Trusts & Estates

Top 10 **Developments**, **Lessons** and **Reminders** of 2017

BY SHARON L. KLEIN

SHUTTERSTOPCK

From new legislation, to important proposals, to instructive case law, 2017 saw some significant developments, lessons and reminders.

10. Trust and Estates, Matrimonial and Religious Law: Multi-Disciplinary Considerations Can Impact Divorce.

With the increasing overlap between the trust and estates and matrimonial practices, trusts and estates practitioners often become involved in premarital planning and should be cognizant of religious issues that can impact divorce.

A Get is a religious divorce under Jewish law that must be given voluntarily by a husband to a wife in order for her and any children of a subsequent marriage to marry freely within the Jewish faith. This has been problematic if, out of spite or as a manipulative tool, a husband refuses to give his wife a Get. There are a number of incentives that can be imposed by a secular court to facilitate the granting of the Get, however, since the Get must be given willingly to be valid, this raises the issue of whether the Get is truly "voluntary" if delivered under threat.

In *Sharabani v. Sharabani*, 54890/2010, NYLJ 1202798565597, at *1 (Sup., KI, decided Aug. 30, 2017), the court considered the implications of a husband's refusal to grant his wife a religious divorce, and relied on a New York statute (New York Domestic Relations Law (DRL) §253) with the unstated, but clear, purpose of solving a problem that is unique to Jewish marriages.

New York's Domestic Relations laws allow a court to consider the effect of a barrier to marriage when distributing marital assets and determining spousal support awards. DRL §§236(B)(5)(h) and 236(B)(6)(d). In *Sharabani*, the court found that Husband's refusal to give Wife a Get essentially limited her future financial circumstances in depriving her of the ability to remarry religiously and deprived her of emotional support. Husband's refusal to provide a religious divorce led the court to award Wife 100 percent of certain marital assets, if Husband continued to refuse.

To avoid a Get deviously being withheld, the Rabbinical Council of America has had some success in providing a form prenuptial agreement. In order to give the husband financial incentive to grant the Get, the agreement provides for a fixed sum of support to be paid to a spouse until the Get is delivered.

A preferred solution might be to negotiate a contractual promise to deliver a Get upon request and have that promise contained within a prenuptial agreement. A flurry of cases in New York in the 1970s all upheld provisions in parties' separation agreements with respect to the obligation to deliver a Get. See for example *Waxstein v. Waxstein* 90 Misc.2d 784 (Sup. Kings 1976). Against this statutory and decision framework, although applied to post-marriage agreements, it seems that such promises in prenuptial agreements should be enforced as well. Assuming that the promise to deliver the Get was made voluntarily before the marriage, the prospect of subsequent penalties for failure to honor the promise arguably should not detract from the voluntariness of the initial promise.

> A preferred solution might be to negotiate a contractual promise to deliver a Get upon request and **have that promise contained within a prenuptial agreement.**

9. Estate Planning Documents Should Be Revisited in Event of Divorce or Separation.

New York's Estates, Powers and Trusts Law (EPTL) §5-1.4 provides that divorce revokes dispositions to, and fiduciary nominations of, former spouses. In *McCauley v. New York State*, 46 N.Y.S.3d 262 (N.Y. App. Div. 2017), the Appellate Division considered whether this statute revoked the designation of a former spouse as the beneficiary of her ex-husband's retirement plan. The court found that, according to the plain language of the EPTL and the legislative history, the statute applies to dispositions like the one made by the decedent and to persons who, like the decedent, died after the statute was amended to its present form because the disposition did not become effective until after death (when the amended statute was in effect). Further, the court found that the spouse had affirmatively waived any rights to death benefits under a separation agreement.

Although ultimately the statute worked to prevent a disposition that surely was not intended by the decedent, this case serves as key reminder of the significance of premarital planning, and the importance of avoiding reliance on state default law alone. Divorced spouses, spouses in the process of getting a divorce and unmarried couples who are separated should give immediate attention to their planning documents, to ensure they reflect their intent, and issues such as these should be clearly addressed in prenuptial agreements. (Subject to applicable laws and other legal restrictions, including elective shares rights and spousal rights in certain retirement plans.)

8. Property Discovered After New York Estate Tax Return Filed Didn't Require Filing of Amended Return or Payment of Additional Taxes, Penalties or Interest.

An Advisory Opinion (TSB-A-17(1)M) issued on Oct. 6, 2017 considered whether any additional New York estate tax was due when funds were discovered in the decedent's name more than 10 years after her death, following a search of the NYS Comptroller's Unclaimed Property records.

The Department of Taxation and Finance (the Department) concluded that, because the omitted asset was discovered more than three years after the timely filing of the original estate tax return, and the date of death value was less than 25 percent of the New York gross estate, the executor was not required to file an amended estate tax return or pay any additional estate taxes, penalties, or interest. A tax may be assessed at any time if a false or fraudulent return is filed with intent to evade tax, but the Department found no indication that was the case.

