Recent Developments: July 1-Sept. 30, 2017
By the Trusts and Estates Team of Moore & Van Allen PLLC

Federal Cases

**Charitable deduction denied for failure to provide cost basis of property contributed.**

In *Reri Holdings I, LLC v. Commissioner*, 149 T.C. No. 1 (July 3, 2017), the Tax Court denied a charitable deduction for the contribution of a remainder interest in an LLC to a university because of the taxpayer’s failure to strictly or substantially comply with the applicable substantiation requirements for the contribution. The taxpayer’s Form 8283 for the contribution contained a summary of the appraisal of the remainder interest but omitted the taxpayer’s initial cost basis with respect to the remainder interest. The taxpayer purchased the remainder interest for $3,400,000 approximately eighteen months before the charitable contribution and claimed a charitable deduction of $33,019,000, so the disclosure of the basis amount would have alerted the Service to the disparity between the recent purchase price and the deduction claimed. Because of the nature of the information that was omitted, the taxpayer was denied substantial compliance and was subject to a gross valuation misstatement penalty for claiming a deduction in excess of 400% of the correct deduction amount.

**Charitable deductions denied for lack of contemporaneous written acknowledgments, insufficient records, and failure to obtain appraisals.**

In *Ohde v. Commissioner*, T.C.M. 2017-137 (July 10, 2017), the Tax Court upheld the denial of a $145,000 charitable deduction and the issuance of an accuracy-related penalty for a married couple’s failure to provide contemporaneous written acknowledgments with individual dollar amounts and cost basis information for more than 20,000 noncash items the taxpayers claimed to have donated to Goodwill, including clothing, books, toys, furniture, and other household items. The taxpayers produced receipts for their donations that included general descriptions of the types of property contributed but that did not describe any specific items or their conditions. While taxpayers later produced a spreadsheet containing a description of specific items, that list was not prepared contemporaneously with the donations. The court held that each category of donated items (e.g., clothing, books, etc.) was subject to aggregation for purposes of the application of the additional record requirements for contributions of noncash property in excess of $500 and the qualified appraisal requirements for contributions of noncash property in excess of $5,000. The taxpayers reported contributions in excess of $500 in 11 separate categories, together constituting more than 99% of the total contributions claimed, and the taxpayers did not submit the additional information required for such contributions, being (1) the date the property was acquired, (2) a description of the property, (3) the cost or other basis of the property, (4) the fair market value of the property, and (5) the method used for determining the property’s fair market value. Further, the taxpayers reported contributions in excess of $5,000 in four separate categories, together constituting more than 88% of the total contributions claimed, and the taxpayers submitted no appraisals. The taxpayers did submit several Forms 8283, but neither Goodwill nor any appraiser executed those forms. The court cast doubt on the credibility of the taxpayers’ claims, particularly provided that the taxpayers had claimed more than $292,000 in deductions for noncash charitable contributions in the three years prior to the year in question and nearly $105,000 in deductions for such contributions in the two years after, all for contributions of similar household items. The court upheld a 20% accuracy-related penalty on the amount of the taxpayers’ underpayment as a result of the taxpayer’s negligence attributable to insufficient recordkeeping.

**Roth IRA arrangement invalidated for lack of business purpose.**

In *Block Developers LLC v. Commissioner*, T.C.M. 2017-142 (July 18, 2017), the Tax Court upheld excise taxes imposed on a Roth IRA arrangement that was deemed to have no valid business purpose. The taxpayer owned a series of companies that built retaining walls using patent-protected specialty blocks. The taxpayer sold the patents for the specialty blocks to an LLC co-owned by the taxpayer’s attorney and four Roth IRAs created by the taxpayer and his family members. The LLC in turn licensed the patents back to one of the taxpayer’s companies in exchange for a royalty equal to 10% of the company’s gross sales of the blocks. The purchase price for the patents was $250,000 and was almost entirely financed by the company, since the LLC was capitalized with less than $10,000. However, royalties paid by the company to the LLC in the first month of the arrangement totaled more than $270,000, so the LLC fully satisfied its debt to the company immediately (with the company’s money). Royalties paid by the company to the LLC over the next six years totaled nearly $1 million, $800,000 of which was funneled into the Roth IRAs. In finding that the arrangement served no legitimate business purpose, the Tax court noted that the sale of the patents was not necessary for the taxpayer to raise cash (as the taxpayer claimed), the LLC did not market the patents to third parties, the taxpayer’s companies continued to produce, test, certify, and promote the blocks as if the companies owned the patents, the legal realities of the transaction were not well-defined, the records kept regarding the transaction and resulting cash payment were inconsistent, and the royalty obligations were sporadically enforced. The court concluded that the transaction was “just a conduit to shunt money to the [IRAs]” and upheld the Service’s excise tax on the amounts funneled to the IRAs that exceeded the maximum contribution amounts. The court further held that in auditing the LLC, the Service was required to send audit notices to the LLC’s direct members but not necessarily to any indirect members (such as the taxpayer as an IRA beneficiary) when the Service had not been affirmatively furnished with the identity or contact...
information of any such indirect members (despite that the Service knew such information from its own files).

