lost touch with all family members and has no idea how to gather family tree information, nor any inclination to do so. The revocable trust may be especially recommended when the client plans to disinherit some or all of his distributees and a Will contest may be expected. This last reason is a compelling one.

Experience has taught us that the overlooked heir has no compunction about delaying the probate process. He will settle in for a lengthy discovery period and pepper counsel for the proponent of the Will with the standard objections. Often unfounded, the objections challenge the Will on the grounds that the testator lacked testamentary capacity; that the Will was not executed in accordance with the required testamentary formalities; undue influence was exercised upon the testator and the instrument was the product of fraud and duress'.

An untidy, but lawful, extortion process will unfold and the fiduciary must make his Hobson's choice: pay off the disinherited or expend precious estate assets to vanquish their arguments. Does the revocable trust protect the estate from this unhappy development?

Statutory Requirements

With the proliferation of revocable trusts, has come the inevitable challenge to their validity and the path to challenge is becoming clearer. First, the trust may be questioned on the grounds that it was not executed in accordance with the required statutory formalities. EPTL 7-1.174 now requires that a trust be in writing, signed by the grantor and at least one trustee unless the grantor is the sole trustee. Even a trust executed prior to the effective date of the statute may fail lesser standards of required formality, because contained in a three-ring looseleaf binder, with pages easily removable.' Signatures must be acknowledged, in the form required for the recording of a conveyance of real property

or, in lieu thereof, executed in the presence of two witnesses who shall affix their signatures to the trust instruments. The acknowledgment itself may be subject to challenge, if not in compliance with §309-a of the Real Property Law. If the acknowledgment is affixed after September 1, 1999, it must comply with the new, uniform acknowledgment statute.

Trusts created on or after December 25, 1997 are valid as to any assets therein to the extent the assets have been transferred to the trust.¹ The transfer of real property, cash and securities into the trust is easily documented, but what of the grantor's jewelry, coin collection, antique furniture and the like? Where the grantor is also the sole trustee, "transfer shall mean...a written assignment describing the asset with particularity".² Where the grantor is not the sole trustee, presumably, there must be delivery with intent to transfer into the trust in accordance with prior case law. Clearly, the procedural requirements of this statute present some ammunition for the creative challenger of the trust.

The Heart of the Matter

The creator of the trust must have the necessary capacity. As we know, something less than capacity to contract is required for the testator to create a valid Last Will and Testament? The trust, however, purports to be a species of contract. Should capacity to contract be required to uphold the trust? One Surrogate has referred to the "illusory concept of a revocable trust as a contract." While a trust is established in the form of an agreement, "it is really unilateral in nature because the negotiation that characterizes bilateral instruments is totally absent".³ This reasoning has led to prayers to set aside both decedent's Will and trust on the grounds of, inter alia, lack of capacity.⁴ As the proceeding to set aside the trust is an equitable one, there is disagreement among the courts as to whether the right to trial by jury on the issue is available.⁵ The right to a jury trial on a claim of lack of testamentary capacity is statutory when the validity of decedent's Will is at issue.⁶

The usual accompaniments to a claim of lack of capacity are those of fraud and undue influence and the revocable trust is open to challenges on those grounds as well.⁷

The prayer for relief is a pleading. One claimant cited, inter alia, tortious interference with trust by means of the exercise of undue influence, "although a cause of action based on tortious interference with prospective inheritance is not recognized in New York State.¹⁶ Aside from the customary claims of lack of capacity, fraud, duress and undue influence, we see, inter alia, bank irregularities leading to improper revocation of Totten Trust;" invalid amendment by one creator of a trust following the death of another. '\$

The Appropriate Forum

The Surrogate's Court now has jurisdiction over lifetime trusts pursuant to SCPA §1509 and SCPA §207. Jurisdiction is co-extensive with that exercisable by Supreme Court.

Notwithstanding the "illusory" contractual nature of a revocable trust, common law still regards the trust as a species of contract. Accordingly, equitable relief to set aside the agreement may be sought in Supreme Court.