7. Grandson of Jewish Art Collector Has Standing to Sue on Behalf of Foreign Estate for Nazi-Confiscated Art.

In *Maestracci v. Helly Nahmad Gallery*, 63 N.Y.S.3d 376 (N.Y. App. Div. 2017), the Appellate Division, First Department, found that the grandson of a Jewish French art collector whose Modigliani painting was allegedly confiscated by the Nazis has standing to sue for the painting in New York. Defendants argued that Maestracci had no standing to bring the action, because, under EPTL 13-3.5, he had not established, as a foreigner, that he was a duly appointed representative of the nondomiciliary estate. Although the court agreed that merely asserting that one is a beneficiary of a foreign decedent does not confer standing to bring suit on behalf of the estate, it noted that it has construed EPTL 13-3.5 to permit certain representatives of estates in foreign countries to bring suit in New York without first obtaining New York letters of administration. The court found that Maestracci had followed the alternative procedure of filing an affidavit and supporting documents establishing his right to pursue claims on behalf of the estate under foreign law.

6. Commissions on Adjusted Income After Using Power to Adjust Recharacterized.

Under New York's power to adjust regime in EPTL §11-2.3(b)(5), a trustee is permitted to make adjustments between income and principal to be fair and reasonable to all beneficiaries. » Page 11

SHARON L. KLEIN *is the Tri State Region President at Wilmington Trust, N.A. Colleague* ALEX WAXENBERG, *Private Client Advisor, provided valuable assistance in the preparation of this article. This article includes developments through Jan. 1, 2018.*


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Estate Planning For Copyrights

BY DAVID WECHSLER AND MOIRA A. JABIR

In the 21st century, the term artist encompasses many different mediums from literary works and paintings to music, apps, audiovisual and architecture. And implementing an estate plan around the unique assets of modern artists requires the estate planner to consider different strategies to protect the value of the artist's creations during life and after death. Understanding the impact of copyright on estate planning the artist/client is the initial priority.

Since 1978, a copyright has come into existence with the creation of an "original work of authorship fixed in any tangible medium of expression" (17 U.S.C. §102) but the enforceability of that copyright is dependent on the registration with the US Copyright Office. Copyright ownership is separate from the ownership of the artistic work and the sale of the artistic work will not automatically transfer the copyright, unless expressed in writing. 17 U.S.C. §204. The transfer of an interest in a copyright can be to the whole or a portion and can occur in a number of ways. 17 U.S.C. §201(d). The transfer of a copyright can be limited in use and in timeframe. The term of a copyright created on or after Jan. 1, 1978 is "life plus 70 years." 17 U.S.C. §302.

If during the representation of the artist/client, an asset is identified that has not been registered, it is important to facilitate the registration as this is the only means by which the artist/client is protected from copyright infringement and by which she or he can collect statutory damages and attorney fees in the event of said infringement. The application is straightforward and available on the U.S. Copyright Office website. It requires the following information: title and nature of work; the full name and nationality of the artist as well as a statement of the artist's understanding that the work was not created within the scope of an employment contract ("work made for hire" is a defined term in §101 of Article 17 of the 1976 Copyright Act); the date that the work was created and if published, the date it was first published; and finally, if the work was adapted or derived from a preexisting work, and if so, what preexisting work.

Once registered, or if the asset is already registered, the estate planner needs to work with the artist/client to ensure that all underlying agreements related to the work are organized in one place and docketed for dates and payment schedule. With timely registration, the copyright owner can be assured of collecting statutory damages and attorney fees in the event of infringement. Such was the case when the estate of Marvin Gaye sued Robin Thicke, Pharrell Williams, Clifford Harris Jr. and the distributors of "Blurred Lines, for the similarity of sound and feel to Marvin Gaye's 1977 billboard hit "Got to Give It Up." *Williams v. Bridgeport Music*, 2015 U.S. Dist. LEXIS 97262, Copy. L. Rep. (CCH) P30,791. The estate was successful in establishing that there was direct and circumstantial evidence that "Blurred Lines" was in some manner derived from Marvin Gaye's work and obtained recuperative damages. Id.

After registration of the asset, another aspect the estate planner must consider is how to protect the value of the asset during life and after death of the artist. Copyright is a bundle of rights granted to creators of original works enabling them to exclusively display, reproduce, perform, sell and transfer their original works[1] and derivatives[2] of their work. 17 U.S.C. §106. The goal behind this legal right to copy is that the creators receive a fair return for their work and avoid exploitation by others. And so to be successful, the estate planner must plan with the understanding that the copyright is a bundle of separable intangible rights which are conferred on the copyright owner for a limited period of time.

> Implementing an estate plan around the unique assets of modern artists requires the estate planner to **consider different strategies** to protect the value of the artist's creations during life and after death.

