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FDIC Insurance of Nontrust Accounts of Interest to Estate Planners

This article summarizes information that may be useful to estate planners about Federal Deposit Insurance Corporation (FDIC) insurance for bank accounts other than trust-owned accounts. Such nontrust accounts are owned by personal representatives, agents, conservators, custodians for minors, joint owners, and retirement plans. Accounts held by trustees are covered by a companion article in this newsletter, titled "Is Your Trust Covered?"

This article also describes the Certificate of Deposit Account Registry Service (CDARS) technique for expanding FDIC coverage and the temporary increase to FDIC insurance limits that took effect on October 3, 2008.

Deposits at credit unions are insured under their own set of rules, described at 12 C.F.R. part 745.

In General

The FDIC regulations are set forth at 12 C.F.R. part 330. Those regulations are also described in a nontechnical FDIC guide, *Your Insured Deposits – FDICs Guide to Deposit Insurance Coverage* (hereinafter YOUR INSURED DEPOSITS), which is available at www.fdic.gov/deposit/deposits/insured/index.html.

A depositor's accounts at one FDIC-insured bank or savings association are insured up to the FDIC limit that applies to each owner per ownership category. 12 C.F.R. § 330.3(a). Until the recent temporary increase, the FDIC limit had been $100,000, except for self-directed retirement accounts, which had a $250,000 limit. 12 C.F.R. §§ 330.1(n), 330.14(a), (b)(2).

Deposits in separate branches of an insured bank are not separately insured. Different kinds of accounts, such as savings, money market, and checking accounts, are also not separately insured.

The separate ownership categories of accounts entitled to separate coverage include single ownership accounts (those held in one person's name), joint ownership accounts, revocable trust accounts (including POD, ITF, and similar bank arrangements), irrevocable trust accounts, and retirement and other employee benefit plan accounts.

There is a six-month grace period in which separate insurance limits continue to apply after the merger of two insured institutions. 12 C.F.R. § 330.4.

Temporary Increase in FDIC Coverage Limits

The $100,000 FDIC insurance limit was temporarily increased to $250,000, effective October 3, 2008 through December 31, 2009. Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, § 136(a)(1) (amending 12 U.S.C. § 1821(a)(1)(E)). This gives depositors more breathing room for deposits that exceed $100,000 but not $250,000. However, unless the increase is made permanent, prudent depositors should assume that the $100,000 limit continues to apply for time deposits that mature after December 31,

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2009. Otherwise, if the FDIC limit returns to $100,000 on January 1, 2010, depositors holding time deposits above the $100,000 limit will be trapped until the deposits mature and can be withdrawn. That will be too late if the banks become insolvent.

Accounts Held by Agents, Custodians, and Conservators

To advise clients effectively on FDIC insurance for accounts held by agents, custodians, and conservators, lawyers should keep in mind (1) who is treated as the owner of the account and (2) what documentation is required so that the FDIC will give the account its full amount of insurance coverage.

Fiduciary accounts are those in which one person, such as trustee, custodian, or conservator, holds money on behalf of other persons. 12 C.F.R. § 330.5(b)(1). Fiduciary accounts are not a separate "ownership category" for FDIC purposes; rather, one must look at the ownership category assigned by the FDIC to each kind of fiduciary account.

The Principal, Not the Fiduciary, Is the Owner

Funds that are owned by one or more persons (the principals) and deposited into an account that is properly titled in the name of an agent, custodian, or conservator will be deemed to be owned by the principal and will be insured as if the funds were deposited in the principal's name. 12 C.F.R. § 330.7(a)-(b). For example, if a child owns a $20,000 bank account and the child's UTMA custodian holds a $90,000 account at the same bank, total FDIC coverage for the accounts until October 3, 2008 was $100,000, not $110,000. During the temporary increase in coverage through December 31, 2009, total FDIC coverage is $250,000.

Disclosure of Fiduciary Relationship on All Account Records

It is crucial that fiduciary accounts be set up to disclose the fiduciary ownership properly. The FDIC will recognize a claim for insurance coverage based on a fiduciary relationship only if the relationship is expressly disclosed in the deposit account records. 12 C.F.R. § 330.5(b). "Deposit account records" include account ledgers, signature cards, certificates of deposit, passbooks, and other books and records of the bank, including records maintained by computer, that relate to the bank's deposit-taking function, but "deposit account records" do not include account statements, deposit slips, items deposited, or cancelled checks. 12 C.F.R. § 330.1(e).

If the records are ambiguous on the nature of ownership, the FDIC has sole discretion to look beyond the deposit account records. 12 C.F.R. § 330.5(a)(1). However, depositors should not rely on this possibility.

If the deposit account records show a fiduciary relationship, the details of the relationship and the interests of the other parties to the account may be disclosed by the depositor's records rather than on the bank's records. 12 C.F.R. § 330.5(b)(2).

If the deposit account records do not show a fiduciary relationship, the deposit will be insured along with other accounts *of the fiduciary*, not the principal.

Accounts Held by Personal Representatives and Administrators

A decedent's account held by a personal representative or administrator will be insured along with all other deposits in the decedent's sole name at the same bank. 12 C.F.R. § 330.6(d). Here, as with accounts held by agents, custodians, and conservators, the personal representative or administrator should make sure that the fiduciary relationship is properly disclosed in the deposit account records.

There is an important grace period: the death of a deposit owner does not reduce the insurance coverage for the deposit for six months. 12 C.F.R. § 330.3(j). For example, if an account is jointly owned by A and B, and then A dies, the account is insured for six months in the joint ownership category (see below) and not as an account in B's sole name.

The dollar amount of coverage for a decedent's accounts is more limited than for revocable and irrevocable trust accounts. Coverage at a single bank is $100,000 (temporarily increased to $250,000), regardless of the number of heirs or devisees. In contrast, coverage for trust accounts can increase as the number of beneficiaries increases.

Practice Tip for Advising Fiduciaries

In light of these rules, lawyers should advise their fiduciary clients to sign all account opening forms, including signature cards, in their fiduciary capacities and not using their individual names. Examples of acceptable signatures include "Mary Smith, Personal Representative of the Estate of Joseph Smith" or "Mary Smith, as Custodian for John Smith."