The case may be commenced in Supreme Court and, under appropriate circumstances, transferred to Surrogate's Court. In Matter of the Estate of Aronoff, 171 Misc.2d 172, Surr. Ct., N.Y. Cty., 1996, supra, petitioners commenced a proceeding in Supreme Court seeking to set aside the trust. Objectants moved to transfer the proceeding to the Surrogate's Court and to consolidate it with a pending probate proceeding.

Commonly, the Surrogate's Court is the forum of choice. The decedent may have created both a revocable trust and a so-called pour-over Will, providing that the residuary be conveyed to the trustees of the trust and the assets administered in accordance with its terms.⁹

Standings and How to Proceed

The Court, in Estate of Davidson, 177 Misc.2d 928, Surr. Ct., N.Y. Cty., 1998, supra, likened the challenge to the validity of the revocable trust to the one questioning the validity

of a Last Will and Testament and concluded that a distributee who is entitled to file objections to probate should also be accorded standing to commence an action to set aside a revocable trust.

As in the Will contest, excluded beneficiaries will complain. The Settlor himself, since armed with the power of revocation, customarily does not need to avail himself of the Courts". The creator of a revocable trust, now suffering incapacity, may be able to seek redress through his guardian 2', as should the personal representative of a grantor induced to enter into the agreement by fraud or undue influence²². Clearly, however, the issue of standing will be fact specific.

In the pour-over will scenario, the nominated executor proponent of the Will and the trustee of the revocable trust is usually the same person; often the person who is alleged to have been instrumental in diverting the assets.

In such a case, the objectants to the validity of the trust can seek an appointment as limited temporary fiduciaries for the purpose of commencing a discovery proceeding against the nominated executor on the ground that the executor cannot pursue a claim against himself, [SCPA § 702 (10)]²³, as is suggested by the Court in Estate of Tisdale, 171 Misc. 2d 716 (Surr. Ct., N.Y. Cty., 1997), supra. The Court observed that a proceeding to set aside a revocable trust is like a discovery proceeding in that the relief sought is recovery of estate assets allegedly wrongfully transferred. The classical situation arose in Matter of Estate of Davidson, 177 Misc. 2d 928, supra, where decedent's disinherited distributee sought limited letters of administration pursuant to SCPA § 702 [9] in order to commence a discovery proceeding against the trustee of decedent's revocable trust, who was also the nominated executor of her Will. The Court opined that the statute's purpose is to authorize the appointment of a limited fiduciary where the acting fiduciary has a conflict of interest and, accordingly, the Court issued limited letters to the petitioner.

To complete this brief discussion, the Court's explanation in Estate of Aronoff, 171 MISC 2d 172 (Surr. Ct., N.Y. Cty., 1996), supra, is helpful; the Court noting that customarily, a fiduciary will bring a discovery proceeding to recover legal title for ultimate disposition as determined by the applicable governing instrument, or law, as the case may be. There, the decedent excluded two of his children as beneficiaries of his Last Will and Testament and

his revocable trust. The offended parties objected to probate and sought to set aside the trust. The Court drew a distinction between the fiduciary seeking to recover assets on behalf of the estate and the objectants before it, who were seeking recovery of assets as intestate distributees, suggesting the objectants might use a "reverse discovery proceeding" in such a case.

Conclusion

Although the revocable trust continues to afford more protection to potential questioning of its validity than a Last Will and Testament, as we have seen, its very analogy to the last Will and Testament also leads to the inescapable avenues to set it aside. In addition, secrecy, much valued by some clients, is a casualty, as the trust agreement becomes an official Court document upon legal protest.

In advising the client, who, nevertheless, will choose the trust to dispose of his assets, counsel may wish to instruct the client to create a clear defense of ratification. Although the issue of ratification has not received a great deal of attention,²⁴ this potential defense should not be overlooked. The client's revocable trust will be well served by a well documented history of purposeful administration in which the client himself takes an active part; a defense never available to the proponent of decedent's last Will and Testament.

Finally, counsel should heed the Court's cautionary note sounded in Estate of Pozarny, 177, Misc. 2d 752, supra, about making use of pre-packaged living wills, heavily promoted throughout New York State, and take the time to draft the documents with care.