Sale of land did not constitute farming income to enable taxpayers to be “qualified farmers” eligible for an increased deduction cap with respect to a qualified conservation easement.

In Rutkoske v. Commissioner, 149 T.C. No. 6 (Aug. 7, 2017), the taxpayers were brothers who were each 50% members of an LLC that owned 355 acres of real property and, in the form of a conservation easement, conveyed development rights in the property to a public charity as a part gift/part sale before subsequently selling its remaining interest in the property to a third party. The taxpayers claimed they were “qualified farmers,” within the meaning of Section 170(b)(1)(E)(v), due to more than 50% of their gross income coming from the trade or business of farming; however, to meet that threshold, the brothers claimed that their income from the sale of the real property constituted income from the trade or business of farming. While taxpayers argued that the sale of the property was part of the capital investment required for the business of farming, the Tax Court rejected that position and found that the plain language of IRC Section 2032A(e)(5) did not include the sale of land, even if the land was related to farming activity, in the calculation of a taxpayer’s income directly attributable to farming. The court conceded that the taxpayers were farmers in the general sense and that in a typical year, they would have been qualified farmers. However, the taxpayers’ income in the year of the sale was at issue, and the sale income not qualifying as farming income caused the taxpayers’ disqualification. As qualified farmers, the taxpayers would have been entitled to deduct the value of the gift portion of the conservation easement up to 100% of their adjusted gross income (less other charitable contributions), instead of the typical limit of 50%.

In BC Ranch II, L.P. v. Commissioner, 867 F3d 547, 2017 WL 3446583 (5th Cir. Aug. 11, 2017), the Fifth Circuit vacated and remanded three of the Tax Court’s findings in BC Ranch II, L.P. v. Commissioner, T.C. Memo 2015-130 (July 14, 2015). The Tax Court had disallowed a charitable deduction for a series of conservation easements because several five-acre homesite parcels had been reserved within the easement boundaries, and the easements permitted the modification of the boundaries of the homesite parcels provided that no homesite parcel exceeded five acres and the conservation purposes of the easements were not adversely affected. The Tax Court determined that such potential for modification violated the requirement the conservation easements be perpetual. The Fifth Circuit disagreed, finding that the easements were perpetual as required because neither the exterior boundaries nor the total acreage of the easements could be changed and the charitable recipient had to consent to any modification. The Tax Court had also found fault with the required baseline documentation associated with the easements, but the Fifth Circuit again disagreed and noted that the documentation requirements were intended to be flexible. The Fifth Circuit ultimately remanded the matter to the Tax Court for consideration of other objections to the conservation easement deductions raised by the Service that were not addressed in the Tax Court’s initial ruling. The Tax Court had also found that capital contributions of $350,000 to $550,000 by limited partners to the partnership that owned the conserved land were receipts from disguised sales when each such limited partner was deeded one of the five-acre homesite parcels. Since each homesite parcel was worth less than $30,000, the Service had relied on the value of the limited partners’ use of the partnership’s common areas and the value of the limited partners’ charitable income tax deductions resulting from the conservation easement in justifying that the full amounts of the capital contributions constituted disguised sale proceeds. The Fifth Circuit found that the record included no valuation of the common area usage rights, cast doubt on whether the value of such rights would materially add to the homesite parcel values, and chided the Service for relying on the value of a conservation easement deduction that the Service had simultaneously argued should be disallowed.

In determining unrelated business taxable income, social club could not deduct losses incurred from activity not intended to generate profit.

In Losantiville Country Club v. Commissioner, T.C.M. 2017-158 (Aug. 14, 2017), the taxpayer was a social club qualifying as a tax-exempt organization under Section 501(c)(7). The club collected revenue from members through membership dues and from nonmembers through surcharges for the use of its facilities. Under its Form 990-Ts filed for 2010, 2011, and 2012, the club allocated a proportion of its overhead expenses against its nonmember revenues, resulting in a loss purportedly attributable to its nonmember revenue activities. Taxpayer subsequently deducted such loss from its investment income for purposes of determining its unrelated business taxable income. The Tax Court denied the deduction because such loss did not result from an attempt to collect revenue from which taxpayer intended to profit. The club contended that its activities with respect to nonmember revenue should be analyzed under Regulations § 1.183-2, which provides factors to consider in determining whether an activity is carried on for profit, but the court ruled such regulations inapplicable because they only apply to individuals and S corporations and not to tax exempt entities.