The protection afforded a copyright is dictated by the U.S. Constitution in Article 1, §8 Clause 8 and the duration of the copyright depends on the status of the work on Jan. 1, 1978.[3] If the work was made on or after Jan. 1, 1978, then it will last the author's life plus 70 years. And, if multiple creators were involved, then it is the term of life of the last surviving author plus 70 years. And if the work was "made for hire" during the scope of employment, then the employer or other person for whom the work was prepared has protection for the shorter of 95 years from the first publication or 120 years from creation.

A key aspect of planning around copyright is the knowledge that the transfer or assignment of a copyright by the artist/client is not necessarily irrevocable. U.S. Copyright law allows the recapture of a copyright (called a termination or recapture right). 17 U.S.C. §203. This was done because legislators understood that the value of a copyright is unknown initially and it is important » Page 11

DAVID WECHSLER *is a partner and* MOIRA A. JABIR *is an associate at Moritt Hock & Hamroff.*

Guiding the Dead Hand: Decanting Under EPTL 10-6.6

BY TONI ANN KRUSE AND CHRIS NASON

As oenophiles know, red wine often produces sediment as it ages, introducing a bitter flavor and gritty texture to the wine. The process of removing these impurities by carefully pouring the wine from the original bottle into a new vessel before serving is known as "decanting." An old trust agreement can similarly acquire "sediment" in the form of tax provisions that are no longer applicable or distribution requirements that are no longer appropriate. In the trust context, the term "decanting" refers to the process of carefully appointing assets from an old trust to a new trust with more favorable terms. The practical effect of the appointment is to revise the terms governing the original trust agreement. If a trust instrument's provisions do not provide the trustee with an amendment power, decanting may be the best way to modify unfavorable provisions and can be accomplished in New York without consent from the person who created the trust, the beneficiaries, or any court.

> New York's EPTL 10-6.6 remains one of the best and is **a powerful tool for practitioners.**

Decanting may be useful, for example, when a trust agreement requires mandatory distributions at a time when the beneficiary is involved in a messy divorce or is struggling with substance abuse, a distribution in the next year might not be in that child's best interest. In the case of a disabled beneficiary, decanting a trust into a third-party supplemental needs trust may be particularly advantageous because, although new trust (the "appointed trust") will be created with assets set aside for the beneficiary, that beneficiary will not be considered the creator for purposes of the Medicaid payback provisions. See, e.g., *Kroll v. New York State Dep't of Health* (N.Y. App. Div. 2016).

The first decanting statute was passed in New York in 1992. This statute, Estates Powers and Trusts Law §10-6.6 (EPTL 10-6.6), has been amended several times since, most recently in 2015. Although at least 25 states also have decanting statutes, New York's EPTL 10-6.6 remains one of the best and is a powerful tool for practitioners.

Decanting Under EPTL 10-6.6

Although EPTL 10-6.6 allows the trust that receives the appointed property (the appointed trust) to have substantially different provisions from the trust from which property is appointed (the invaded trust), there are limits to the trustee's powers. The most important restriction stems from the nature of the power. The power to decant is a fiduciary power and must be exercised in the best interests of one or more of the beneficiaries. A trustee planning to decant should carefully consider the reasons for decanting. This is especially true if the trustee plans to make changes which » Page 11

TONI ANN KRUSE *is a partner and* CHRIS NASON *is an associate in the private client group of McDermott Will & Emery in New York.* CARLYN McCAFFREY *provided helpful comments in the preparation of this article.*

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The Inevitable: **Death and Taxes**

BY CHRISTINA JONATHAN AND TERENCE E. SMOLEV

There is an old English saying, usually attributed to Benjamin Franklin, that "nothing in our lives is certain except death and taxes." As is seen frequently in mass media, many wealthy individuals, politicians and corporations attempt to dodge one of these life certainties. However, if in attempting to avoid one of these certainties, violations are committed, the consequences are severe and will not be pardoned, not even in death.

A recent illustration involves the loss by the Caribbean community of Lowell Hawthorne, founder and CEO of the franchise Golden Krust Caribbean Bakery & Grill (Golden Krust), known for its staple Jamaican style beef patties. Golden Krust is a popular chain that Hawthorne started in 1989, which developed into a national franchise with over 120 restaurants in nine states. In addition, Golden Krust patties are sold by most supermarkets, including Costco, in over 30 states and also served to students in New York City public schools. Lowell documented his company's success in his 2012 publication, "The Baker's Son," and he also appeared in a 2016 episode of CBS' "Undercover Boss." With such great achievement, it was a shock that the 57-year-old Jamaican born entrepreneur was found dead from a self-inflicted gunshot wound. Lowell was allegedly driven by "fears that the Feds were investigating him for evading millions of dollars in taxes."

Tax evasion is a serious crime that can ultimately lead to substantial penalties and incarceration up to five years. In general, the Internal Revenue Code §7201 creates two kinds of tax evasion: the willful attempt to evade or defeat the assessment of a tax and the willful attempt to evade or defeat the payment of a tax. While death may end a criminal case against an individual to a certain extent, death in and of itself does not defeat the payment of the taxes, penalties and interest that the individual may owe, or prevent further prosecution of the individual's business.

