Wealth Management Update

October 2021

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As part of our ongoing efforts to keep wealth management professionals informed of recent developments related to our practice area, we have summarized below some items we think would be of interest. Please let us know if you have any questions.

October 2021 Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-Family Loans and Split Interest Charitable Trusts

Federal interest rates increased slightly for October of 2021. The October applicable federal rate ("AFR") for use with a sale to a defective grantor trust, self-canceling installment note ("SCIN") or intra-family loan with a note having a duration of 3-9 years (the mid-term rate, compounded annually) is 0.91%, up from 0.86% in September and up from 0.38% in October of 2020.

The October 2021 Section 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 1.0%, the same as in September, but up from 0.4% in October of 2020.

The AFRs (based on annual compounding) used in connection with intra-family loans are 0.18% for loans with a term of 3 years or less, 0.91% for loans with a term between 3 and 9 years, and 1.74% for loans with a term of longer than 9 years.

Thus, for example, if a 10-year loan is made to a child, and the child can invest the funds and obtain a return in excess of 1.74% the child will be able to keep any returns over 1.74%. These same rates are used in connection with sales to defective grantor trusts.

In re Gerald F. Johnson Revocable Trust, No. 351134, 2021 Mich. App. LEXIS 3732 (Ct. App. June 17, 2021) – Unintended Waiver of Ex-Spouse's Creditor Rights

Barbara Johnson ("Wife") and Gerald F. Johnson ("Husband") divorced in 2008. As part of the divorce they entered into a Settlement Agreement (the "Agreement"), distributing the marital assets, and setting Husband's alimony obligation at $10,000 per month. The Agreement did not terminate alimony automatically at Husband's death, leaving the divorce court with the discretion to continue, modify, or terminate alimony upon his death. Among the assets awarded to Husband in the Agreement was his stock in Novi Springs, Inc. (the "stock"), which was awarded to him "free and clear of any right, claim, title or interest" of Wife. After executing the Agreement, Husband assigned his interest in Novi Springs, Inc. to his revocable trust. He also assigned some portion of his shares to an irrevocable trust for the benefit of his son from a previous marriage.

After Husband's death, his Personal Representative filed a motion to terminate his alimony obligation. While that motion was pending, the trustee of the revocable trust distributed the stock to three employees who were named in the trust as specific devisees of the stock. Wife alleged that the distribution of the stock caused the estate to be insolvent and thus did not have sufficient assets to meet the alimony obligation, and therefore she should be able to reach the stock for continued spousal support after Husband's death. Wife filed a petition in the probate court requesting that the stock be returned to the trust pending the litigation addressing the modification of spousal support. The probate court determined that under the terms of the Agreement the stock was the separate property of Husband and Wife waived any claim she might have against it, and therefore dismissed Wife's petition.

The Appellate Court affirmed the probate court's decision, relying on the plain language of the Agreement, specifically Paragraph 4.D of the Agreement, which provided that Husband was to have as his "sole and separate property, free of any claim thereto by [Wife], except as hereinafter stated to the contrary, the following assets," which included the stock in Novi Springs, Inc. The Court held the Agreement to be unambiguous in deciding that Wife had essentially waived her interest, even as a creditor, to any of the assets separately awarded to Husband under Paragraph 4.D. The Court states that "the word "hereinafter" denotes that there must be contrary provisions after Paragraph 4.D. Yet, there is no exception listed for the stock." Thus, the stock was a separately awarded asset, and Wife could not reach the stock as satisfaction and payment of the alimony obligation.

The Court also considered Paragraph 4.L of the Agreement, which it held to be a "catch-all" that makes it clear that the property retained by each of Husband and Wife was to be within their full individual power and they are free to do with it what they choose. The Court held that Wife's agreement to Paragraph 4 constituted an intentional and express relinquishment of her rights to the stock and her intent to waive claims to the stock. The Court concluded that the plain language of the Agreement awarded the stock as a separate asset to Husband, free and clear and Wife had no valid claim to have the stock returned to the trust, even if no other assets existed to satisfy her alimony obligation.

Estate of Wall, No. C087730, 2021 WL 3732360 (Cal. Ct. App. Aug. 24, 2021) – Community Property Presumption Prevails Over Title Presumption in Actions between Spouses, Not After Death

After Benny Wall's death his surviving spouse, Cindy Wall, petitioned the probate court to determine that a home, titled in Benny's name alone, was community property because it was acquired during marriage. Benny's children objected, arguing that the presumption of title prevailed over the community property presumption, and tracing proved the house was Benny's separate property. During the trial the children testified that Benny and Cindy's marriage was "not close," that Benny took title to the home in his sole name in 2010, and that he used separate property funds for the down payment and financing of the home. He refinanced the home in 2013 and did not include his wife on the loan. The children's testimony indicated that Benny did this on purpose to protect his own interests.

Cindy's testimony told a different story. She testified that she and Benny decided to buy the home together and that they applied for the loan as joint borrowers but were denied because she had a prior mortgage. The mortgage broker suggested that Benny apply for the loan himself and add Cindy's name to the title later. The broker testified that she understood the spouses to be joint owners of the home. A few days after signing the loan, Benny encouraged Cindy to sign a quit-claim deed, although she states that she did not know what that meant and no one explained it to her. However, she signed the deed whereby she "remised, released, and forever quit-claimed" the home to Benny. Cindy claims that Benny told her throughout the marriage that she was an owner, she paid for improvements, painted, and worked to install fixtures in the home. Cindy testified that Benny's actions led her to believe she was financially contributing to paying down the mortgage and that she was an owner of the property.