Joint Ownership Accounts

Joint ownership accounts, including accounts owned by joint tenants with right of survivorship or by tenants in common, are insured separately from single ownership accounts maintained by the co-owners. 12 C.F.R. § 330.9(a). For example, a husband and wife could have up to $200,000 (temporarily increased to $500,000) in one or more joint accounts at the same bank and the deposits would be fully insured. These amounts would be in addition to the insurance on accounts owned solely by the husband or solely by the wife. *See* 12 C.F.R. § 330.9(b).

To qualify for insurance under this category, joint ownership accounts must meet the following three requirements as stated in 12 C.F.R. § 330.9(c):

- All co-owners must be "natural persons" (human beings);
- All co-owners must have equal rights to withdraw funds from the account; and
- All co-owners must sign the deposit account signature card (unless the account is a certificate of deposit or is established by an agent, nominee, conservator, or executor).

Nonqualifying joint accounts are treated as owned by the co-owners individually, in proportion to their actual ownership shares. Those shares are then added to other single ownership accounts of each co-owner at the same bank. 12 C.F.R. § 330.9(d).

Retirement Accounts

There is separate insurance for bank deposits held by certain self-directed retirement accounts and by other retirement accounts.

Certain Self-Directed Retirement Accounts

Certain self-directed retirement accounts owned by the same person at the same bank are added together, and the total is insured to $250,000. (The $250,000 limit already applied before the recent general increase in insurance that started on October 23, 2008 and is unaffected by the new legislation.) These self-directed accounts are traditional and Roth IRAs; Simplified Employee Pension (SEP) IRAs; Savings Incentive Match Plans for Employees (SIMPLE) IRAs; Section 457 accounts; self-directed defined contribution plan accounts, such as self-directed 401(k) plans; and self-directed Keogh plan accounts. 12 C.F.R. § 330.14(b)(2); Your Insured Deposits, *supra*, at 7-8.

Naming beneficiaries for these accounts does not increase the deposit insurance coverage.

Other Retirement Accounts

Other employee-benefit plans are insured at a single bank up to $100,000 for each participant's noncontingent interest in the plan. 12 C.F.R. § 330.14(a); Your Insured Deposits, *supra*, at 21-22. The $100,000 amount temporarily increased to $250,000 starting on October 3, 2008.

The CDARS Alternative

An alternative to opening separate accounts at several different banks is CDARS. There are nearly 2,500 member banks across the country, including two dozen in Oregon, that offer the CDARS program for depositors. See www.cdars.com for a list of participating banks.

CDARS is operated by the Promontory Interfinancial Network. It allows a customer to deposit funds of up to $50 million in one participating bank. The deposit is then dispersed in individual CDs of up to $100,000 each in participating banks across the country. This service offers three important benefits:

- There is no need for the depositor to open separate accounts;
- All deposits are included on one bank statement at one interest rate, and one Form 1099 is issued; and
- The customer pays no additional charge (although the bank is charged, which may reduce the interest rates offered).

CDARS offers a reasonable alternative for fiduciaries seeking to protect deposit accounts while minimizing the time and expense associated with administering a number of separate accounts. Because the increase in FDIC insurance to $250,000 is temporary, for now participating CDARS banks are continuing to place deposits in $100,000 rather than $250,000 increments.

Jonathan A. Levy
Sara L. Butcher

Cavanaugh Levy Bilyeu LLP
Portland, Oregon

Banking Crisis

The Newsletter Board delayed this issue of the Newsletter so that we could include the two articles on FDIC insurance. We profusely thank the three authors, Jonathan Levy, Michelle Johansson, and Sara Butcher, who wrote the articles in a short timeframe and then rewrote them as the laws continued to change. Please keep in mind that these articles present snapshots of a rapidly evolving situation.

Even after the articles went to press, Jonathan Levy sent additional information:

> The FDIC has adopted a "Temporary Liquidity Guarantee Program" that will insure without dollar limit personal and business checking deposit accounts that do not earn interest. This unlimited insurance coverage is temporary and will remain in effect for participating institutions until December 31, 2009. This enhanced coverage will apply to institutions that sign up for it and pay a surcharge. *See* FDIC Press Release 100-2008, Oct. 14, 2008, at
>
> http://www.fdic.gov/news/news/press/2008/pr08100b.html.

Daily Journal of Commerce Publication Update

Those of us practicing in Multnomah County have been spoiled by the Daily Journal of Commerce (DJC), which automatically published the Notice to Interested Persons without any action by us. DJC was recently purchased by another company, and its procedures have changed. To trigger publication of the notice, the attorney must send a written request to DJC. The request may be given by fax or by email, and should include the decedent's name, the court and case number. The contact person for notices at the DJC is Marc Caplan. His email is *marc.caplan@djc-or.com*, and his fax number is 503-222-5358. Requests for publication should be sent to Mr. Caplan.

Stephen J. Klarquist
Zalutsky, Klarquist & Reinhart, P.C.
Portland, Oregon

Liability for Referrals to Other Lawyers

My client—a longtime, solid client—is angry, and has asked to meet tomorrow morning. Years ago, I did an estate plan for him, and since then he has on occasion hired me for one reason or another. When his father died, I secured my client's appointment as personal representative of the estate, and I continued to represent him. The deceased owned real property in California that was subject to a reverse mortgage. Without much thought, I pulled out my national directory for the Academy of Estate Planning Attorneys (AEPA), found a name I recognized from an AEPA Conference that I attended five or six years ago, and passed the name along to the client. I have given this referral considerable thought since then. The California attorney took too much time opening the ancillary probate proceeding in California and then could not get the real property sold and the lender foreclosed on the mortgage. Now all the estate has to show for its effort to marshal and sell the California property is a bill from an attorney whose delay in opening probate may constitute malpractice. The estate beneficiaries are not happy, and neither is my client.

If my client's anger is directed at me, I need to understand my potential liability for making the referral. This liability could arise from one or a combination of three factors. First, the tort of negligent referral may arise as a cause of action against me. Second, based upon my relationship with the California attorney, I could be jointly liable for his malpractice. Finally, the Oregon Rules of Professional Conduct have guidelines for referrals. Before my meeting tomorrow morning, I will outline my exposure arising from these three factors, and summarize how I can mitigate this risk in the future.

The Tort of Negligent Referral

The most oft-cited case regarding the tort of negligent referral is *Tormo v. Yormark*, 398 F. Supp. 1159 (D.N.J 1975). In this case, a client asked Devlin, his New York attorney, for a referral to a New Jersey personal injury attorney. Devlin made the referral, and the New Jersey attorney ended up embezzling the injury settlement.