Unpaid gift taxes resulting from net gift not deductible by decedent’s estate for estate tax purposes.

In Estate of Sommers v. Commissioner, 149 T.C. No. 8 (Aug. 22, 2017), the Tax Court denied a deduction taken by a decedent’s estate for the amount of gift taxes payable with respect to net gifts made by the decedent within three years of the decedent’s death. Regulations § 20.2053-6(d) generally permit the deduction for estate tax purposes of unpaid gift taxes with respect to gifts made by a decedent during life, but the court ruled that such deduction does not apply with respect to net gifts because the donees of such gifts, and not the estate of the donor, are responsible for the payment of the gift taxes. The court also declined to apportion the estate tax payable as a result of the gift taxes being included in the decedent’s estate against the
gift donees because under applicable state law, such apportionment would only be permissible if the donee had received property includible in the decedent’s gross estate. Since the gifted property was not included in the decedent’s estate (only the amount of the gift tax was includible), the donees were not responsible for any estate tax payable as a result of the decedent’s death.

Deed conveying conservation easement satisfied contemporaneous written acknowledgment requirements.

In Big River Development, L.P. v. Commissioner, T.C.M. 2017-166 (Aug. 28, 2017), the Tax Court upheld a deduction taken by a limited partnership for a conservation easement. The partnership income tax return included a Form 8283 signed by the donee’s president, but the Form 8283 failed to include a statement that the donee provided no goods or services in exchange for the contribution. A subsequent letter from the donee to the partnership did include the requisite statement, but it was sent more than two years after the transfer of the easement. While the letter provided by the donee was found not to be contemporaneous with the transfer of the easement, the Tax Court determined that the deed conveying the easement did satisfy the substantiation requirements for a deduction. The deed was signed by the donee’s president and, while it indicated that the donee would provide services as to the property in connection with the transfer, those services were funded by a $93,500 fee paid by the partnership under the terms of the deed. The deed also contained a merger clause indicating that its terms constituted the entire agreement of the parties, so that was sufficient for the Tax Court to conclude that no additional goods or services were provided to the donor.

IRS permitted to examine estate tax return of predeceased spouse in connection with DSUE claimed by surviving spouse.

In Estate of Sower v. Commissioner, 149 T.C. No. 11 (Sept. 11, 2017), the Tax Court upheld the Service’s adjustment of the deceased spouse unused exemption amount (DSUE) available to the estate of a surviving spouse based on a reexamination of the estate tax return of the predeceased spouse. The predeceased spouse’s return erroneously calculated the DSUE by failing to take into account the predeceased spouse’s lifetime gifts. The Service had initially issued a closing letter with respect to the predeceased spouse’s estate. However, the closing letter did not estop the IRS from reexamining the predeceased spouse’s return for purposes of determining the DSUE because the letter did not constitute a negotiated closing agreement, no party was demonstrated to have relied on the closing letter to its detriment, and no double taxation was at stake. Further, the evaluation of the DSUE was not an impermissible second examination of the predeceased spouse’s estate because the IRS sought to obtain no additional information as to the predeceased spouse’s estate, and, in any event, the rule against reexamination only protects the predeceased spouse’s estate, not the surviving spouse’s estate. Finally, there was no statute of limitations for the examination of the predeceased spouse’s estate for purposes of calculating the surviving spouse’s DSUE because the DSUE would apply to tax assessed against the estate of the surviving spouse and not the estate of the predeceased spouse.

Early distribution from retirement account subject to income tax and penalties and not offset by business or education expense deductions.

In Cates v. Commissioner, T.C.M. 2017-178 (Sept. 13, 2017), the Tax Court upheld the ordinary income and 10% penalty tax imposed on an early distribution from the taxpayer’s 401(k). The taxpayer failed to complete a qualified rollover of the distributed amount and could not substantiate deductions the taxpayer claimed for tuition expenses. The taxpayer also claimed deductions for business-related expenses, but the court determined that no such deductions were available because the expenses were reimbursable by the taxpayer’s employer. The court upheld the accuracy-related penalty assessed against the taxpayer for substantial underpayment because the taxpayer did not establish reasonable cause or good faith with respect to the underpayment.

Federal Administrative Developments

Proposed Section 2704 Regulations Withdrawn.