As a basic rule, a corporation is treated as a separate entity, taxed unto itself, wherein shareholders and officers are shielded from corporate liabilities. However, there are a number of exceptions to both the IRS and NYS tax laws that will allow the government to assess taxes and commence an action against an individual shareholder, or officer. Specifically, I.R.C. §7343 defines the term "person" to include an officer or employee of a corporation, or a member or employee of a partnership, who is under a duty to perform the act in respect of which the violation occurs. Therefore, if a responsible shareholder fails to file a required corporate return, or files with false information, or fails to collect and turn over taxes that were assessed against his business, then there may be personal liability against that individual.

Once an assessment has been made against an individual, his or her estate will still be responsible for addressing and paying this liability. Or even worse, if an assessment is made against an individual who filed a joint return with his or her spouse, the spouse will be jointly and severally liable for any taxes, penalties and interest owed during the years that they filed jointly, including additional assessments from ongoing investigations or audits.

When a taxpayer passes away, his executor or an administrator of his estate will now be responsible for negotiating and paying from estate assets any tax liabilities due. Sometimes assets transferred to third parties may be seized by the collection officer. The IRS has a strict collection process for decedent's and estate taxes owed. Once an assessment has been made and the case is assigned to collection, the first thing that a collection agent determines is if there is a joint liability. As mentioned, if there is a joint liability, then the taxing authorities will take collection against the surviving spouse. If the collection case is not dealt with immediately, the surviving spouse may be subject to adverse action such as levies, wage garnishments, driver's license suspension, etc.

An infamous case dealing with this exact issue was that of Carol Ross Joynt, former producer of Larry King on CNN's "Larry King Live" and author of the 2011 memoir "Innocent Spouse." Carol's husband died of pneumonia, leaving behind Nathan's, a popular Georgetown bar. He also left behind $3 million in back taxes, penalties and interest. Although the taxing authorities take a hard position on joint liability, in certain circumstances, a surviving spouse can plead innocence for her husband's tax liability, as was successfully done by Carol through her tax attorneys.

Both the IRS and NYS offer relief of tax, interest and penalties on joint tax returns if the injured spouse can prove that such relief is warranted. The IRS statute offers three types of relief: Innocent Spouse, Separation of Liability and Equitable Relief. Innocent spouse relief completely eliminates the tax liability of a spouse pursuant to provisions of the tax law, its regulations and rules. Separation of liability relief provides for the separation of income and deductions for each of the spouses. Thus, each spouse has his/her own separate tax liability, interest and penalties, and will not be liable for the other's allocation. Equitable relief exists when a taxpayer does not qualify for innocent spouse or separation of liability relief. The intricacies of the statute, regulations and rules are beyond the provisions of this article. However, any matrimonial attorney, tax attorney, or general practitioner should be aware of the existence of these provisions of the tax law, regulations and rules to appropriately advise clients, when joint tax liabilities are involved.

As for tax liabilities that are solely decedent's, the collection case may be assigned to an IRS Revenue Officer (R.O.) to enforce against the estate. Generally, an R.O. cannot commence any collection action against an estate until he has completed all of the required fact finding actions. These regulations impose a duty that the R.O. must research the surrogate's court records, as well as internal and third-party resources. Note, an R.O. has the ability to secure all pertinent probate or administration documents, such as copies of the death certificate, will, letters testamentary, list of assets, any proceedings that outline distribution or litigation of the deceased's assets, list of heirs and their contact information, bonds posted by the fiduciary, accountings, documents related to the businesses owned by the decedent. See IRM/Part5/workingdecedentcases/5.5.3.4. The R.O. also has tools to assist with identifying assets owned by the decedent prior to death and can determine if decedent made any transfers prior to death.

The goal of an R.O. is to ultimately collect all monies owed to the government, by any means available to him. There are certain federal and state remedies available that will allow an R.O. to force a fiduciary to pay amounts due from the estate assets. A beneficiary may be required to personally pay decedent's tax liability to the extent that he received assets from the decedent's estate. This may be accomplished by the R.O. commencing a transferee action against beneficiaries who received assets. It is important for the Executor or Administrator to determine when a notice of Federal Tax Lien (Lien) has been filed by the IRS against the decedent to properly defend such actions. If a Lien was recorded on a tax assessment made before death, then it attaches to all assets owned by the deceased taxpayer, including any assets that were transferred after the Lien. Therefore, any assets that would automatically pass to an heir will be subject to that Lien, possibly making the beneficiary liable to the government for the value of that asset. In contrast, if the Lien was recorded on a post-death assessment, it does not attach to non-probate property and can only attach to probate assets in the estate.