When the client sued Devlin for malpractice, Devlin moved for summary judgment. Devlin argued that he could not have committed malpractice because no attorney-client relationship existed. The district court rejected the summary judgment motion, indicating that Devlin "was under a duty to exercise care in retaining [the New Jersey attorney] to ensure that he was competent and trustworthy." *Id*. at 1170.

The court asserted that Devlin adequately researched the New Jersey attorney's credentials when he confirmed that the attorney was licensed by the state of New Jersey before making the referral. Although the attorney was under an indictment for insurance fraud at the time of the referral, and the indictment that had not escaped scrutiny in New Jersey newspapers, the court did not fault Devlin for being unaware of the indictment. The court did fault Devlin for missing other clues that the New Jersey attorney was not trustworthy. For example, the attorney had cold-called Devlin regarding the case and solicited a referral. This violated state bar ethical rules, and should have put Devlin on notice that the attorney was not worthy of a referral, according to the court.

The tort of negligent referral makes no appearance in Oregon case law. Other jurisdictions have considered and rejected it. Pennsylvania courts, for example, have expressly ruled that no such cause of action exists. *See Bourke v. Kazaras*, 746 A.2d 642 (Pa. Super. Ct. 2000). The U.S. District Court for the Eastern District of Pennsylvania has also rejected this tort, in the strongest of terms: "[M]any attorneys routinely refer cases because they cannot or do not want to handle them, or because they believe that the receiving attorney has greater expertise in the relevant subject area. Any holding that they nevertheless should be liable for the receiving attorney's conduct of a case would be logically and legally unpersuasive, and could unduly disrupt a process integral to the profession . . . ." *Felker v. O'Connell*, Civ. A. No. 89-7307, 1990 WL 31912, at*1 (E.D. Pa. Mar. 20, 1990).

How would an Oregon court regard the tort of negligent referral? If the injured client were vulnerable enough, if the injury were deep enough, or if the receiving attorney's conduct or prior history were disturbing enough, this tort could find footing in any jurisdiction. The questions that were particularly important to the court in *Tormo* appear to be these: Did the referring attorney establish an attorney-client relationship? Did the referring attorney uphold his duty of care in making the referral, particularly in ensuring the trustworthiness of the attorney receiving the referral?

In my case, I represented to my client that the California attorney was reputable, based upon my knowledge of him from the AEPA seminar. In *Tormo*, the court found that Devlin owed a duty of care to the client when he had expressed that the New Jersey attorney was a "good well-qualified attorney." 398 F. Supp. at 1166. Like Devlin, I had vouched for the attorney and perhaps created a duty to the client in the process. However, the California attorney had not waved the red flags of untrustworthiness that the New Jersey attorney had waved to Devlin. In addition, the California attorney was not under indictment when I made the referral. The New York court did not expect Devlin to proactively research the New Jersey attorney, only to confirm that the attorney had a license. I had not even done that. Still, the New Jersey attorney's background and behavior were so questionable in *Tormo* that the court may have been uniquely motivated to impose a duty on Devlin to protect the client. The California attorney's background and reputation are not so dismal. I may be safe from liability for this cause of action.

Joint Venture/Joint Liability

Courts in Oregon and other states have examined the relationship between the referring and the receiving attorney to determine whether the referring attorney has joint liability for the receiving attorney's negligence. In my case, I did not split fees with the California attorney. I did, however, periodically check in with him to monitor progress and to provide information regarding the decedent and the Oregon probate case. On occasion, I would report to my client regarding my discussions with the California attorney.

The absence of a fee split or other fee arrangement may be my saving grace. In *Scott v. Francis*, 314 Or. 329, 838 P.2d 596 (1992), an Oregon attorney associated another attorney to manage a malpractice action. The attorneys agreed to split fees, but they missed a filing deadline and lost the opportunity to bring the malpractice action. The attorneys blamed each other, but the court found them jointly liable. Similarly, a Florida court, basing its decision in part on Florida ethical rules that differ from Oregon's, determined that if a referring attorney has a fee-splitting agreement with the receiving attorney, written or implied, joint liability exists, regardless of whether the referring attorney was actively involved in the case. *See Noris v. Silver*, 701 So. 2d 1238 (Fla. Dist. Ct. App. 1997); *Duggins v. Guardianship of Washington*, 632 So. 2d 420, 428 (Miss. 1993) (stating that "intent to share both the responsibility and the profits from this representation clearly demonstrate the presence of a joint venture").

These cases indicate that I could be found to be jointly liable for the California attorney's malpractice if (1) I was actively involved in or monitored the California case, (2) I took a referral fee or had another fee arrangement with the California attorney, and (3) my client had the reasonable expectation that I was overseeing or otherwise involved in the California case. Although the absence of a fee arrangement is a certainty, I can construct creditable arguments on both sides of the other factors.

Oregon Rules of Professional Conduct (ORPC)

Although the ORPC have several rules that guide referral situations involving nonlawyers, *see* ORPC 5.4(a) sharing fees with nonlawyer, 5.5(a) assisting nonlawyer in unlawful practice of law, 5.4(c) influence of referral source on legal counsel, 7.2(a) compensation for recommendations, only one focuses on referral relationships between lawyers. ORPC 1.5(d) indicates that lawyers who are not in the same firm can split fees only if the client gives informed consent and if the total fee for all services rendered is not excessive.

The Oregon rule is gentle compared to the ABA model rule, which indicates that a fee split is appropriate if either the division of fees is proportionate to hours worked or each lawyer is jointly responsible for work. It is the ABA rule, modified and adopted in Florida, that endangered a referring attorney who directed a personal injury plaintiff to an Illinois attorney and faced potential liability for the Illinois attorney's malpractice. *See Noris*, 701 So. 2d 1238. Although the referring attorney took no action in the Illinois case, the Florida court found that if the two attorneys entered a fee-splitting agreement, the referring attorney may have a financial interest in the malpractice case that could create joint liability. *See id.* at 1240. The court relied on Florida's ethical rule regarding fee agreements in rendering this decision.

Oregon's ethical rule does not imply joint liability from fee agreements, and, regardless, I had no fee agreement with the California attorney. My exposure to an ethical violation arising from ORPC 1.5(d) appears to be nominal.