In Second Report to the President on Identifying and Reducing Tax Regulatory Burdens (Oct. 2, 2017), the Treasury Department announced its plan to withdraw the proposed Treasury Regulations under Section 2704 that were initially released in Aug. 2016.

Distributions from incomplete gift trust were completed gifts by grantor of trust and were not gifts by distribution committee.

In PLR 201729009 (July 21, 2017), the Service provided that when a grantor created an irrevocable trust for the benefit of beneficiaries other than the grantor under which distributions could be made pursuant to (i) the unanimous consent of a committee of trust beneficiaries, (ii) the consent of the grantor and a majority of such committee, (iii) the direction of the grantor, subject to an ascertainable standard, or (iv) the direction of the grantor upon the grantor’s death, then (a) the grantor’s transfer of property to the trust was an incomplete gift, (b) any distribution from the trust would constitute a completed gift by the grantor to the distributee, (c) the trust was not a grantor trust with respect to the grantor or any committee member, and (d) no committee member had a general power of appointment with respect to the trust property.

CRUT investment in college endowment did not cause UBTI for CRUT even though endowment activities caused UBTI for college.

In PLR 201729014 and PLR 201729013 (July 21, 2017), and PLR 201730022 and PLR 201730019 (July 28, 2017), the Service provided that income realized by a charitable remainder unitrust from investing in a college’s endowment was not unrelated business taxable income (“UBTI”), even though the endowment included investments that constituted UBTI to the college and the college was the trustee and remainder beneficiary of the trust. The endowment did not constitute a partnership, and payments by the endowment to the trust were only made pursuant to a schedule that was unaffected by the performance of the endowment’s assets, so the UBTI nature of the endowment’s income was not relevant to the characterization of the trust’s income from the endowment payments.
Judicial reformations of trusts to correct errors and ambiguities did not affect GST exempt status.

In PLR 201732029 (July 21, 2017), the Service found that the judicial reformation of a grandfathered GST trust to correct a scrivener's error that would have denied a share of the trust assets to the descendants of a predeceased child of the primary beneficiary upon the primary beneficiary's death did not cause the trust to lose its GST exempt status or cause gift tax consequences. In PLR 201735009 (Sept. 1, 2017), the Service found that an amendment to a grandfathered GST trust that unintentionally caused a potential extension of the duration of the trust did not affect the trust's GST exempt status when the amendment was declared void ab initio by a court order made in accordance with applicable state law. Federal regulations permit the judicial modification or construction of a grandfathered GST trust to resolve a bona fide ambiguity in the trust terms or to correct a scrivener's error if the modification or construction is consistent with applicable state law (notwithstanding whether the modification extends the terms of the trust, though no extension occurred in these cases).

Relief granted for inadvertent terminations of S corporation status.

In PLR 201730002 (July 28, 2017), the Service retroactively restored a corporation's S corporation status that had been terminated as a result of the corporation's sole owner, an LLC co-owned by an individual and a grantor trust with respect to such individual, becoming an ineligible shareholder upon the individual's death due to the trust's grantor trust status being terminated and the LLC thus becoming a partnership for income tax purposes. In PLR 201730021 (July 28, 2017), the Service retroactively restored a corporation's S corporation status that had been terminated as a result of two trusts that were shareholders failing to file timely ESBT elections. In both cases, the Service found relief appropriate because the terminations were inadvertent, the circumstances causing the terminations were corrected within a reasonable period, and the applicable taxpayers treated their tax circumstances as if S corporation status had not been terminated.

Affirmative allocation of GST exemption allowed despite absence of Notice of Allocation.

In PLR 201731005 and PLR 201731010 (July 28, 2017), the Service found that when two taxpayers made gifts to a trust, elected out of the automatic allocation of GST exemption with respect to the gifts, and affirmatively allocated GST exemption to the gifts on Schedule D of their gift tax returns, the affirmative allocation of GST exemption was valid notwithstanding the fact that the taxpayers did not attach the otherwise required Notices of Allocation to their returns.

Conversion of non-grantor CLAT to grantor CLAT was not a transfer for income tax purposes and did not result in charitable deduction for Grantor.

