August 2014

ESTATE PLANNING

Maximize Basis to Reduce Income Tax

Succession Planning for European Assets

Administering Estate's Personal Property

estate tax treaties between the U.S. and a Member State will continue to apply in determining tax liabilities to the U.S. and the applicable Member State.

Creation, administration, and dissolution of trusts. The Regulation also does not apply to questions regarding the creation, administration, and dissolution of trusts. The exclusion of trusts from succession proceedings under the Regulation is important because U.S. citizens use trusts frequently as part of their estate plan.

However, while a court of a Member State will not issue a decision under the Regulation pertaining to the creation, administration, and dissolution of a trust, the law selected in a will should determine whether assets will pass under the will to a trust. According to the Preamble:

> Questions relating to the creation, administration and dissolution of trusts should also be excluded from the scope of this Regulation. This should not be understood as a general exclusion of trusts. Where a trust is created under a will or under a statute in connection with intestate succession the law applicable to the succession under this Regulation should apply with respect to the devolution of the assets and the determination of the beneficiaries.[75]

Thus, if the law applicable to the succession recognizes trusts, such law should enforce testamentary provisions that create trusts or transfer assets to a trust. Accordingly, a U.S. citizen who wants property located in a Member State to be transferred, administered, and disposed of under a trust should consider executing a will that selects the law of the U.S. as the law governing succession because U.S. law recognizes trusts and enforces bequests to trusts. The will of a U.S. citizen governed by U.S. law could bequeath property to a testamentary trust under the will, and the bequest should not fail even though the law of the Member State in which the deceased citizen's property is located does not recognize trusts. The will could also contain provisions permitting the testamentary trust to merge or combine with a substantially similar trust, which would allow the trustee of the testamentary trust to ultimately merge or combine that trust with a trust established by the deceased citizen under a revocable or irrevocable trust created by the deceased citizen in the U.S.

Conclusion

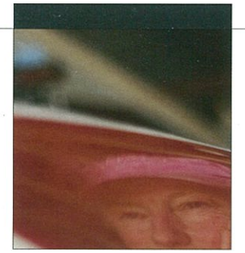
The Regulation's goal of reducing complexity of successions in the EU by having one jurisdiction apply one law in administering a succession should have a substantial impact in the 25 EU countries that adopted the Regulation. Estate planners who have U.S. citizen clients with property located in one or more Member States will need to consult the Regulation in connection with the disposition of property in Member States after 8/16/2015.

A U.S. citizen can execute a will that selects U.S. law to govern the succession of property located in one or more Member States. Consequently, the succession law of those Member States, including any forced heirship rules, will not govern the disposition of that property *unless* that property is either rights *in rem* or "immovable property, certain enterprises or other special categories of assets" that are subject to special distribution rules irrespective of the law applicable to the succession.

If a U.S. citizen has a habitual residence in a Member State, then the Member State will have jurisdiction over the entire succession. As discussed above, however, if the citizen's habitual residence at death is determined to be in the U.S. rather than in a Member State and the citizen has property located in two or more Member States at death, the citizen's estate may have to commence separate succession proceedings in each Member State in which such property was located at death, even though the citizen's will selects U.S. law to govern the succession of such property. Thus, the one forum goal of the Regulation may not apply in those circumstances.

Although the Regulation should make it easier to transfer a deceased citizen's property located in a Member State, the death tax consequences of that transfer will still be governed by other applicable law such as treaties between the U.S. and a Member State. Furthermore, the creation, administration, and dissolution of trusts are not covered by the Regulation, so when a U.S. citizen wants to bequeath property located in a Member State to a trust, the citizen should consider selecting the law of the U.S. as the law governing the succession, especially if the law of the Member State having jurisdiction over such property does not recognize trusts. ■

[75] Preamble ¶ 13.



Heirs and Heirlooms Can Create Hurdles in Estate Administration

The treasures and trash that comprise the personal property of an estate may create emotional responses that complicate estate administration.

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One of the most challenging aspects of administering an estate can be dealing with personal property—the tangible items that Mom, Dad, or Grandma left behind. This article addresses the many issues confronted by fiduciaries, beneficiaries, lawyers, and the courts when trying to determine how to distribute a decedent's personal property. It will also offer suggestions about how to avoid, or at least manage, some of the most contentious issues when administering an estate.