Limiting Liability

If I had handled this referral differently, I could have narrowed my potential liability—arising from the tort of negligent referral, joint liability, or the ORPC—considerably. Clearly, several steps take the risk out of referral:

- Referral to a referral service. Several jurisdictions have ruled that a referral service is not liable for the misconduct of the attorney receiving a referral. *See Weisblatt v. Chicago Bar Association*, 684 N.E.2d 984 (Ill. App. Ct. 1997); *Bourke*, 746 A.2d 642.
- Indemnification from the receiving attorney.
- Interview of the receiving attorney before referral, to inquire about malpractice coverage and experience.
- Basic investigation of the receiving attorney through Internet or state bar inquiry, or both.
- Communication with client in writing, both in a letter and in retainer agreement, that the referring attorney is not vouching for the receiving attorney or monitoring his or her work.
- Avoidance of fee-splitting arrangements with the receiving attorney.

In my case, the only prudent step that I took was by habit rather than by design: I did not negotiate a fee split with the California attorney. In my meeting tomorrow, my client will most likely care little about that. I will go into it believing that my liability risk is low. The case is not outrageous enough to support a tort action that has never been recognized in Oregon or to overcome the public benefit of lawyer referrals. I did not share fees or interact with the California attorney sufficiently to earn joint liability for his actions. I breached no ethical rule in making the referral. Still, although liability may be low, my apprehension going into this meeting is high. I tend to feel this way when I know I could have handled something better.

Tim McNeil
Davis Pagnano & McNeil LLP
Portland, Oregon

Author's note: For a more comprehensive analysis of this issue, see Barry R. Temkin, *Can Negligent Referral to Another Attorney Constitute Legal Malpratice?*, 17 TOURO LAW REVIEW 639 (2001).

Why Every Estate Planner Should Know More About Probate Litigation

Many estate planners prefer an estate and trust practice because it is transactional, or because they want to avoid appearing in court. However, in recent years, estate and trust litigation has become more common. The increase in probate litigation may be due to the rise in population and to the rise of litigation in general. The increase is probably also due to the extensive use of revocable living trusts and the resulting protracted administration, the transfer of wealth by the baby-boomer generation, the frequency of divorce and blended families, and general discord in the family unit. Probate litigation includes will and trust contests; lawsuits against trustees, personal representatives, and other fiduciaries for breach of fiduciary duty; claims against attorneys and other third parties who allegedly assisted in the breach of a fiduciary's duty; and requests for interpretation of or instructions regarding a will or trust.

Lawyers who draft estate planning documents can provide better service if they are aware of the problems that can occur when an estate plan is administered, so they can take certain precautions when drafting. Estate planning, administration, and litigation are all interrelated. Although this article does not provide an exhaustive discussion of all possible probate litigation issues, it identifies some of the most common matters lawyers should consider in representing estate planning clients.

Tax Awareness

Tax issues commonly arise in estate planning and administration. A lawyer should realize the limit of his or her tax knowledge to properly assist a client. Typically, the size of the estate is indicative of the level of tax complexity. An estate planner with tax credentials or sufficient tax knowledge and experience often advises high net worth clients. The same rule applies to advising fiduciaries in the administration of estates and trusts. Issues that might come up in a taxable estate include estate tax returns, distributions of income and principal, generation-skipping transfer taxes, and the like. In a situation involving tax questions, a client should seek advice from an attorney with experience in these matters.

The preparation of appropriate tax returns is another critical matter. Collaboration and communication between the lawyer and the tax preparer are important. A fiduciary is held to high standards when filing required tax returns, and the fiduciary must be properly advised to meet the responsibilities for such filings. A personal representative or trustee is responsible for filing the decedent's final income tax returns, as well as the estate tax return or the trust's fiduciary income tax returns. The Internal Revenue Service ("IRS") holds the fiduciary liable for the accuracy of these returns. The IRS defines "executor" broadly and includes anyone appointed by the court to administer the estate, including a trustee. In addition, "any person with actual or constructive possession of any property of the decedent" is also defined as an executor who may be liable for filing an erroneous return. The IRS holds all executors personally liable for penalties or false errors on the return. The Oregon Department of Revenue similarly holds any person having actual or constructive knowledge of the decedent's property responsible for filing such returns.

No Contest Clause

A client may want to disinherit a child or give one child less than other children. Treating the same class of beneficiaries unequally increases the chances of litigation during administration. The client may also worry that a child or other person will seek to challenge the estate plan. A no contest clause, or *in terrorem* clause, provides that any person who unsuccessfully challenges the validity of a testamentary document will forfeit any interest they had in that estate. *See* ORS 112.272. If a client completely disinherits a child, the child may have nothing to lose by filing a contest claim. One solution is to include a gift to the child with a well-drafted no contest clause. This may deter the potential contestant and save thousands of dollars and months (or even years) of litigation. Estate planners should discuss with clients the risks associated with disinheritance of an heir, and advise the clients to take steps to minimize the risk of future litigation.

Choice of Fiduciary

All fiduciaries have strict duties, and fiduciaries should be selected based on their character and skills. Clients often do not realize the magnitude of tasks and duties that a fiduciary must fulfill, so the attorney should advise and guide the client in selecting the most appropriate fiduciary. The selection of an appropriate fiduciary will directly affect the beneficiaries' satisfaction with the administration.

Naturally, a parent often wants to treat children equally. In doing so the parent may want to nominate all of the children as co-equal fiduciaries. Unfortunately, co-fiduciaries can create difficulties. Disputes may arise among the co-fiduciaries during administration. Family situations may then become strained and the business of administration may suffer. The attorney can assist the client to choose the best person to serve as fiduciary, thereby reducing the possibility of future costly litigation. If a single family member cannot be chosen, a compromise may be to name a neutral third-party professional, either a corporate fiduciary or a private professional organization.

Fulfilling Fiduciary Duties

A primary duty of a fiduciary is the duty of loyalty to the beneficiaries. ORS 130.655. The individual or institution that serves as a fiduciary becomes legally obligated to act in the best interests of the beneficiaries and in accordance with the terms of the trust or the will and applicable laws.