In PLR 201730018, PLR 201730017, and PLR 201730012 (July 28, 2017), the Service found that a trust modification granting the settlor's brother a power to substitute assets in a nonfiduciary capacity from a CLAT, thereby causing the settlor to be treated as the owner of the trust for income tax purposes and converting the trust from a non-grantor trust to a grantor trust, did not constitute a transfer of the trust assets from the trust to the grantor for income tax purposes (unlike the conversion of a grantor trust to a non-grantor trust during the settlor's lifetime). Further, the modification did not constitute self-dealing because the settlor's brother was not a disqualified person for purposes of the private foundation rules. Finally, though contributions to CLATs that are grantor trusts generally entitle the grantor to a charitable income tax deduction at the time of contribution, the Service did not permit the settlor to take any charitable income tax deduction as a result of the conversion, since the conversion did not represent a transfer from the settlor to the trust. The modification did not appear to be retroactive, and the trust had taken charitable income tax deductions in prior years with respect to its annuity payments to charity.

Service recognizes common law marriage.

In TAM 201734007 (Aug. 25, 2017), the Service ruled that a decedent and the decedent's common law spouse (as recognized under applicable state law) were married for federal tax purposes when the decedent died.

In PLR 201735005 (Sept. 1, 2017), when the beneficiary of a grandfathered GST trust was incorrectly directed to pay income tax attributable to a capital gain realized by the trust, did in fact pay such tax, and was later reimbursed for such tax by the trust within the statute of limitations for her legal recovery of the tax, no actual or constructive transfer or addition to the trust occurred for estate, gift, or GST tax purposes.

Service grants extension to make carryover basis election.

In PLR 201735015 (Sept. 1, 2017), the Service permitted the estate of a decedent who died in 2010 to file a late Form 8939, electing out of estate tax treatment and submitting to carryover basis treatment, when professional advisors the estate relied on in good faith failed to file the form or recommend it to be filed.

Surviving spouse substituted as beneficiary of IRA after judicial termination of trust originally designated as beneficiary.

In PLR 201736018 (Sept. 8, 2017), when a trust that was the beneficiary of a decedent's IRA was judicially terminated in the aftermath of the decedent's death, resulting in the IRA assets being payable instead to the decedent's surviving spouse free of trust, the Service treated the IRA as having passed directly from the decedent to the surviving spouse, making the IRA eligible for "rollover" treatment.

Service may only communicate with taxpayers' representatives with respect to forms specifically listed on Form 2848 Power of Attorney.
In Chief Counsel Advice 201736021 (Sept. 8, 2017), the Service found that Form 2848 Powers of Attorney only cover the tax returns and forms specifically listed on the Form. Separate forms that are commonly attached to tax returns, including international information returns, must be separately listed on Form 2848 in order for the IRS to communicate with the named representative regarding such forms.

Procedure simplified for private foundations to determine if grants to foreign charities are qualifying distributions.

In Revenue Procedure 2017-53 (Sept. 14, 2017), the Service issued guidance simplifying the procedure for a private foundation to determine if a foreign grantee qualifies as a public charity for purposes of the qualifying distribution private foundation rules. Revenue Procedure 92-94 has been modified and superseded.

Service waives income tax consequences of IRA distribution to non-IRA account when taxpayer relied on incorrect professional advice.

In PLR 201737016 (Sept. 15, 2017), when an attorney advised a taxpayer to transfer the assets of the taxpayer's IRA to an account arranged by the attorney, told the taxpayer the new account was an IRA account when it was not, and then embezzled the assets of the new account, the Service waived the treatment of the account transfer as taxable income to the taxpayer (due to the assets leaving the original IRA and not being recontributed or "rolled over" to another IRA within 60 days) and permitted the taxpayer to contribute an amount up to the transferred amount to a new IRA account to reestablish the IRA.

North Carolina Cases

No North Carolina income tax deduction for gain on maturity of bonds purchased at discount despite federal income tax deduction.

In Fidelity Bank v. NC DOR (392A16, 393PA16) (Aug. 18, 2017), the North Carolina Supreme Court denied a North Carolina income tax deduction with respect to gain on the maturity of United States government bonds that were purchased at a discount from face value. Such gain ("market discount income") is deductible for federal income tax purposes because it is considered under the Code to be "interest" with respect to such bonds for such purposes, and interest earned from such bonds is deductible under the Code. North Carolina law provides that interest earned on United States government bonds is deductible for North Carolina income tax purposes but does not incorporate the provision of the Code defining market discount income as interest. The court provided that since North Carolina law does not incorporate the Code wholesale but rather only incorporates provisions on a piece-by-piece basis, the failure of North Carolina law to incorporate the definition of market discount income as interest means that for North Carolina law purposes, interest is defined in accordance with its plain meaning, which does not include market discount income.

Clerk's removal of guardian of estate and trustee of special needs trust upheld by Supreme Court.

