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Top 10 Developments, Lessons and Reminders of 2019

BY SHARON L. KLEIN

2019 saw significant developments, lessons and reminders:

10. Plan for Access to Digital Assets After Death.

Family members can face many challenges in attempting to retrieve a decedent's digital information. In *Matter of Coleman*, 96 N.Y.S.3d 515 (2019), parents of a 24-year old who died unexpectedly in his sleep requested access to the contents of their son's iPhone, in part to determine if he had any medical issues his siblings may also have. Estates, Powers & Trusts Law (EPTL) Article 13-A, which governs the administration of digital assets, uses a three-tiered approach to determine fiduciary access:

(1) Directions given via an online tool provided by a custodian prevail;

(2) If no online tool has been used or provided, a user's direction in a will, trust, power of attorney or other records prevails; and

(3) In the absence of any direction, the terms of service agreement controls.

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The statute distinguishes between access to the *content* of an electronic communication and access to a *catalogue* of electronic communications (like the "to" and "from" lines of an email, without content). The default rule for personal representatives is that privacy is on: The custodian may disclose the catalogue of digital communications, but content access is not permitted unless the decedent consented to disclosure or the court determines that disclosure is reasonably necessary for the administration of the estate. In *Coleman*, the decedent neither used an online tool nor had a will or other document that controlled disposition of his digital assets. The court determined that the decedent's parents did not need to access the digital assets for the administration of his estate, concluding that they may access the non-content information only.

In comparison, in *Matter of Estate of Swezey*, NYLJ, Jan. 18, 2019, (Sur. Ct., NY County), the executor petitioned for turnover of photographs stored in the decedent's Apple account. Decedent's will left all of his personal property to petitioner, but did not expressly authorize petitioner to access his digital assets. The court determined that, in today's increasingly digital world, a decedent's property "must include assets kept in a digital form in cyberspace." In requiring Apple to disclose the photographs, the court found that photographs are not "electronic communications" that require the account holder's specific consent to disclose.

These cases are important reminders to practitioners to consider access to digital assets as part of the estate planning process.

9. New Real Estate Transfer Tax Disclosure Requirements.

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Effective Sept. 13, 2019, when a limited liability company (LLC) is the grantor or grantee in a deed transfer of a building containing one-to-four family dwelling units, certain real estate transfer tax returns (Forms TP-584 and TP-584-NYC) will not be accepted for filing unless accompanied by a list of the names and addresses of all members, managers and other authorized persons of the LLC. If any LLC member is itself an LLC or other business entity, all shareholders, directors, members or partners must also be provided until ultimate ownership by natural persons is disclosed. (N.Y. Tax Law §1409(a), TSB-M-19(2)R, issued Nov. 4, 2019). Although the new law explicitly states that "[t]he identification of such names and addresses shall not be deemed an unwarranted invasion of personal privacy …," some have raised privacy concerns, as well as concerns about the compliance burden, given that the disclosure process might need to parse through several layers of entities before natural persons are revealed.

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8. Personal Income Tax Changes Enacted.

In TSB-M-19(4)I, issued Sept. 3, 2019, the Department of Taxation and Finance (the Department) discusses personal income tax changes that were enacted in the 2019-20 Executive Budget.

Charitable Contributions Itemized Deduction Limitation Extended. If an individual's New York adjusted gross income (AGI) is greater than $1 million and less than $10 million, the New York itemized deduction is limited to 50% of the federal deduction for charitable contributions. For individuals with New York AGI greater than $10 million, the itemized deduction is limited to 25%. That limitation was due to expire, but has been extended through 2024 (N.Y. Tax Law §615(g)).

Retroactive Fiduciary Income Tax Guidance Issued. Although the Department originally took a different position, for tax years beginning on or after Jan. 1, 2018, trusts and estates, as well as individuals, may claim some deductions on their New York returns that are no longer available for federal purposes (N.Y. Tax Law §615(a)). These deductions allowable for state but not federal purposes include state and local taxes over the $10,000 federal limit and certain miscellaneous deductions, such as tax preparation fees and investment expenses. Additionally, for tax years beginning on or after Jan. 1, 2018, estates and trusts must add back the qualified business income deduction allowed under Internal Revenue Code (IRC) §199A.