> Tax evasion is a serious crime that can ultimately lead to **substantial penalties** and **incarceration up to five years.**

The death of a loved one is always difficult to deal with, especially if a federal or state investigation targets a surviving spouse, or beneficiary of the estate. It is critical that an executor or administrator of an estate that is facing issues of tax investigations, lawsuits, or the like are fully aware of his or her obligations and exposure of all individuals involved.

A final note: the newly enacted federal tax law need be considered when dealing with tax matters. Collection issues should continue as before the enactment.

CHRISTINA JONATHAN *is a partner at the firm Berkman, Henoch, Peterson, Peddy & Fenchel.* TERENCE E. SMOLEV *is of counsel to the firm.*

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In order to effect consistency in how adjusted amounts are treated for purposes of computing commissions, Gov. Andrew M. Cuomo signed a new law into effect on Sept. 12, 2017 (New York A.1482/S.2079 (2017) [Eff. Jan 1. 2018] Amends EPTL §11-2.3b(G)), which treats an adjustment as a recharacterization of the adjusted amount from income to principal or principal to income, as the case may be, in order to calculate commissions.

5. When Disputing New York Domicile for Income Tax Purposes, Perhaps Love Is All You Need.

New York generally taxes residents on their worldwide income. There are two separate and independent bases on which an individual can be taxed as a resident: (1) the individual is domiciled in New York or (2) the individual is a nondomiciliary who satisfies the statutory residency test.

Domicile is the place a taxpayer intends to have as his permanent home; the place to which he intends to return to after being away. A New York domicile does not change until a taxpayer can demonstrate by clear and convincing evidence that he has abandoned his New York domicile and established a new permanent domicile.

In *Matter of Patrick*, taxpayer met his current wife Clara in high school in New York in 1965. He gave her a heart-shaped necklace inscribed with their names as a token of his love. After high school, taxpayer joined the army and Clara was sent to boarding school in Italy. When she married another man, taxpayer was so upset he destroyed the mementos he had from her, except for one photo that he kept for 40 years.

Taxpayer married his first wife, lived in Connecticut and worked in New York City, where he had a very demanding job. After a near-deadly health scare, taxpayer reevaluated his life and his marriage, with which he had been unhappy for years. He separated from his first wife, renting an apartment in New York City to be close to his job. His thoughts turned to Clara and he searched for her, eventually tracking her down in Paris. They spoke on the phone for the first time in 40 years and reunited shortly thereafter in New York City, where Clara revealed the heart necklace she had cherished for all those years. Love between them was immediately rekindled and the taxpayer asked her to marry him that very night. They were secretly married in New York City the following year after their divorces from their first spouses were final. Taxpayer claimed he changed his domicile when he moved to Paris in 2011 to be with Clara.

The auditor initially determined that the five primary domicile factors set out in the Nonresident Audit Guidelines issued by the Department—Home, Active Business Involvement, Items of Sentimental Value ('Near and Dear"), Family Connections, and Time Spent—"all appear to be in our favor," and issued taxpayer a notice of deficiency for over $2 million. Indeed, taxpayer kept the New York City apartment after the move to Paris, spent substantial time there, received phone bills, credit card statements, W-2s, and 1099s there and remained registered to vote in New York. Time spent in Paris was low in comparison.

Nonetheless, the Administrative Law Judge focused on taxpayer's intent and found credible the taxpayer's testimony that he never considered New York his true home, that it was simply a place to sleep near work especially during the divorce, and to receive medical treatment. Taxpayer timely paid and filed all taxes due in France in 2011 and 2012 and for all years since. He obtained a French driver's license, a lengthy and difficult process. He also purchased and made extensive renovations to a home in Paris, where he moved the day after retiring early to be with Clara, despite forfeiting substantial benefits from his company.

4. Proposal to Clarify Taxation as New York Statutory Resident—"Gaied Legislation."

Under New York's statutory residency test, a nondomiciliary will be taxed as a New York resident on his worldwide income if he (a) maintains a permanent place of abode (PPOA) in New York and (b) spends over 183 days in the state during the taxable year. N.Y. Tax Law §605(b)(1). The statutory residence test was at issue in the landmark decision of *Gaied v. Tax Appeals Tribunal*, 22 N.Y.3d 592 (N.Y. Ct. App. Feb. 18, 2014).

Gaied, a New Jersey domiciliary who worked in New York, purchased a three-unit apartment building in New York where his parents occupied one apartment, and he rented out the other two. He kept no clothing or personal belongings in the apartment and had no bed there, sleeping on a couch when he occasionally spent the night. Since Gaied did spend over 183 days in New York for business, the matter turned on whether the apartment could be considered a PPOA. The Tax Appeals Tribunal determined that he did maintain a PPOA, finding it significant that he maintained and owned the property, and had unfettered access to it (despite his actual infrequent use). The Appellate Division affirmed. However, the Court of Appeals concluded that there was no rational basis for the Tribunal's interpretation. According to that court, a mere ownership interest is not sufficient; there must be some basis to conclude that the residence was utilized as the taxpayer's residence.