In In re Estate of Skinner (277A16) (Sept. 29, 2017), a divided North Carolina Supreme Court held that the Assistant Clerk of Court did not commit an abuse of discretion in removing a principal's spouse as trustee of a special needs trust for the principal and guardian of the principal's estate when, within 60 days of the special needs trust being funded with approximately $170,000, the trustee/guardian spent nearly $160,000 of such funds on a house for the principal and the trustee/guardian, furnishings and appliances for such house, a prepaid funeral expense insurance policy for the principal, and a payment of more than $8,000 to the trustee/guardian's personal business, approximately $2,500 of which was acknowledged to be in reimbursement of legal expenses the trustee/guardian personally incurred in pursuit of marriage to the principal (who was incapacitated at the time of the marriage, which occurred four years before the special needs trust was funded) and in pursuit of being named as trustee and guardian. The Court of Appeals had overturned the Assistant Clerk's judgment as being "so arbitrary that it could not have been the result of a reasoned decision." The Supreme Court admitted that the Assistant Clerk had made certain errors in justifying the removal, such as presuming that the purchase of the funeral expense insurance policy violated a term of the trust when it did not and presuming that the trustee/guardian improperly benefitted from the purchase of house as a result of residing there with the principal. However, the Supreme Court held that the Assistant Clerk's removal of the trustee/guardian was justified because the facts indicated a general breach of fiduciary duty by the trustee/guardian in spending such a high percentage of the special needs trust funds within such a short amount of time in ways that either directly or indirectly benefitted the trustee/guardian. The dissenting justices disagreed that the purchase of the house, furnishing, and appliances was inconsistent with the purpose of the special needs trust, which the dissenting justices determined was to improve the principal's quality of life while not adversely affecting the principal’s eligibility for government benefits. The dissenting justices deemed the removal as a misapprehension of applicable law by the Assistant Clerk.

Power of attorney void when principal is judicially incompetent at time of execution.

In O'Neal v. O'Neal (16-1299) (July 5, 2017), the Court of Appeals declared void ab initio (i) two powers of attorney executed by a principal previously adjudicated incompetent (and whose competency had not been restored) and (ii) three deeds executed by the purported attorney-in-fact on behalf of the principal under the auspices of the voided powers of attorney. The court equated the capacity to execute a power of attorney to the capacity to execute a general contract and distinguished that capacity from the capacity to marry or to make a will, neither of which are per se absent when the principal has been adjudicated incompetent. The court provided that third parties dealing with attorneys-in-fact or agents have constructive knowledge of whether the principal was judicially incompetent at the time the principal executed the applicable power of attorney due to the public nature of incompetency court proceedings.

Decedent's estate not bound by arbitration clause in assisted living agreement when neither decedent nor any legal agent of decedent executed agreement.
In *Mclaurin v. Med Facilities of NC, Inc.* (16-1161) (July 5, 2017), in a claim by the estate of a decedent against the decedent's assisted living facility at the time of the decedent's death, the Court of Appeals held an arbitration clause in the assisted living agreement unenforceable against the decedent's estate when the decedent did not execute the agreement and the decedent's "responsible party" under the agreement, who did execute the agreement and by virtue thereof was responsible for the decedent's financial obligations to the facility under the agreement, had not been appointed the decedent's attorney-in-fact or otherwise legally designated as the decedent's agent at the time the agreement was signed (notwithstanding that such responsible party was also the decedent's executor).

**Pre-mortem gift of principal's real property by attorney-in-fact upheld when power of attorney specifically authorized gifts.**

In *Russell v. Russell* (17-21) (July 5, 2017), the Court of Appeals upheld a gift of real property made by an attorney-in-fact on behalf of a principal immediately prior to the principal's death when gifts of real property were specifically authorized by the power of attorney and no evidence indicated that the attorney-in-fact failed to take into account certain factors the power of attorney required the attorney-in-fact to consider in making gifts of the principal's property, which factors included the participation of the recipient in the decedent's care and the tax consequences of the gift.

**Purported surviving spouse not entitled to spousal allowance from decedent's estate when marriage deemed void.**

In *In re: Meetze* (16-796) (July 18, 2017), when two purported surviving spouses of the decedent claimed the statutory one-year spousal living allowance from the decedent's estate, the court awarded the allowance to the spouse whose purported marriage was earlier. The later of the two marriages was deemed void because the decedent was still married to the earlier spouse at the time – no divorce proceeding between the decedent and the earlier spouse was ever completed. The later spouse contested the evidentiary validity of the earlier spouse's marriage license because it was not separately authenticated in the court proceeding, but the court ruled that the marriage license, as a certified public record, was self-authenticating.