Breach of fiduciary duty is a problem estate and trust litigators frequently encounter. The fiduciary must comply with the standard of care spelled out in the trust document and under Oregon law. A common error that occurs during administration is a fiduciary's failure to properly transfer assets to the estate and fund sub-trusts pursuant to the terms of the trust. The fiduciary duties can become complicated when the trustee has duties both to income beneficiaries and to the remainder beneficiaries who will ultimately receive the trust's principal.

An attorney representing a fiduciary should be aware of all fiduciary duties and inform the client about the duties and obligations required by law. For example, a trustee may be held personally responsible during the course of the administration if the trustee is found to be personally at fault due to the trustee's intentional or negligent conduct. *See* ORS 130.845(2). It is good practice to discuss the numerous fiduciary duties with fiduciary clients at the outset of representation and follow up these discussions with a letter itemizing these duties. A detailed description of the various fiduciary duties is a good reference tool during their administration. Watch for "Trustee Duties - A Refresher" in the January 2009 issue of this newsletter.

Estate and trust attorneys should also be aware that liability for breach of fiduciary duty may extend to third-party professionals such as attorneys and accountants who advise the fiduciary in the estate's administration.

Choice of Law

The choice-of-law provision in a trust typically appears at the end of the document and is often overlooked. However, because the applicable law can affect a trust's validity, construction, administration, meaning, or effect, a trust's choice of law provision is one that should be carefully considered. If the trust is silent regarding choice of law, then the law of the state or other jurisdiction with "the most significant relationship to the matter at issue" will apply. ORS 130.030. The trust document can also indicate the trust's principal place of administration, although the Oregon Uniform Trust Code provides some limits on that choice. *See* ORS 130.022.

A narrowly tailored choice-of-law provision can bind a trustee, while a broadly drafted provision allows the trustee more choice in enforcing and administering the trust. For example, if a trust's choice-of-law provision applies Oregon law in effect in 1975, the trustee may not have the flexibility to do what is best for the trust, including applying laws that would support the trust's validity or transfer the trust's situs to a state with a better income tax treatment. Choice of law quickly and easily becomes a complex topic. A detailed discussion of choice of law is beyond the scope of this article, but being aware of the issue is half the battle.

Drafting with Clarity and Specificity

Estate planning documents should be as clear and concise as possible to accurately reflect the client's intent and avoid later questions or disputes. It is wise to include at least two successive beneficiaries and fiduciaries, to avoid a distribution or vacancy question. When ambiguities or questions arise in the estate plan, a petition for instructions can be made to the court to determine the issue. Whether the petition is contested, however, depends on the case.

Disputes involving personal property are prevalent in estates and trusts, due to the emotional and sentimental attachments people have to such property. An attorney should work with his or her client to provide accurate descriptions of any specific items being given to individuals. Including specific bequests in the will may be the safest option, because the lawyer has control over the drafting, but some clients want to list specific items of personal property and who they go to in a separate document. The separate document can be incorporated by reference into the will, but the lawyer should remind the client that in Oregon changes made to the document after the will is executed will not be given effect unless the client executes a new will or codicil.

A will or revocable trust can identify who should resolve disputes regarding the personal property during administration. A provision stating who is to bear the costs of packing, storing, insuring, and shipping personal property items may also be helpful.

Any unique or specific wish of the client should be clearly drafted. Several years ago, the author was involved in a case involving a $20 million trust and a nonprofessional trustee who received $250,000 a year as his fee. The trustee argued that the deceased trustor had intended and agreed to this fee, yet the trust document provided for the usual, and subjective, reasonable fee. Although the drafter of the trust recalled general discussions with the trustor regarding the trustee's fee, extensive discovery did not confirm a specific fee agreement between the trustor and trustee. If the trustor had intended a specific trustee's fee (particularly a set dollar amount) the trust document should have detailed the fee.

Conflict Waivers

A lawyer should review potential and actual conflicts with each client, particularly when the lawyer represents spouses, co-fiduciaries, or more than one family member in an estate. Analyzing who is or should be the client is the first issue. If a conflict-of-interest waiver is needed, it must be discussed, put in writing, and signed by the necessary parties. It is good practice to obtain a written conflict waiver when representing co-trustees and when representing couples, whether they are married, unmarried, or registered or not registered as domestic partners. The lawyer should inform all parties that if a conflict arises each party may need to seek independent counsel and that the lawyer cannot take one side or the other.

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Get It in Writing

Although it is always wise to keep all client files thoroughly papered with relevant information, this is particularly true when a dispute is on the horizon. If a problem arises it is critical that the file is documented with appropriate, and legible, memoranda and confirming letters. Agreements or compromises of claims made among the parties should be reduced to writing and executed. Oral agreements alone may not satisfy the statute of frauds or other statutes that require a sufficient writing.

If a file is thoroughly documented with the attorney's observations, analysis, and communications, future disputes may be avoided. If these writings are absent from the file, then the lawyer must rely on witnesses who may not remember the past or are unavailable or even deceased. Granted, taking the time to make good notes is time-consuming, but you will always be glad you did, especially if litigation ensues.

Managing Client Expectations

Each client should be informed of the risks his or her estate plan may face in the future. In addition, a fiduciary should be advised of the risks the fiduciary may encounter if the fiduciary does not fulfill the fiduciary duties. Properly advising clients of the risks and benefits of an estate plan goes hand in hand with properly managing their expectations. Likewise, managing expectations is the primary objective when working with families in contested probate matters.

Discovery and Discoverable Documents

A common misconception regarding the attorney-client privilege is that it provides absolute protection from inquiry into attorney-client communications. In fact, there are significant exceptions to this rule. ORS 40.225(4)(b) states there is no privilege with respect to communications between the attorney and client regarding the estate plan when a will or trust is being contested. The case of *Moeller v. Superior Court*, 947 P.2d 279 (Cal. 1997), is important because the court found the "office" of trustee is the holder of the attorney-client privilege, not a particular trustee. The author had a case involving a professional conservator against a professional trustee, in which the *Moeller* case was used by the professional trustee to obtain the incapacitated and resigned trustee's privileged attorney-client information regarding her estate plan. The professional successor trustee, not the conservator, retained control of the privileged information.

The power between a trustee and conservator can be interpreted differently, however, under the Oregon Revised Statutes. *See* ORS 125.420, 125.025, 125.650(5)(b). The *Moeller* case also states that when a fiduciary hires an attorney for assistance in administering a trust, the fiduciary, not the trust, is the attorney's client. *Moeller*, 947 P.2d at 282.