Personal property can include automobiles, jewelry, tools, art collections, furniture, personal papers, holiday ornaments, and all other kinds of possessions that individuals collect in order to keep up with the Joneses, fuel the consumer economy, and connect to the past.

Personal property may include valuable antiques. It may include a treasure trove of family history and memories. It may include a boatload of worthless tchotchkes or, even worse, piles of moldy or infested refuse that provide a sad window into a hoarding pathology or cognitive decline.

Executors, personal representatives, or trustees may face many confounding issues when dealing with personal property. In most estates, gathering assets, paying expenses, making distributions, and filing an account are fairly straightforward administrative tasks. Refereeing who gets the cardboard Santa Claus (true story) is much more difficult.

The personal property may have modest economic value. The time and expense of dealing with the personal property, however, may very well exceed that value. But when emotions percolate after the death of a family member, the personal property—and disputes over personal property—can become symbolic of these emotions. Very often these issues are more volatile than family feuds over just money. Beneficiaries can often be unduly sentimental about tangible stuff after the death of a loved one. These items can be a happy reminder of childhood, a link to the deceased, or a memento to pass on to the next generation. These items also can be pawns in a power play between siblings or other beneficiaries where, right or wrong, taking a coveted item settles some type of score.

Of course, sometimes disputes over personal property stem from good old-fashioned greed.

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Communicating and honoring decedent's wishes

The primary role of a fiduciary is to honor the intent of the testator or settlor. When a will enumerates

specific bequests to specific people, the fiduciary should do everything he or she can to ensure that the designated beneficiary receives the designated property. Making distributions is easier when Uncle Benny specifically bequeaths his tools to Ella, his bike collection to Eddy, and his boat to Miles. If specific bequests are itemized in a will, the fiduciary must make those bequests and do what he or she can to obtain cooperation from interested parties.

A testator may not know what personal property will be in his or her estate when he or she executes an estate plan. Grandpa may decide to sell his taxidermy collection or Grandma may decide to gift her jewelry during her lifetime. Between the date of the will and the date of death, the testator may downsize or may accumulate many more possessions.

Many estate planners will instruct testators to list specific bequests in a written memorandum separate from the provisions in the will. The will typically directs the executor or personal representative to make the gifts listed in the memorandum. The memorandum is a guide, and fiduciaries and families who play well together will typically respect the gifts enumerated in the memorandum. However, unless the memorandum satisfies the requirements for the execution of a will, it is not a will, may not be enforceable, and may be vulnerable to allegations of fraud, lack of capacity, and undue influence.

If a testator is particularly concerned that a certain beneficiary receives certain personal property, then the testator should say so in the will. It is particularly important to delineate specific bequests in a will when a remote family member or nonfamily member is the intended recipient.

As in so many aspects of estate planning, communication between the testator and his or her intended beneficiaries can help avoid disputes after the testator's death. Conversations about estate plans can help manage expectations and minimize questions about the decedent's intent. Ideally, a testator will share his or her intentions with the beneficiaries, engage in conversations to clear up any misunderstandings, and seek input about beneficiaries' wants and expectations. Parents often do not know what is important to adult children or what weird stuff has sentimental value. As probate litigators know, good communication across generations is usually an exception. Few families speak openly about mortality and what the family dynamics will be when someone is no longer around (or about the feeding frenzy that may occur when Mom and Dad are no longer around to keep the middle-aged offspring in line).

Multiple beneficiaries sharing property

Very often, a will does not bequeath specific items to specific beneficiaries. Instead, Dad's will may direct that his personal property—including every necktie, baseball card, or even his Mercedes—be divided among his three children. Or, the personal property may comprise all or part of the residue. Such dispositions can be challenging because the interested parties, the fiduciary, or, as a last resort, the court, has to decide who gets what. A distribution of $3 million to three sons is easy; we can all do the math. A distribution of 90 years' worth of personal property valued at $3,000 can be much more difficult.

People can get intensely sentimental over stuff. Fishing poles and chipped china may represent happy memories with the decedent. Showing affection toward an item that the decedent treasured may connect the beneficiary to the loved one. Or a beneficiary's interest in certain items of personal property may be chiefly utilitarian. Angela needs a car. Simon could use the table saw. Howard likes the big-band record collection. Mindy wants to sell the watch collection to raise money for a vacation. All kinds of family dynamics come into play when it is time to deal with personal property. And while the value of the personal property certainly is a factor in the dynamics, the value is often not the primary driver of the beneficiaries' emotions and the resulting behavior.