If 2018 Form IT-205, *Fiduciary Income Tax Return*, was filed without making these required modifications, TSB-M-19(4)I directs that the taxpayer **must** file an amended 2018 Form IT-205 (N.Y. Tax Law §§619(b) and 619(e)).

Tax law provisions extended. The top personal income tax bracket, tax rate, and tax table benefit recapture provisions were extended through 2024. (N.Y. Tax Law §§601(a)(1)(B), 601(b)(1)(B), 601(c)(1)(B), 601(d-1)(1)(D), 601(d-1)(2)(C), and 601(d-1)(3)(C)).

7. While Corporate Trustee Did Not Breach Duty To Diversify, Consider Directed Trust Structure in These Situations.

In *Matter of Wellington*, 85 N.Y.S.3d 497 (decided at the end of 2018), the Appellate Division, Second Department, found that a trustee's deference to a former co-trustee's investment strategy was made with reasonable care, skill and caution, as required under the Prudent Investor Act. While the corporate trustee and son of the grantor acted as co-trustees, the trusts contained stock concentrations. The corporate trustee continually suggested diversification

strategies, which were repeatedly rejected by the individual trustee. After that trustee's death, a beneficiary filed objections to the corporate trustee's accounting, alleging it had breached its fiduciary duty by failing to diversify. The court dismissed the objections, finding that the corporate trustee did recommend diversification, but properly deferred to the co-trustee because he was very sophisticated and the trust terms evidenced the grantor's intent for his son to retain ultimate control over investment strategy: The son succeeded his father as president of an investment management firm and his trust investment strategy had been very successful, he had the ability to remove the corporate trustee for any reason, one trust expressly stated the trustees were under no obligation to diversify, and when the corporate trustee became the sole trustee it gradually diversified the trusts' assets.

While the trustee in this case was not liable for failure to diversify, oftentimes a directed trust structure can provide a better solution: Under the laws of some jurisdictions, investment and administrative duties can be bifurcated. An individual co-trustee or other advisor can be authorized to direct the trustee with respect to investments. The bifurcation between investment and administrative duties in Delaware, for example, is very clear. Except in cases of willful misconduct, an administrative trustee will not be held liable for any loss resulting from complying with an investment direction given by an authorized person. Del. Code Ann. tit. 12, §3313. *Duemler v. Wilmington Trust Co.*, C.A. 20033, V.C. Strine (Del. Ch. Oct. 28, 2004). Even if a trust has not been established under Delaware law, it may be possible to move the trust to Delaware, and then make an application to the Delaware court to add the directed trustee language to the trust instrument. In 2019, Delaware added a new provision that can facilitate creating a directed trust (Del. Code Ann. tit. 12, §3343). That section expands a trustee's power to appoint a successor trustee to include the power to appoint multiple successor and additional trustees, with the ability to delegate specific trustee powers to selected trustee(s) and not to other trustee(s). Accordingly, a directed trust structure can be created, for example, by selecting a co-trustee to make all investment decisions, along with the power to direct the other trustee(s).

In 2019, Delaware added a new provision that can facilitate creating a directed trust.

6. Economic Civil War: Battle Over Cap on State and Local Tax (SALT) Deductions Continues.

The 2017 Federal Tax Cuts and Jobs Act (the Federal Tax Act) limits an individual's SALT deduction to $10,000 for tax years beginning after Dec. 31, 2017 and before Jan. 1, 2026.

The battle over the SALT cap continues in two separate sets of lawsuits. First, on July 17, 2018, four states—New York, Connecticut, New Jersey, and Maryland—filed suit against the federal government in the U.S. District Court for the Southern District of New York, alleging that the cap is unconstitutional. On Sept. 30, 2019, the U.S. District Court granted the federal government's motion to dismiss the case. Relentless in what Governor Cuomo has described as "economic civil war," the states filed a Notice of Appeal in the U.S. Court of Appeals for the Second Circuit in November.