When a matter appears to be headed toward litigation, it is a good idea to draft all further correspondence and documents knowing that they could be discovered at a later date. It can be problematic to have an unfavorable letter appear before the judge, although a litigator would relish discovering and producing such a letter.

Mediation

An attorney should be aware of ways to resolve potential or actual disputes informally, thereby saving the time, expense, and emotional toll that can result from litigation. Mediation is a particularly effective solution for estate and trust disputes because the parties are often related and may have a difficult history, and because emotions often run high in these relationships. Frequent differences of opinion about the facts of the case are also common. The uniquely private matters that surface in estate and trust disputes are protected in mediation. A will or trust could make mediation mandatory or discretionary as a means of resolving family disputes. Mediation with a trained probate mediator who can help the parties fashion creative solutions to estate and trust problems can be productive and appealing to families involved in emotional crises. Mediation may help clients avoid a divisive conflict.

In mediation, the parties' mutually agreed on mediator does not make any ultimate findings, but instead tries to help the parties and their attorneys resolve the dispute through an agreeable settlement. Often the agreement is memorialized in writing and signed during the mediation. If all parties agree to the settlement, the dispute is resolved. If the parties cannot reach a global settlement, the mediation ends and the case moves toward trial. If mediation is not successful, all settlement discussions during mediation remain completely confidential and cannot be used in litigation later.

Conclusion

The more conscious an estate planner is of the risks that give rise to probate litigation, the more the practitioner can properly advise clients of these problems and plan to avoid them. Estate planning clients want an estate plan that will be smoothly administered and will avoid disputes, and these clients may be particularly concerned about avoiding the costs, delays, and divisiveness associated with litigation. An estate planner's knowledge and awareness of probate disputes (and how to avoid them) will allow the lawyer to properly advise clients. That advice will produce better estate plans, allow for smoother administrations, and ultimately yield happier clients.

Hilary Newcomb
Law Offices of Nay & Friedenberg
Portland, Oregon

Is Your Trust Covered?

In 1933, Congress created the Federal Deposit Insurance Corporation (FDIC) to address the losses to account holders caused by widespread Depression-era bank failures. The FDIC insures "deposit accounts"—including savings accounts, checking accounts, and certificate of deposit accounts—in banking and thrift institutions. Because deposit accounts have a relatively low rate of return, many trusts concentrate their holdings in real property or securities. But almost every trust will have at least one deposit account, such as a checking account for paying ordinary bills and expenses, and it is common for trust assets to be temporarily consolidated in a deposit account, such as during the period of administration immediately after the death of a settlor.

Especially in light of recent bank failures, practitioners should remember the importance of advising their estate planning clients how to minimize the risk to trust holdings through FDIC insurance, and should periodically review the holdings of any trusts they administer to ensure that those trusts' deposit accounts are adequately insured. The FDIC provides an insurance calculator on its Web site, at http://www2.fdic.gov/EDIE/.

This article reminds practitioners of the basic principles that apply in determining the applicability and amount of FDIC insurance.

Basic Definitions

Regardless of whether funds are held in a revocable or irrevocable trust, to determine whether the total deposits at a bank held by a client's trust are within FDIC coverage limits, the estate planner must answer the following questions: (1) Who *owns* the deposits? (2) Under what FDIC *ownership category* does the owner seek to qualify? (3) Does the depositor meet all of that *ownership category's requirements* for coverage?

Who is the owner?

The settlor of the trust is the "owner" of funds held in a trust for purposes of calculating FDIC coverage; the identity of the trustee is irrelevant.

What ownership category applies?

Total FDIC coverage is calculated according to "ownership categories." Funds that are held in the same right and capacity belong to the same ownership category. All deposit accounts in the same ownership category (regardless of the type or number of accounts) are added together and insured up to the maximum FDIC insurance amount. *See FDIC Guide to Calculating Deposit Insurance Coverage for Revocable and Irrevocable Trusts* (hereinafter *Guide*) at 3 (Jan. 2008). (The *Guide* is undergoing revisions; once completed it is expected to be posted at www.fdic.gov/deposit/deposits/di_trust_accounts/.)

Ownership categories include but are not limited to single accounts, joint ownership accounts, revocable trust accounts, irrevocable trust accounts, and employee benefit plan accounts. This article covers the methods of calculating deposit insurance coverage for the ownership categories of revocable trusts and irrevocable trusts only. Other types of ownership categories have other rules for coverage. Please consult the FDIC Web site at www.fdic.gov/deposit/index.html.

What ownership category requirements apply to deposits held in revocable and irrevocable trusts?

Revocable trusts and irrevocable trusts are separate ownership categories, with each having its own set of requirements. On September 26, 2008, the FDIC issued interim regulations that simplify the calculation of insurance coverage for revocable trusts. *See* Deposit Insurance Regulations; Revocable Trust Accounts, 73 Fed. Reg. 56,706-12 (Sept. 30, 2008) (amending 12 C.F.R. pt. 300). The interim rules also provide that irrevocable trusts springing from revocable trusts will continue to be insured under the revocable trust rules. *See interim* 12 C.F.R. § 330.10(h)-(i); 73 Fed. Reg. 56,712.

Revocable Trust Accounts – *Compare Interim* 12 CFR § 330.10 *with Former* 12 C.F.R. § 330.10

Within the ownership category of revocable trusts, the FDIC recognizes both formal and informal revocable trusts. Informal trusts include "pay on death" accounts, "in trust for" accounts, and "transfer on death" accounts. Formal trusts, also known as "living trusts," are those trusts created for estate planning purposes. Before the issuance of the interim rule, FDIC coverage under the revocable trust account category was available only if a "qualifying beneficiary trust relationship" was established. *See Guide* at 8. A qualifying beneficiary was narrowly defined as the owner's spouse, child, grandchild, parent, or sibling. *See former* 12 C.F.R. § 330.10(a). The "kinship" requirement combined with the increasing complexities of formal trusts caused much confusion among banking personnel and the general public. The former regulations made it difficult for institutions to determine quickly and accurately the amount of FDIC coverage for revocable trust deposit accounts in the event of a bank failure. The new rule disposes of the strict qualifying beneficiary requirement; now coverage is available for *any* beneficiary, provided the beneficiary is a natural person or a charitable or nonprofit organization. *See interim* 12 C.F.R. § 330.10(c); 73 Fed. Reg. 56,711. Note that the requirement of a "trust relationship" remains. *Compare interim* 12 C.F.R. § 330.10(a)-(b) *with former* 12 C.F.R. § 330.10(a)-(b). A trust relationship is established when the account provides that the beneficiary receives the funds on the owner's death. *See also Guide* at 8.