Beneficiaries, typically siblings, who got along well enough before the decedent's death, will generally find a way to work together and cooperate after the decedent's death. These folks may make a pact that they are not going to let squabbles over material goods drive them apart. Some folks may not care about the personal property. Others may be more concerned with keeping the peace than staking claim to items, even if he or she would like the items. Some beneficiaries simply want nothing to do with the decedent's personal property; it may be a painful reminder of the death or even a painful reminder of the life.

In the absence of specific bequests and assuming a modicum of civility, dividing up the personal property among two or more beneficiaries should begin with a conversation about who wants what. The conversation could be initiated by the fiduciary or the beneficiaries. The interested parties can engage in horse-trading to see if everyone is satisfied enough. As we all know, the mark of a good compromise is when no one is completely happy.

Some groups of amiable beneficiaries are very democratic about the process of dividing the personal property. They may meet at the decedent's house and draw straws, pick playing cards or pull names out of a hat. The person with the largest straw, highest card, or the first name pulled from the hat gets to pick an item. Armed with Post-It notes emblazoned with his or her name, that person then stakes a claim to an item. The person with the next largest straw, highest card, or the next name drawn from the hat then picks an item. The choosing of items circles through the group in this way until all desired items are claimed. With cooperative beneficiaries, this process is fair, can be a little fun, and can bring folks together. Usually, beneficiaries will choose a few items and agree that the rest of the personal property be discarded, donated, or sold.

Dealing with the leftovers

There is nothing like a weekend spent cleaning Grandma's attic to exemplify the expression, "one man's trash is another man's treasure." Any fiduciaries or beneficiaries who do not need to don a hazmat suit (true story) should consider themselves lucky. If the decedent owned a lot of personal property, at some point the fiduciary or beneficiaries need to decide what needs to be thrown away. The fiduciary and beneficiaries may be able to dispose of the items themselves or they may hire a junk removal company to do the dirty work. Occasionally, there is the very unfortunate predicament when virtually all the personal property is worthless, or the fiduciary and beneficiaries have to dispose of truckloads of trash, refuse, or worse.

If the leftover items are in decent condition and have some utility, then the beneficiaries may wish to take possession and try to donate the items, potentially receiving a tax benefit for the value of the donation. If there are numerous unwanted items, the fiduciary may hire some type of salvage business that may either purchase the remaining items of value or take certain items on consignment. When leftover personal property does not have much value, the estate may have to pay to cart the property away.

It is particularly important to delineate specific bequests in a will when a remote family member or nonfamily member is the intended recipient.

Issues concerning value of the personal property

One of the first tasks a fiduciary should undertake is preparing an inventory of the estate, including personal property. The fiduciary should walk through the house (or wherever the property is located) and should catalogue all items. The fiduciary should obtain appraisals of any valuable items. If the property includes valuable items, the fiduciary should secure the property and make sure appropriate insurance is in place. Ultimately, the fiduciary will have to account for the property.

To determine actual value, a fiduciary may use his or her own experience and may undertake relevant research. He or she may also consult with other family members who may have expertise, for example, on the fair market value of the front loaders piled up on the front lawn (true story). If the personal property includes fine jewelry, fine watches, art, coins, firearms, antiques, heavy equipment, handmade bicycles, etc., the fiduciary may need to obtain formal appraisals. With appraisals in hand, fiduciaries are better able to determine who gets what and how to equalize shares of multiple beneficiaries. Appraisals also help determine value if items are going to be sold.

Fairly often, a beneficiary will believe that certain items are worth far more than the actual value or even an appraised value. Beneficiaries can hang on to overinflated values as a way to attempt to avoid departing with certain items. Squabbling over value may also provide ammunition to criticize the fiduciary, particularly if the fiduciary is a sibling. If a beneficiary is already grumpy about a fiduciary's appointment or conduct, the beneficiary may very well claim that the fiduciary sold the motorcycles for less than fair market value, or improperly donated an original Andy Warhol painting as a way to bolster his or her complaints against the fiduciary, and perhaps even his or her share of the estate.