The second lawsuit relates to the "workarounds" several states enacted in response to the SALT cap: In New York, the 2018-19 Executive Budget introduced two state-operated charitable funds, one for health, the other for education, effectively allowing taxpayers to make deductible charitable contributions instead of state tax payments (N.Y. Tax Law §606(iii)). However, on Aug. 27, 2018, the IRS and Treasury Department issued proposed regulations 83 FR 43563, which were largely adopted in final regulations T.D. 9864 issued June 11, 2019, and effective Aug. 12, 2019. Th e regulations provide that taxpayers must reduce their charitable deductions by the amount of any state or local tax credit they receive or expect to receive, if that credit exceeds 15 percent of the contribution. On July 17, 2019, three states—New York, Connecticut, New Jersey—filed a lawsuit in the U.S. District Court for the Southern District of New York seeking to declare the final regulations unlawful. That lawsuit is pending.

5. Live Outside New York But Work and Own a Vacation Home in New York? Watch Out.

An individual can be taxed as a statutory resident in New York if that individual (1) maintains a permanent place of adobe in New York and (2) spends 183 days or more in the state during the taxable year (N.Y. Tax Law §605(b)(1)(B)).

The issue in *Matter of Obus and Coulson*, DTA No. 827736, was

whether a New Jersey domiciliary who owned a vacation home in New York, which he and his wife used just a couple of weeks a year, was taxable as a statutory resident. Since the taxpayer worked in New York, and was physically present for more than 183 days, the sole issue in the case was whether he maintained a permanent place of abode during the tax years in question. Taxpayers tried unsuccessfully to rely on *Gaied v. Tax Appeals Tribunal*, 22 N.Y.3d 592 (2014). In *Gaied*, the petitioner was a New Jersey domiciliary who worked in New York and owned an apartment building where his parents resided, but he had no bedroom or personal belongings there. The Court of Appeals concluded a mere ownership interest is not sufficient to create a permanent place of abode—there must be some basis to conclude that the residence was utilized as the taxpayer's residence.

The Administrative Law Judge in *Obus* determined that, since the taxpayers purchased the home as a vacation home for their enjoyment, *Gaied* simply did not apply. Even though taxpayers had rented separate living quarters at the house year-round to a tenant and used the house themselves only two to three weeks a year, the judge found that did not prevent them from using the property, nor did the fact that they used it exclusively for vacations transform its characterization as a permanent place of abode.

4. 'Pour Over' Will Changes Enacted.

EPTL §3-3.7 permits an individual to make a testamentary "pour over" disposition into a trust. Senate Bill No. 5513, enacted into law on Oct. 4, 2019, removes an apparent conflict between ETPL §§3-3.7 and 7-1.18 by clarifying that the trust does not need to hold any assets prior to the individual's death.

Additionally, it is no longer necessary that the trust agreement be fully executed prior to or contemporaneously with the will. Under the new law, provided the grantor signed the trust agreement prior to or contemporaneously with his will, the trustee need only sign prior to the testator's death.

An individual can be **taxed as a statutory resident** in New York if that individual (1) maintains a permanent place of adobe in New York and (2) spends 183 days or more in the state **during the taxable year** (N.Y. Tax Law §605(b)(1)(B)).

3. Uniform Voidable Transaction Act Enacted.

On Dec. 6, 2019, New York enacted the Uniform Voidable Transactions Act (UVTA), modernizing New York's fraudulent conveyance law, which had not been significantly updated in over 90 years. The UVTA, effective April 4, 2020, will strengthen creditor protection by providing remedies when a debtor transfers assets or incurs additional debts that hinder the creditor's ability to be fully repaid. For example, a transfer is voidable by a creditor if made by a debtor with actual intent to hinder, delay or defraud a creditor.

The UVTA makes substantive changes to New York's fraudulent conveyance law including:

- Shortening the statute of limitations to the later of: (1) Four years (instead of six years) after the transfer or (2) One year (instead of two years) after the transfer could reasonably have been discovered.
- Reducing the burden of proof of all claims from clear and convincing proof to a preponderance of the evidence.
- Applying choice of law based on the debtor's/transferor's location at the time of the transfer, instead of the current multi-factor test, which led to forum shopping.

There was concern that, while the UTVA legitimately is intended to prevent debtors skirting valid debts, certain official comments to the UVTA undercut an individual's ability to create a domestic asset protection trust. The New York City and State Bars submitted memoranda in support of the UVTA, but disavowed those comments. The New York legislature did not approve the official comments and presumably they should not influence how the UVTA is interpreted in New York.