Unfortunately, despite the groundbreaking *Gaied* decision, practitioners reported that the Department construed the *Gaied* case in a way that still classifies many vacation homes as PPOA, subjecting their owners to New York income tax. A proposal introduced in both Houses (New York A. 8610/S.6860 (2017)) would enact the spirit of the Gaied holding by excluding a dwelling from the definition of PPOA if:

- The dwelling is not used as the taxpayer's principal residence,
- The dwelling is located more than 50 miles from the individual's place of employment in New York; and
- The taxpayer did not stay overnight at the dwelling more than 90 nights during the taxable year.

3. Including Decanting Provisions in Trust Instruments May Maximize Flexibility.

EPTL 10-6.6 permits "decanting," which allows the trustee of an otherwise irrevocable trust to transfer trust assets into a new trust with different terms. The statute requires notice to interested parties and has restrictions on the power, including if a trustee has limited discretion to invade principal. Decanting can be a tremendous tool for dealing with changed circumstances, correcting mistakes, facilitating tax benefits or optimizing a trust's administration.

> The bottom line is that **practitioners should consider reaching out to their clients** to discuss whether they should sign new wills and revocable trusts or make changes to otherwise irrevocable documents through a decanting or other revision process to take advantage of new planning opportunities and **ensure their existing plans still accord with their intent.**

Including decanting provisions in trust instruments may maximize flexibility without resort to EPTL 10-6.6. In *In re Hoppenstein*, 2015-2918/ANYLJ 1202784244139 (Sur. Ct. N.Y. Co, March 31, 2017), 2017 NY Slip Op 30940(U), the trustees successfully relied on their powers under a trust document to distribute a life insurance policy on the settlor's life to a new trust that excluded an estranged daughter of the settlor and her issue. Dismissing an objection that the transfer did not satisfy the requirements of the decanting statute, court held that the New York decanting statute had no bearing on the case since the trustees relied on their powers under the document to effectuate the transfer.

2. Loss of SALT Deductions Heightens Importance of State Income Tax Planning.

On Dec. 22, 2017, President Trump signed into law new tax legislation (the Act). Beginning in 2018, the Act will repeal all deductions for state and local taxes (SALT deductions) in excess of $10,000. Additionally, the home mortgage interest deduction is limited to debt of $750,000, instead of the previous $1 million. These changes may detrimentally affect home values in New York.

The loss of the SALT deductions heightens the importance of state income tax planning. Against the backdrop of the tremendous planning opportunities presented with the Act's doubled gift tax exemptions, setting up trusts in jurisdictions like Delaware becomes particularly attractive since those trusts may not pay state income taxes on accumulated income and capital gains. With the other advantages of Delaware law, including the ability to create a directed trust and control the trust's investments, the ability to create a self-settled trust that is protected from creditors, and the ability to create perpetual trusts, creating Delaware trusts can serve multiple goals.

If some seek to change their residence to a state that does not impose an income tax, it will be important to carefully demonstrate a change in domicile, and ensure they are not taxable as statutory residents.

1. All Estate Planning Documents Need to Be Reviewed in Light of New Tax Laws.

The Act doubles the federal estate and gift exemption to $11.2 million per person ($22.4 million per married couple), beginning on Jan. 1, 2018, and sunsetting after 2025 to $5.6 million (plus inflation adjustments).

The New York estate tax exemption amount is $5.25 million for those dying on or after April 1, 2017 and on or before Dec. 31, 2018. For those dying on or after Jan. 1, 2019, state and federal exemption amounts will be linked to the 2010 federal exemption amount of $5 million, as indexed for inflation, so the doubling of the federal amount will not apply to the New York exemption amount. N.Y. Tax Law §952(c)(2)(A).

The gap between state and federal exemption amounts could have potentially significant consequences from both tax and dispositive standpoints. In terms of tax impact, care must be taken with formula bequests linked to the full federal exemption amount, particularly because an estate that exceeds 5 percent of the New York exemption faces a cliff, causing the estate to be taxable from dollar one. In 2018, if a credit shelter disposition was tied to a federal exemption amount of $11.2 million, that would generate a state estate tax of over $1.25 million. This tax bite might be further compounded with an interrelated tax computation if the tax is payable from a marital or charitable residuary.

To avoid this result, wills can define a formula credit shelter bequest to mean the maximum amount that can pass free of both federal and state taxes, or avoid formulaic dispositions and rely instead on techniques that maximize flexibility after death, including partial qualified terminable interest property (QTIP) elections, Clayton trusts (property passes into a QTIP marital trust, only if the executor makes a QTIP election, and the balance typically passes into a credit shelter trust) and disclaimer trusts (one spouse leaves everything outright to the other, who can disclaim an appropriate amount into a disclaimer marital and/or credit shelter trust, considering the tax laws and specific needs), potentially preserving some unused federal exemption for the surviving spouse through federal portability. Since New York does not impose a current gift tax, utilizing the increased federal exemption through lifetime gifting might be very attractive: Individuals could leverage the full federal exemption while reducing their New York estate tax since the gifted assets will be excluded from the New York estate. (New York has an add back for gifts made within three years of death for individuals who die prior to Jan. 1, 2019—N.Y. Tax Law §954(a)(3).) Given that the doubled gift tax exemption is slated to disappear after 2025, this also presents a limited window of opportunity.