Appraisals help ensure that the fiduciary fulfills the fiduciary duty of maximizing the value of the estate for the advantage of the beneficiaries and help deflect accusations that the fiduciary undervalued and undersold certain items. Sometimes, due to lack of knowledge about an item's worth, or a desire to clean out the house and proceed with the administration, a fiduciary may make hasty decisions about disposing of the property. Beneficiaries may know more about the property than the person in charge of disposing the property.

Many beneficiaries do not appreciate the time and expense involved in liquidating items. Often the effort to sell every item that may have some value does not justify the net gain, particularly if professional fiduciaries or other compensated fiduciaries are involved. Nevertheless, people do not like to hear, "It's just not worth it" from their well-meaning but desensitized fiduciary or lawyer. To try to minimize costs, a fiduciary may enlist

other beneficiaries to help clean out the house and to take charge of selling, auctioning, or otherwise trying to dispose of the property.

Family feuds over personal property

The cliché "no good deed goes unpunished" befittingly describes serving as a fiduciary. Even when a will is executed properly and appears to designate who gets what, interested parties can find ways to object. An heir, beneficiary, caretaker, etc. who is disappointed, angry, or jealous may initiate a will contest, a breach of fiduciary duty claim, a *quantum meruit* claim, or some other equitable claim in an effort to acquire property or deprive others of property. He or she may object to accountings or seek to remove the fiduciary. The disgruntled person may also take matters into his or her own hands, literally, and take the desired property (often rationalized as "for safe keeping").

Probate disputes stem from all kinds of emotion and behavior, both real and imagined. Fighting over stuff, sometimes even worthless stuff, can generate particularly raw and intense feelings. If there were problems in the beneficiaries' relationship before the decedent's death, very often those problems will carry over and escalate when it comes time to divvy up the property. Egos, misunderstandings, power struggles, and senses of entitlement—often held in good faith—can greatly complicate the distribution of property.

Not every allegation, of course, is a case of sour grapes. Beneficiaries often must bring legitimate claims to expose a case of undue influence or lack of capacity. And certainly not all fiduciaries are wise and altruistic. More than one fiduciary has put their hands in the proverbial cookie jar or has taken the good stuff for themselves. Some fiduciaries exploit their responsibilities and enjoy the ego trip of the duties. Few phrases will incite the ire of a sibling more than, "Mom put me in charge!"

Dividing personal property can be particularly difficult when the fiduciary is also a beneficiary and has an interest in the property.

Dividing personal property can be particularly difficult when the fiduciary is also a beneficiary and has an interest in the property. The fiduciary may take the diamond ring, sterling silver service, and Oriental rug—and leave the remaining truckload of knickknacks to his sister—saying, "Hey, I took only three things!" (true story). While a fiduciary is supposed to sublimate his or her personal interests and is supposed to treat all beneficiaries fairly, the fiduciary is likely emotionally connected to the decedent and the personal property. Fiduciaries who are also beneficiaries need to take particular care to allocate property equitably.

A typical will designates one sibling as the fiduciary. If folks generally get along and if the fiduciary plays by the rules, the estate administration should be relatively uneventful. But sibling rivalry or simmering resentments can lead to huge battles over the personal property (which are usually not *really* about the personal property). A brother may insist on taking his other brother to court over the disappearance of holiday decorations; a brother may refuse to assent to an account because his sister consigned the china; a sister may accuse her brother of giving a boat away to another brother; a brother may insist on rotating custody of dad's military service mementos; or a sister may squirrel away mom's cremated ashes (all true stories).

Second marriages provide a very common context for disputes over personal property (and all other types of assets). A typical feud happens when Dad dies and leaves everything to his second wife. Dad's biological children from his first marriage are irked, furious that their biological Mom's furniture passed to the evil step-mom and convinced that all items of monetary and sentimental value will end up with the evil step-siblings. With second families, it is vitally important that an estate plan clearly delineate who gets what. Mothers and fathers should not necessarily assume that the surviving step-parent will leave property to the children consistent with the wishes of the biological parent.

Problems may also arise if one beneficiary was a caretaker. One sister may have made extreme personal sacrifices in order to care for an ill parent. As a result, perhaps the parent gave her a valuable family heirloom before the decedent died or in the decedent's will. Other beneficiaries may have trouble understanding the extent of the sacrifice and may accuse the sister of being an opportunist. They also may have some guilt, which may manifest itself as criticism of the sister who assisted the ill parent. But perhaps the sister did take advantage of the situation. Perhaps she did unduly influence the decedent or help herself to property, rationalizing to herself that she earned it and that her laggard siblings in other states do not deserve the special heirloom. Was the caretaker a scoundrel or a saint? Or maybe both?