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Informal Revocable Trusts

For an informal revocable trust to qualify for insurance coverage under the revocable trust category, the deposit must meet the following requirements:

(1) The account must include commonly acceptable terms such as "payable on death," "in trust for," or "as trustee for." These terms can be abbreviated.

(2) The beneficiaries must be identified by name in the deposit account records of the bank. For example, "in trust for my three sons" does not trigger additional FDIC insurance, even if the identity of those sons is readily ascertainable by reference to materials outside the bank's deposit account records. *See, e.g., interim* 12 C.F.R. § 330.10 (b); 73 Fed. Reg. 56,711.

Formal Revocable Trusts

As with informal revocable trusts, revocable trusts must meet certain threshold requirements before FDIC coverage is available in the revocable trust ownership category.

For a formal revocable trust to qualify under the revocable trust category, the account must state that the account is held pursuant to a trust.[1] For example, holding the account as "John Q. Public, as trustee of The John Q. Public Revocable Living Trust," satisfies this requirement. As of April 2004, it is no longer necessary for the banking institution to have a copy of the trust agreement on file. The beneficiaries need not be named on the account, though they must be readily identifiable from the trust agreement.[2] Additionally, only beneficiaries who are entitled to receive the trust monies on the owner's death are considered; contingent beneficiaries are ignored for purposes of determining coverage pertaining to formal revocable trust accounts.

Before the issuance of the interim regulation, the basic rule for both formal and informal revocable trusts was that the owner was entitled to the equivalent of the "standard maximum deposit insurance amount" for each qualifying owner-beneficiary pair. Further, there was "no limit on the number of qualifying beneficiaries that an account owner [could] designate for a revocable trust deposit." *See former* 12 C.F.R. § 330.10(a), (f).

On the whole, removal of the qualifying beneficiary requirement results in increased coverage for most revocable trust account deposits. Additionally, the passage of the Emergency Economic Stabilization Act by Congress in early October 2008 temporarily increases the FDIC standard maximum deposit insurance amount from $100,000 to $250,000.[3] For more information on this new law, please refer to the companion article in this issue, "FDIC Insurance of Nontrust Accounts of Interest to Estate Planners," by Jonathan A. Levy and Sara L. Butcher.

Revocable Trust Deposit Accounts Having Five or Fewer Beneficiaries

The interim rule drastically simplifies FDIC coverage of revocable trust accounts when the trust names five or fewer beneficiaries. In such cases, coverage for an owner's revocable trust accounts is determined by multiplying the number of different beneficiaries named in the trust(s) by $250,000. *See interim* 12 C.F.R. § 330.10(a); 73 Fed. Reg. 56,711.

For example, assume Fred is the owner of the Flintstone Revocable Trust (Trust), a formal revocable trust, with a total deposit amount of $1 million. The trust names four beneficiaries who are entitled to a one-fourth share upon Fred's death. The beneficiaries are his wife, Wilma; his daughter, Pebbles; his neighbor, Barney; and the Bedrock Humane Society (a charity).

Under the old rules, the available coverage for the Trust in the *revocable trust account ownership category* would have been $500,000 because there were only two qualifying beneficiary pairs (Fred-Wilma and Fred-Pebbles). Each pair would have been insured for up to $250,000. The remaining shares, totaling $500,000, would have been insured up to a maximum of $250,000 under the owner's single deposit account, leaving $250,000 of the total deposits in the trust account uninsured.

Under the new simplified rule, the total FDIC coverage available for the Trust in the revocable trust account ownership category is $1 million, which is calculated by multiplying the number of beneficiaries (four) times $250,000. The new rules provide that Fred's $1 million deposit is insured in its entirety.

NOTE: If Fred and his boss, Mr. Slate, were co-owners of the Trust, then the Trust would be insured up to a maximum of $2 million because each owner is presumed to own an equal share of the trust deposit. Thus Fred's "share" would be insured up to a maximum of $1 million (four beneficiaries multiplied by $250,000). Mr. Slate's "share" receives the same treatment. The total coverage afforded the Trust is $2 million.[4] *See interim* 12 C.F.R. § 330.10(f); 73 Fed. Reg. 56,711-12.

In this next example, assume the same facts as in the initial example, but assume also that Fred holds $250,000 in an informal revocable trust in the form of a payable-on-death (POD) account in which he names Wilma and his neighbor Betty equal beneficiaries. The account contains the term "POD" in the title, and it specifically names the beneficiaries in the deposit account records; therefore it qualifies for coverage in the revocable trust ownership category. Fred's two revocable trust accounts have a combined value of $1.25 million and a total of five *different* beneficiaries. The maximum coverage available in the *revocable trust category* is $1.25 million—calculated by multiplying the number of beneficiaries (five) times $250,000. Although Wilma is named in two different trust accounts, she is only counted once—naming the same beneficiary in more than one revocable trust account will not increase the total coverage. *See interim* 12 C.F.R. § 330.10(a), ex. 2; 73 Fed. Reg. 56,711. The new rules provide that Fred's deposits are insured in their entirety.[5]

Revocable Trust Deposit Accounts Having More Than Five Beneficiaries

If a revocable trust has more than five beneficiaries, determination of coverage requires an additional step, but calculation of coverage is simplified greatly compared with the prior rules.

If an owner has one or more revocable trust accounts that name more than five beneficiaries, then the maximum amount of coverage is the *greater of* $1.25 million *or* the total amount of all of the beneficiaries' interests in the trust(s), limited to $250,000 per beneficiary. *Interim* 12 C.F.R. § 330.10(e); 73 Fed. Reg. 56,711. For purposes of calculation of coverage, life estates are valued at $250,000. *Interim* 12 C.F.R. § 330.10(g); 73 Fed. Reg. 56,712.

Application of this rule is demonstrated in the examples below using the facts from the examples above with minor changes to account values and the number of beneficiaries.