A bequest pegged to the federal exemption amount may also produce dispositive distortions. An estate plan designed to leave an amount equal to federal exemption to children, for example, with the balance of the estate passing to a spouse would have resulted in a bequest to children in 2017 of $5.49 million and a bequest of $11.2 million in 2018, possibly leaving much less to the surviving spouse and much more to the children than was intended.

The bottom line is that practitioners should consider reaching out to their clients to discuss whether they should sign new wills and revocable trusts or make changes to otherwise irrevocable documents through a decanting or other revision process to take advantage of new planning opportunities and ensure their existing plans still accord with their intent.

Decanting

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may be adverse to one or more beneficiaries.

The trustee exercising the decanting power must have unlimited discretion to invade trust principal in order to fully access the statute. Unlimited invasion discretion includes the power to distribute principal for a beneficiary's best interest, welfare, comfort or happiness. The logic behind the decanting statute is that a trustee who has the power to pay the trust's entire principal to the beneficiaries should be allowed to pay the principal to a new trust for the benefit of one or more of those beneficiaries. The class of current and remainder beneficiaries of the appointed trust can be reduced but cannot be increased, although the trustee may grant a beneficiary a new discretionary power of appointment. This power of appointment must be very broad and can exclude as permissible appointees only the beneficiary, the trust's creator, the creator's spouse and the creditors, estates or the creditors of the estates of the beneficiary, the creator, and the creator's spouse.

If no trustee has unlimited discretion, the statute allows the trustee to effect a decanting in a more limited manner. The current and remainder beneficiaries must remain the same, the trustee must have the same authorization to invade principal and distribute income, and any powers of appointment must remain identical. However, the term of the appointed trust may be extended beyond the term of the invaded trust. During this extended period, after the invaded trust would have ended, the trustee may be granted unlimited discretion to invade principal, allowing the trustee to decant to a new trust and eliminate beneficiaries or grant powers of appointment.

Some restrictions apply regardless of the level of discretion a trustee has. For example, a beneficiary's presently exercisable withdrawal rights may not be eliminated. Additionally, a trustee may not decant to increase her compensation, reduce her liability, or eliminate a provision allowing someone else to remove or replace her. An extension of the perpetuities period beyond the period that would be required in the invaded trust will render the decanting invalid, and the trustee may not make changes that would jeopardize the trust's marital or charitable deductions or cause it to fail to qualify for the gift tax annual exclusion.

Approval is not required for decanting but notice must be provided to the trust's creator (if living), anyone who may remove or replace the trustee exercising the decanting power, and anyone interested in the invaded trust or the appointed trust 30 days before the effective date of the decanting. An "interested person" is anyone who would be required to receive notice if the trustee were to judicially account. Failure to object to the notice does not constitute consent to the decanting, although a court will consider the facts and circumstances of the notice in determining if it starts the statute of limitations to compel a trustee to account.

> EPTL 10-6.6 requires many steps and practitioners advising trustees to implement a decanting under the statute **should carefully document each step.**

GST Issues

Before decanting, a trustee is required by EPTL 10-6.6 to consider the tax consequences of the decanting. Unfortunately, there is some uncertainty about these consequences. Although the Internal Revenue Service (IRS) has long recognized that guidance is needed, none has been issued (Notice 2011-101 (Dec. 21, 2011)). In addition, the IRS has said that until guidance is released it will not issue private letter rulings in connection with decanting transactions that change beneficiaries' interests in a trust.

Although the income, gift and estate tax consequences of decanting must also be considered carefully, the generation-skipping transfer (GST) tax can pose particularly complex problems for the trustees of trusts that are protected from the GST tax either because they were irrevocable on Sept. 25, 1985 or because their transferors have allocated sufficient GST exemption to them. The IRS has suggested in a substantial number of private letter rulings that a trust could lose its exempt status if its terms are amended to change the interests of its beneficiaries.

The Treasury Regulations provide two safe harbors that may be relied on to protect a trust from loss of GST exempt status when beneficial interests are changed through a decanting. The first will not protect a trust unless state law then applicable to the trust permitted the decanting at the time the trust became irrevocable. The second will not protect a trust if the terms of the appointed trust shift a beneficial interest to any beneficiary who occupies a lower generation than those who held the beneficial interests before the decanting.

Any New York trust that became irrevocable before New York's decanting statute was enacted will not be protected by the first safe harbor unless the New York Court of Appeals recognizes that New York's common law permitted decanting prior to the enactment of EPTL 10-6.6(b). The second safe harbor described in the preceding paragraph will not be available unless it can be shown that there is no possibility that younger generation beneficiaries will receive more than they would have received under the terms of the invaded trust.