Beneficiaries often hold onto promises made long ago. Even at age 40, Reggie may remember that Grandpa promised him the train set when Reggie was five. In his will, Grandpa may have left all personal property to Reggie's aunt. If Reggie has other reasons to challenge his aunt's behavior, one can be sure that Reggie will at some point grouse about the train set. There is also the common phenomenon when folks, often the always-eager-to-please-grandparents, end up promising the same item to several people. Decades later, three cousins claim that Grandma promised them the ruby earrings—and they each may be right! Testators need to keep in mind that little kids remember all kinds of things. It is astounding how many people, who are often grandparents themselves, remember who got what for Christmas 60 years ago.

Fiduciaries caught in the crossfire

Fiduciaries have significant discretion, which may come into play when dividing personal property. In the absence of clear direction from the will, a fiduciary may choose who gets what and may even divide the personal property into lots. Regardless, it is hard to please everyone. If feuds over personal property persist, the fiduciary may decide it is in the best interest of the estate to liquidate all assets, turn it into cash, and divide it in accordance with the will. At the end of the day, the fiduciary's actions should be reasonable and should balance his or her fiduciary duty with the objective of minimizing conflict and the resulting cost.

Fiduciaries may have to initiate claims to recover personal property. If someone takes property from an estate without legal justification, the fiduciary may need to institute a claim for conversion or may need to deduct the value of the property from the balance of a beneficiary's share of the estate.

When a fiduciary encounters a dispute regarding the division of personal property or an ambiguous instrument, he or she may file a petition for instructions or a complaint for declaratory judgment. A petition for instructions takes a neutral position and a complaint for declaratory judgment defines a controversy and then advocates for a specific resolution. These actions ask the court, "What do we do?" The resulting judgment resolves the legal question and provides guidance to the fiduciary, successor fiduciaries, and beneficiaries.

The judgment also should insulate a fiduciary from liability for actions the fiduciary takes in accordance with the judgment. The judgment takes some of the guesswork out of fulfilling fiduciary obligations and thus should help avoid, or at least minimize, conflicts with beneficiaries and the potential claims for breach of fiduciary duty that can arise from those conflicts. Questions asked in a petition for instructions or complaint for declaratory judgment can include how to make distributions and how to value assets.

Role of the lawyers

Lawyers for parties who have an interest in an estate's personal property not only can advocate for their client's interests in certain items, but also can help facilitate compromise that will bring closure to the disputes. So often in probate disputes, emotional and psychological issues impede what otherwise should be decisions based on the decedent's intent and the economics of litigation. Many litigants, particularly those involved in emotional family litigation, become very invested in the fight. Fighting defines their view of the world, or at least their family, and can even engender blind spots about the economics of the matter. The attorney for the beneficiary can play an important role in helping the client understand what the law can and cannot do.

In family feuds, lawyers should probe about the family dynamics. History among the parties helps explain a client's perception of facts and their motivations. Lawyers must explain the many variables inherent in probate disputes. Clients need to understand from the start that there is (usually) no such thing as an "open and shut case" and that very rarely is there a "win."

Many emotional family members expect that a judge will tell a recalcitrant sibling that he or she was naughty. Such drama in the courtroom is atypical. Lawyers should explain that it is impossible to predict behavior of parties, lawyers, and courts. Furthermore, the law can rarely regulate human behavior. The law generally cannot stop people from badmouthing each other, cannot give a bad guy good character, and cannot ensure that Thanksgiving is warm and fuzzy.

In the end, it is just stuff

We human beings can have odd relationships with material things. We think shiny things are valuable, think more is better than less, and often want what others have just because they have what they have. For good or bad, our possessions help define us, much like our families do.

Clients should be made aware that they do their families big favors by clearly expressing (ideally in a legally valid document) how they want their possessions to be distributed. Communicating about all aspects of estate plans is always a good idea. It will usually make a fiduciary's job easier, will help diffuse beneficiaries' emotions, and will greatly help any judge charged with sorting out who gets what. Conveying intent is not so much about what we want to happen to the personal property as it is about how we wish to treat the people we leave behind. ■