More Than Five Beneficiaries with Equal Beneficial Interests. Assume Fred is the owner of the Trust, a formal revocable trust, with a total deposit amount of $1.4 million. The Trust names seven beneficiaries, each of whom is entitled to a one-seventh share ($200,000 each) upon Fred's death. The beneficiaries are Wilma; Pebbles; his neighbors Barney, Betty, and Bam-Bam; his boss, Mr. Slate; and the Bedrock Humane Society. FDIC coverage is determined by adding the aggregate interests of all the beneficiaries (totaling $1.4 million) and comparing that amount to $1.25 million. The available FDIC coverage for this Trust account is $1.4 million, the *greater of* $1.4 million and $1.25 million. Fred may like to know that the *maximum* amount of coverage for his Trust is $1.75 million. This upper limit is quickly figured by multiplying the maximum available coverage for each beneficiary by the number of beneficiaries ($250,000 x 7).[6]

More Than Five Beneficiaries with Unequal Beneficial Interests. Now assume Fred is the owner of the Trust, a formal revocable trust, with a total deposit amount of $1.5 million. The Trust names six beneficiaries: Wilma; Pebbles; his neighbors Barney, Betty, and Bam-Bam; and the Bedrock Humane Society. Upon Fred's death, Wilma will receive $1 million and the remaining five beneficiaries are entitled to $100,000 each.

Under the new rules, the available coverage for the Trust is the greater of $1.25 million or the aggregate amount of all of the beneficiaries' interests in the trust (limited to $250,000 per beneficiary). The aggregate interests of the five beneficiaries ($500,000) plus Wilma's interest (limited to $250,000) totals $750,000. The maximum coverage afforded the account is the *greater* of $1.25 million and $750,000. The deposits in the Trust are insured up to $1.25 million, leaving $250,000 uncovered.

Fred can (and should) remedy the gap in coverage by taking the uncovered $250,000 and opening up a revocable trust deposit account at another institution and then adjusting the disposition to Wilma in the Trust accordingly.

In this next example, the Trust has a total deposit amount of $1.5 million. The Trust names six beneficiaries, all of whom are to receive a percentage of the corpus upon the death of the owner. Wilma's interest of 40 percent is the largest share. Coverage is the greater of $1.25 million or the coverage based on each beneficiary's actual interest in the Trust, not to exceed $250,000 per beneficiary. Applying this rule, the maximum coverage on actual interests is $625,000 ($250,000 divided by 0.40 = $625,000). Because this is less than $1.25 million, the Trust is insured for up to $1.25 million, leaving $250,000 uninsured. If instead the largest beneficial interest were only 10 percent, then the maximum coverage afforded the Trust would jump to $2.5 million (the greater of $1.25 million and $250,000 divided by 0.10). Application of this rule can be found at www.fdic.gov/edie/fdic_info.html#11d.

Irrevocable Trust Accounts – 12 C.F.R. § 330.13

The FDIC did not promulgate new rules regarding calculation of coverage of irrevocable trust accounts. A separate set of rules governs coverage of trusts that are irrevocable from their inception. Generally, application of these rules results in less FDIC coverage for irrevocable trusts than revocable trusts.

As with revocable trusts, per-beneficiary coverage is available for irrevocable trust accounts regardless of the beneficiary's relationship with the owner. The main distinction in determining FDIC coverage for revocable and irrevocable trusts is that contingent interests in an irrevocable trust must be considered and identified. Per-beneficiary coverage is only available for noncontingent interests. All interests of contingent beneficiaries are added together and insured up to a maximum of $250,000. 12 C.F.R. § 330.13(a).

The easiest way to see how contingencies affect coverage of an irrevocable trust is through an example. Barney Rubble establishes the Rubble Irrevocable Trust and funds it with $600,000. Betty and Bam-Bam are equal beneficiaries upon the death of Barney. The trust contains a provision allowing the trustee to reallocate 100 percent of the trust funds to any beneficiary for medical needs. (Recall that this contingency is ignored if calculating FDIC coverage for a revocable trust.)

In calculating coverage, the contingency that the trustee may pay 100 percent of a beneficiary's medical bills must be considered. *Both* of the beneficiaries are subject to this contingency. To determine available coverage, the two contingent interests are added together and insured up to a maximum of $250,000. Betty's interest ($300,000) and Bam-Bam's interest ($300,000) are added together and insured up to a maximum of $250,000.[7]

Calculating deposit coverage for irrevocable trusts can be very complicated. The FDIC strongly suggests that because of "*the prevalence of contingencies in irrevocable trust agreements, the trustee of an irrevocable trust may wish to place no more than $250,000 of an irrevocable trust's funds at any insured bank.*" *Guide* at 64. Application of the rules for determining coverage for irrevocable trust accounts can be found at www.fdic.gov/edie/fdic_info.html#11d.

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This article is by no means comprehensive, but it should inspire practitioners to remind their clients to make certain that their trusts are covered.

Michelle Johansson
Cartwright and Associates
Portland, Oregon

Endnotes

1 This requirement can be found under *former* 12 C.F.R. § 330.10(f)(4). Although this provision does not appear in the interim rule, a recent conversation with an FDIC "trust expert" confirmed that the account title must continue to reflect that the funds are held pursuant to a formal revocable trust.

2 Though not required, the FDIC strongly recommends that owners of revocable trust deposit accounts include the names of the trust's beneficiaries in the bank's records.

3 The temporary increase in the insurance limit from $100,000 to $250,000 results in a proportional increase of the figures and examples provided in the interim rule published in the *Federal Register*.

4 Note that the death of a co-owner of a revocable trust account may result in a reduction of FDIC insurance coverage.

5 Under the old rules the coverage in the revocable trust category would have remained at $500,000 because there would have still been only two qualifying beneficiary pairs. Betty would not have passed the "relationship test," and her share would have been added into Fred's single ownership account.

6 This quick calculation to determine the *maximum* available coverage only applies to trusts when the beneficiaries have *equal* beneficial interests.

7 If the trust were revocable, under the interim rules the available coverage is $500,000—quite a large difference!

Questions, Comments or Suggestions About This Newsletter?

***Contact*:** Susan N. Gary
University of Oregon School of Law
Eugene, OR 97403-1221
Tel: (541) 346-3856
E-mail: *sgary@law.uoregon.edu*

Oregon State Bar

Oregon State Bar
Estate Planning and
Administration Section
PO Box 231935
Lake Oswego, OR 97281-1935

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