In this respect, the provisions of EPTL 10-6.6(b)(2) that permit the appointed trust to give a beneficiary a power of appointment present a potential trap. Because, as discussed above, any new power of appointment may not exclude members of a lower generation, the grant of any new power of appointment will be treated as shifting beneficial interest to a lower generation and cause the decanting to fall outside of the safe harbor.

Checklist

EPTL 10-6.6 requires many steps and practitioners advising trustees to implement a decanting under the statute should carefully document each step. A checklist is below:

(1) Set up the appointed trust (i.e., draft, execute, provide initial funding). Ensure the terms of the appointed trust do not violate any of the restrictions of EPTL 10-6.6.

(2) If the appointed trust is not a grantor trust, acquire an EIN. Open bank and brokerage accounts for the appointed trust.

(3) Determine which individuals interested in the invaded trust must receive notice.

(4) Execute and acknowledge an instrument exercising the decanting power to transfer all, or part, of the assets of the invaded trust to the appointed trust. Unless the individuals who must receive notice of the transfer consent, the effective date of the transfer must be at least thirty days after service.

(5) Send copies of (i) the invaded trust, (ii) the appointed trust, and (iii) the instrument exercising the power, by registered or certified mail, return receipt requested, to the individuals entitled to receive notice.

(6) Retitle the invaded trust's assets in the name of the trustees of the appointed trust.

(7) If the invaded trust is subject to proceedings in Surrogate's Court (e.g. a testamentary trust), a copy of the transfer instrument must be filed in the Court within twenty days of the effective date of the transfer.

Copyrights

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to allow the creator a "do over" to ensure fair value is ultimately obtained by the artist.

There are two clauses in the Copyright Act that address termination rights, one of which applies to pre 1978 works and the other that applies to post 1978 works. 17 U.S.C. §203, §304. Both of these clauses provide that the copyright owner retains control over the copyright through the power to terminate the transfer at a future date. So an artist, or if she or he is deceased, their surviving spouse or issue, has a non-assignable non-waivable right to terminate most transfers and licenses granted by the copyright owner, during her or his life, at a defined point in the future. 17 U.S.C. §203(a)(2). And if the copyright owner is deceased and she or he has no surviving spouse or issue then the executor or administrator assumes this right. The purpose is to give the copyright owner, his or her family or his or her estate the opportunity to market their work after the original sale of the copyright. This addresses the injustice that occurs when a copyright is assigned before fair value could be determined.

The rules of recapture are as follows: the termination of an assignment can be effectuated at any time during a five-year period beginning at the end of 35 years from the date of execution of the assignment. 17 U.S.C. §203(a)(3)-(4). If the artist is living, then it is sufficient for the artist to serve written notice of the termination on the grantee at least two years before the termination date stated in the notice and recording of said notice with the copyright office. Id. If the artist dies prior to the termination period, and there is a surviving spouse, then the surviving spouse owns 100 percent of the termination interest unless there are children and grandchildren. When there are children and grandchildren involved, then the spouse owns 50 percent of the termination rights and the issue shall own the other 50 percent of the termination rights, and the issue shall each take shares based on their generational assignment. And when the termination rights are owned by more than one person, it takes the holders of more than 50 percent of the interest to exercise the termination right which means that family members need to cooperate with each other. Upon the effective date of termination, all licenses and rights associated with the copyright revert to the artist or to the persons owning the termination interest including those that did not join in signing the notice.

The statutory heirs remain unknown until the termination right comes into effect and this raises a complication. The termination rights provisions of the Copyright Act apply generally to any transfer of a copyright or any right comprised in copyright. Therefore, if an artist assigns his or her rights in the copyright of a piece of work to an individual during life, or to a limited liability company or to a revocable living trust, a statutory heir, if the artist is deceased, would be able to undo the artist's intent. However, there is a specific exception under Copyright Law, which will make all estate planners smile (or cringe if you fear probate) for transfers by Wills.

This is just a brief examination into the estate planning intricacies surrounding copyrights. The estate planner working with the artist/client must tread a careful path because not all the normal estate planning recommendations will apply and there are many opportunities for errors. It is important to keep detailed records of the artist/client's work and understand potential hurdles that may be encountered if the copyright to certain works are transferred during life. Foremost, it is important to understand what you do not know, and to work with a team to enable the goals of your artist/client to be maximized both during life and after death.

1. Original work is any literary work, computer program, apps, musical works, pantomime, choreography, pictorial, graphic or other audiovisual, sound recordings, architectural works created and fixed in any tangible medium of expression on or after January 1, 1978.

2. Derivative work is work based on a preexisting original work.

3. The U.S. Constitution grants Congress the power "To promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries" and it is often referred to as the "patent and copyright clause."