1. EPTL §7-1.1.

2. IRC §2038 (a)(1).

SCPA §1404; Children's Aid Society v. Loveridae, 70 N.Y. 387 (1877); Matter of

Bianco, 195 A.D. 2d 457 (2d Dept. 1993); Matter of Evanchuk, 145 A.D. 2d 559 (2d Dept. 1988).

- 4 . Laws of 1997, c. 139, §7 provides that: "this act shall take effect immediately [June 25, 1997] and shall apply to lifetime trusts created on and after such date, provided, however, that Sections 7-1.117 and 7-1.18 of the estates, powers and trusts law added by Section three of this act shall take effect six months after it shall have become a law [December 25, 1997]."
- 5 . Estate of Pozarny, 177 Misc. 2d 752 (Surr. Ct., N.Y. Cty., 1998).
- 6 . EPTL §7-1.17(a).
EPTL §7-1.18.
- 8 . EPTL §7-1.18.
- 9 . Matter of Coddington, 281 A.D. 143, aff'd 307 N.Y. 181 (1954).
- 10 . Matter of Estate of Tisdale, 171 Misc. 2d 716; 720 (Surr. Ct., N.Y. Cty., 1997).
- 11 . Matter of Estate of Davidson, 177 Misc. 2d 928 (Surr. Ct., N.Y. Cty., 1998);
Matter of Estate of Tisdale, 171 Misc. 2d 716, supra; Matter of Estate of Aronoff, 171 Misc. 2d 172, (Surr. Ct., N.Y. Cty., 1996).
- 12 . Matter of Estate of Tisdale, 171 Misc. 2d 716, supra; Matter of Estate of Aronoff, 171 Misc. 2d 172, supra, c.f. Matter of Mary Richman, Surr. Ct., Queens Cty., N.Y.L.J. 4/26/2000, p. 31, col. 6.
- 13 . SCPA §502 [1]; cf. Matter of Estate of Tisdale, 171 Misc. 2d 716, supra.
- 14 . Matter of Estate of Davidson, 177 Misc. 2d 928, supra; Matter of Estate of Tisdale, 171 Misc. 2d 716, supra; Matter of Estate of Aronoff, 171 Misc. 2d 172, supra.
- 15 . Zeff v. Weisman, 209 A.D. 2d 612, (2d Dept. 1994).
- 16 . Vogt v. Witmeyer, 87 N .Y. 2d 998 (1996).
- 17 . Hucko v. Apple Bank for Savings, 210 A.D. 2d 39 (1st Dept. 1994).
- 18 . Gaig_al v. Laub, 236 A.D. 2d 362, ap. den. 90 N.Y.2d 802 (1997), holding that the power of revocation reserved by joint creators "during lifetime" terminated upon first creator's death. (Analogous to a joint and mutual Will situation).
- 19 . See e.g. Estate of Pozarny, 177 Misc. 2d 725, supra; Estate of Davidson, 177 Misc. 2d 928, supra; Estate of Bourget, 175 Misc. 2d 144 (Surr. Ct., Nassau Cty., 1997); Estate of Tisdale, 171 Misc. 2d 716, supra.

- 20 . But see Tabor v. Bristol, 236 A.D. 2d 841(4th Dept. 1997). Action by Settlor of revocable trust against Co-Trustee who refused to turn over real property after the trust was revoked.
21. Matter of Rebecca Derechin, Surr. Ct., Nassau Cty., N.Y.L.J. 4/26/2000, p. 32, co, l. 5.
- 22 . Estate of Davidson, 177 Misc. 2d 928, supra, and its thorough discussion of the issue citing, inter alia, Petrie v. Chase Manhattan Bank, 31 N .Y. 2d 856, mod. 33 N.Y. 2d 846 (1973).
- 23 . The "catch-all" provision of SCPA §702
- 24 . Kazaras v. Manufacturers Trust Co., 156 N.Y.S. 2d 275, aff'd 4 A.D. 2d 227, aff'd 4 Ky. 2d 930 (1958), dealing, however, with an irrevocable trust.