**Promissory note unenforceable when conveyance in consideration of note was unenforceable.**

In *Kyle v. Felsel* (16-1318) (Aug. 1, 2017), a promissory note was made in consideration of the grant of an option to purchase real property. However, the grantor of the option never executed the instrument conveying the option. Because the option, as an interest in real property, was unenforceable due to the statute of frauds, the note, even though executed by the grantee of the option, was not enforceable against the grantee due to lack of consideration.

**Statute of frauds applies to family settlement agreement dividing an interest in land.**

In *Blount v. Whitley* (16-1234) (Aug. 1, 2017), the court ruled that a family settlement agreement dividing an interest in land is subject to the statute of frauds.

**Selection of New York law in premarital agreement honored in North Carolina divorce proceeding.**

In *Wolfe v. Wolfe* (16-57) (Aug. 1, 2017), for equitable distribution purposes in a North Carolina divorce proceeding, the court honored a provision in the parties’ premarital agreement selecting New York law to govern the agreement. Under North Carolina law, an unchallenged provision in a contract selecting a foreign jurisdiction’s law is honored by the court unless it lacks a reasonable basis or is contrary to North Carolina law or public policy, even if neither party affirmatively petitions the North Carolina court to apply the foreign law. The court is responsible for applying the law validly selected by the parties. In *Wolfe*, the parties married in New York and later moved to North Carolina. The court by implication provided that the choice of New York law for the premarital agreement had a reasonable basis and that applying New York law to the premarital agreement was not contrary to North Carolina public policy.

**No survival action available for negligent act that causes decedent’s death; estate must bring wrongful death claim within shorter statute of limitations.**

In *Bullard v. Prime Building* (16-1279) (Sept. 5, 2017), the Court of Appeals dismissed a survival action advanced by the administrator of a decedent’s estate as time-barred because the alleged negligent act giving rise to the survival action caused the decedent’s death, and no viable alternate explanation for the decedent’s death existed, meaning that the administrator’s only available claim for such negligent act was a wrongful death action. Whereas the three-year statute of limitations for survival actions was still open, the two-year statute of limitations for wrongful death actions had expired.

**Estate must exhaust all assets before accessing joint bank account co-owned by decedent to pay estate claims.**

In *Fortner v. Hornbuckle* (17-44) (Sept. 5, 2017), among other procedural holdings, the court held that a bank account held jointly by a decedent and a survivor could not be accessed by the decedent's estate unless the account funds were necessary to satisfy claims against the decedent's estate after all other estate assets (including illiquid or non-income producing assets) had been exhausted.

**North Carolina Statutes**

**Trust Decanting Statute Replaced.**

SL 2017-121 – Uniform Trust Decanting Act (July 18, 2017) North Carolina’s Uniform Trust Decanting Act differs from the prior North Carolina trust decanting statute in the following notable ways:
Key Revisions:
- Statutory trust decanting can now be considered a modification of the existing trust or the transfer of trust assets to a separate trust. Under the prior statute, any decanting constituted the transfer of trust assets to a separate trust.
- The statutory decanting power may now be exercised by a trustee who is also a beneficiary of the trust. Previously, a statutory decanting could only be performed by a non-beneficiary trustee.
- Under the prior statute, 60 days' notice of a statutory trust decanting must be given to the qualified beneficiaries of the trust with respect to which the decanting power is being exercised. Under the new statute, such notice must also be given to the settlor of the trust (but only if the post-decanting trust would be a grantor trust with respect to the settlor), any person with the power to remove or replace the fiduciary performing the decanting, and all other fiduciaries of the trust. The notice must now include a copy of the original trust in addition to the post-decanting trust. Any party entitled to notice of a proposed decanting may initiate a court proceeding to approve or disapprove of such proposed decanting.
- If the decanting would eliminate the ability of the settlor or another person to terminate grantor trust status with respect to the trust, or if it would convert the trust to a grantor trust without providing the settlor the ability to terminate grantor trust status, then the settlor may unilaterally prevent the decanting from occurring.
- Statutory trust decanting is no longer expressly considered to be the exercise of a special power of appointment with respect to the trust property.

Helpful Additions:
- The statute expressly provides that third parties may rely on the valid exercise of the statutory decanting power.
- The statute includes a savings provision to “fix” purported exercises of the decanting power that are partially invalid.
- If additional property of the original trust is discovered after a decanting of all of the assets of the original trust, then such later discovered property is subject to the decanting without any new action being required.

Clarifications:
- The statutory decanting power is made expressly inapplicable to trusts established for charitable purposes (without any specifically designated beneficiaries).
- The statute provides that the settlor of a trust established or modified pursuant to decanting is the settlor of the original trust.