2. Fundamental Reminders About Estate Planning.

In *Matter of Morris*, 2019 N.Y. Slip Op. 30514(U), a long-term same-sex couple died 12 days apart. An ambiguous 30-day survivorship clause caused a dispute as to whether the first-to-die's partner inherited substantial assets, which would then pass to the partner's beneficiaries under the partner's will, or whether the gift to her partner failed because she did not survive 30 days, causing the property to pass instead to the first-to-die's remainder beneficiary charities. The court found the decedent intended to impose a 30-day survivorship requirement.

Lessons learned?

Estate planning is not a DIY business. The poorly crafted will was in fact revised

by a non-lawyer friend of the first-to-die months before her death.

Unmarried couples, same sex or opposite sex, will not garner the protections of marriage. According to the Surrogate, the general rule of construction that testamentary provisions should be construed in a spouse's favor was inapplicable to this unmarried couple.

Create trusts to control disposition of assets. Survivorship clauses typically are used both to prevent property passing through probate (and potentially being taxed) twice in quick succession, and so property passes to the decedent's alternate beneficiaries instead of passing through the estate of a beneficiary who dies shortly after the decedent. However, the same result may follow if the beneficiary dies just outside the survivorship period. To prevent losing control of assets after death, individuals may be well-advised to create trusts instead of providing for outright dispositions.

1. Significant Estate and Gift Tax Changes Enacted.

In TSB-M-19(E), issued Nov. 20, 2019, the Department summarized estate tax legislation enacted in 2019.

Treatment of Dispositions to Non-US Citizen Surviving Spouses Extended. For a disposition to a non-U.S. citizen surviving spouse to qualify for the federal marital deduction, the disposition must pass in a Qualified Domestic Trust (QDOT). For estates below the federal filing threshold, the New York estate tax is based on the taxable estate computed on a pro-forma federal return. Although not required for New York purposes, dispositions to non-U.S. citizen spouses had to be in QDOT form because federal elections on the pro-forma return flow through to the New York return. This artificial need to create a QDOT resulted in significant unnecessary administrative burdens and legal fees.

A law enacted in December 2013 eliminated the requirement to create a QDOT if no federal return was required to be filed and the disposition would otherwise have qualified for the federal estate tax marital deduction. The law, which was set to sunset on July 1, 2019, has been extended to July 1, 2022 (N.Y. Tax Law §951(b)).

Qualified Terminable Interest Property (QTIP) Must Be Included in the Surviving Spouse's NY Estate. The 2019-20 Executive Budget amended New York Tax Law §954 due to the holding in *Matter of Seiden (Hogan)*, 2018 N.Y. Slip Op. 32541(U). In that case, a husband died in 2010, when his estate was not subject to federal estate tax. His executor created a QTIP trust for state purposes, making a QTIP election on the pro-forma federal return filed with the New York return. IRC §2044 imposes a tax on QTIP property for which a marital deduction was previously allowed. The Surrogate found that, since there was no federal estate tax return filed, there was no previously allowed marital deduction to trigger IRC §2044's inclusion of the property in the surviving spouse's New York gross estate. Consequently, the QTIP property escaped federal and state taxation in both estates.

New York Tax Laws §§954(a)(4) and 955(c) now require QTIP property to be included in the surviving spouse's New York estate if New York previously allowed a marital deduction for that property, irrespective of whether the QTIP election was made on the New York return or via a federal pro-forma return, if a federal return was not required to be filed. The change applies to estates of individuals dying on or after April 1, 2019.

Gift Add-Back Extended, With Small Window of Exclusion. The New York gross estate of a deceased resident is increased by the amount of any taxable gift made within three years of death, if the decedent was a New York resident at the time the gift was made and at the time of death. New York's three-year gift add-back expired for individuals dying on or after Jan. 1, 2019, but was extended until Dec. 31, 2025 (N.Y. Tax Law §954(a)(3)). The final legislation excepts from the add-back gifts made between Jan. 1, 2019 and Jan. 15, 2019, the period prior to the release of the 2019-20 Executive Budget.

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