The issue presented in this case is whether (i) the community property presumption under California Family Code Section 760 (providing that all property acquired during marriage is community property), or (ii) the title presumption under California Evidence Code Section 662 (absent clear and convincing proof to the contrary, ownership is as set forth in the legal title), should apply. The probate court granted Cindy's petition, explaining that because the children essentially stood in the shoes of the decedent, it is treated as a dispute between spouses and thus the community property presumption applies. The probate court reasoned that because source of funds is insufficient to overcome a form of title presumption, it could not overcome a community property presumption either, and thus the tracing argument was not dispositive. Cindy also argued that California Family Code Section 721(b) applies, which provides that there is a rebuttable presumption of undue influence when one spouse obtains an advantage over another in a community property transaction. The probate court agreed, finding no persuasive evidence of any intent, agreement, or common understanding between the spouses to overcome the presumption that the home was intended to be a community asset, and that Cindy did not freely and voluntarily sign the quit-claim deed. The probate court found that the undue

influence presumption applied to the purchase of the home, the decision to title it in decedent's name, and the quit-claim deed, and that the children did not provide sufficient evidence to rebut the presumption.

The Appellate Court affirmed the probate court's decision, concluding that the undue influence presumption was properly applied. However, the Court held that the probate court erred in applying California Family Code Section 760 over California Evidence Code Section 662, stating that the community property presumption applies only in actions between spouses, and form of title controls at death. Still, the Court held that the undue influence presumption applies to post-death disputes, and prevails over the title presumption. Cindy's evidence surrounding the transactions between the spouses constituted substantial evidence of constructive fraud to support the probate court's finding of undue influence under California Family Code Section 721.

Giller v. Grossman, No. 3D19-2514, 2021 WL 3889320 (Fla. Dist. Ct. App. Sept. 1, 2021) – Children are Intended Beneficiaries in Dispute Over Trust Language

The Third District Court of Appeal affirmed a December 2019 Final Judgment that a beneficiary's children were intended beneficiaries of the trust and that reformation of the trust was not supported by evidence. The facts are as follows:

Brian Giller ("Brian") and his siblings, Anita Grossman ("Anita") and Ira Giller ("Ira"), have been involved in litigation over the administration of the estate of their father, Norman Giller, for the past seven years. While he was alive, Norman Giller created seven trusts to hold beneficial interests in various real estate holdings and other family assets. Pursuant to the terms of the trusts, Brian, Anita, and Ira were each allocated one-third of the assets and accumulated income. Anita and Ira received their one-third shares outright, and Brian elected to place his one-third share in separate subtrusts due to his financial difficulties, in order to protect his share from creditors. Brian and his two now adult children, Jamie and Jason ("issue"), are equal beneficiaries of all but the subtrust to the Giller Family Trust, of which Brian is the primary beneficiary and his children are the remaindermen. Norman appointed Anita as Trustee of the seven trusts, with Brian's approval. Brian borrowed money from one of the family businesses and agreed to repay the loan, with Norman's approval, however, it soon became obvious that Brian would never repay the loan.

In 2005, Brian began to request distributions from the subtrusts. Anita would make a needs assessment, and then she would issue modest checks to Brian. In 2008, when Anita's husband became ill, she stopped conducting any needs assessments before issuing checks to Brian. After Norman's death in 2009, Brian requested all the accumulated income in the subtrusts. The attorney who drafted the trusts advised Anita that if she was to distribute all the principal to Brian, she would be in breach of her fiduciary duties as Trustee because Brian was not the sole beneficiary of six of the seven subtrusts. Brian then demanded all of the income-generating assets as well as the accumulated income, and Anita refused his demand. Subsequently, the board of the Giller family company sued Brian to recover the loan balance.

In 2011, Brian filed a fifteen-count complaint, among which he argued for Anita's removal as Trustee, breach of trust, and disputed Anita's interpretation of certain trust language that includes his children as beneficiaries, claiming that the language shows the intent to benefit him solely. The trial court disagreed, finding the trust language unambiguous, found no conflict of interest, and no breach of trust by Anita. On appeal, Brian argued that the trial court should have found the language ambiguous and required extrinsic evidence regarding the settlor's intent. He claimed that the trial court should have reformed the language to conform to his interpretation that the subtrusts were solely for his benefit, excluding his children.

The Appellate Court considered the plain language of the subtrusts, six of the seven substrusts contain a dispositive provision providing that the "Trustee may distribute to or for the benefit of such beneficiary, or his issue… so much of the net income of such beneficiary's separate trust as the Trustee, in the Trustee's discretion, deems necessary…" The Court found that the phrase "for the benefit of" does not render the subtrusts ambiguous as a matter of law with respect to the inclusion of Brian's issue as beneficiaries.

The Court further stated that "the subtrust language clearly sets forth Norman Giller's intent to include Brian's children. The polestar of trust or will interpretation is the settlor's intent. (citing Arellano v. Bisson, 847 So. 2d 998 (Fla. 3d DCA 2003); Phillips v. Estate of Holzmann, 740 So. 2d 1, 2 (Fla. 3d DCA 1998))." In order for the Florida Court to reform the trust, there must be clear and convincing evidence that the trust as written does not reflect the settlor's intent. Here, the Court held that reformation of the trust language to eliminate Brian's issue would go against Norman's intent, he created and oversaw the subtrusts to protect Brian's share of the trust from his creditors. The Court also affirmed the trial court's conclusion that Anita did not breach her fiduciary duties as Trustee and upheld the award of trustee's attorney's fees from trust assets for the breach of trust claim, pursuant to Florida Statutes 736.0802(10)(b).

The Private Client Services Department at Proskauer is one of the largest private wealth management teams in the country and works with high-net-worth individuals and families to design customized estate and wealth transfer plans, and with individuals and institutions to assist in the administration of trusts and estates.

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