Provisions to Prevent Abuse:
- Any restrictions on the exercise of the decanting power under the provisions of the original trust must be included in the post-decanting trust.
- Either the qualified beneficiaries or the court must approve any express increase in fiduciary compensation pursuant to decanting.
- In general, trust decanting cannot be used to reduce the liability of the trust's fiduciaries.
- Decanting may not be used to change the power of a person to remove or replace the fiduciary performing the decanting unless either the power holder consents (and the change only applies to such power holder), the power holder and the qualified beneficiaries consent and a similar power is given to another person, or the court consents and a similar power is given to another person.

Additional Provisions of Note:
- The fiduciary power to distribute trust principal alone (without the power to distribute trust income) enables a fiduciary to exercise the statutory decanting power with respect to trust income and principal.
- The statute purports to make the decanting power available to any trust with its principal place of administration in North Carolina, regardless of the governing law of the trust. Query whether this provision expresses a strong public policy of North Carolina against the application of the law of a foreign jurisdiction selected by the grantor in the trust decanting context such that North Carolina law would override the grantor's selected law under N.C.G.S. Section 36C-1-107 for purposes of trust decanting.
- The prior statute's permissive language regarding the granting of powers of appointment pursuant to decanting has been expanded to reference powers of appointment granted to future beneficiaries in addition to current beneficiaries, but the statute provides that any powers of appointment granted to future beneficiaries may only be exercisable once such future beneficiaries become current beneficiaries.

Wills may be judicially modified to correct ambiguities; judicial modification of trusts to correct mistakes must be pursued through general trust modification avenues unless mistake resulted in ambiguous terms.

SL 2017-152 – Reform/Correct/Wills/Trusts (7/20/2017)

If the terms of a will are ambiguous and were affected by a mistake of fact or law, the court may reform the will to conform to the testator's intent as proved by clear and convincing evidence. The court may also modify a will to conform to the testator's tax objectives if the modification is “not contrary to the testator's probable intent.”

Reformation of trusts under N.C.G.S. Section 36C-4-415 to correct mistakes is now only available if the terms of the trust are ambiguous. Before, ambiguity was not a prerequisite for trust reformation under N.C.G.S. Section 36C-4-415 pursuant to mistake.

Power of attorney statute replaced.

Court orders generally effective regardless of timely stamping; suspended or disbarred attorneys removed from court-supervised fiduciary positions; estate accounting due dates clarified.


An order or judgment is valid and enforceable notwithstanding the initial failure of the court to affix a file stamp or date stamp thereto if the clerk later appropriately stamps and enters the order or judgment. The order or judgment would be effective as of the initial date of filing notwithstanding the later act of stamping. The parties to the action must be given notice of the later stamping.

If an attorney is serving as executor, collector, or guardian and is suspended or enjoined from practicing law or is disbarred, the attorney is removed from such fiduciary position.

The default due date for the annual accounting of an executor with respect to an estate is 30 days after the anniversary of the executor’s qualification (if no fiscal year is selected). The selection of a fiscal year for the estate by the executor would cause the annual accounting to be due by the fifteenth day of the fourth month following the close of the fiscal year.

Failure to respond to North Carolina Department of Revenue within prescribed windows causes termination of refund request.

SL 2017-204 – Various Changes to Revenue Laws. Under laws initially passed in 2007, if a taxpayer requests a refund from the North Carolina Department of Revenue and the department does not respond within six months, the request is considered denied, and the taxpayer must then further request review by the department within 45 days of the expiration of the original six-month period. The department is then legally required to respond. Session Law 2017-204 updates those procedures to provide that if the department responds by requesting additional information from the taxpayer, and the taxpayer fails to respond in any way to two separate requests for additional information from the department, each of which allows the taxpayer 30 days to respond, then the department’s denial of the taxpayer’s requested refund becomes final and not subject to further administrative or judicial review.

Spouse’s separate descendants may be beneficiaries of non-marital deduction trusts statutorily protected from creditors.

SL 2017-212 – Budget and Agency Technical Corrections. Under N.C.G.S. § 36C-5-505(c), any inter vivos trust created by a settlor that either qualifies for the marital deduction from the federal gift tax or is otherwise for the benefit of the settlor’s spouse and the settlor’s descendants during the lifetime of the settlor’s spouse is protected from the creditors of the settlor (subject to the provisions of the North Carolina Uniform Voidable Transactions Act). Session Law 2017-212 provides that the beneficiaries of such a protected non-marital deduction trust during the lifetime of the settlor’s spouse may also include descendants of the settlor’s spouse who are not descendants of the settlor.

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