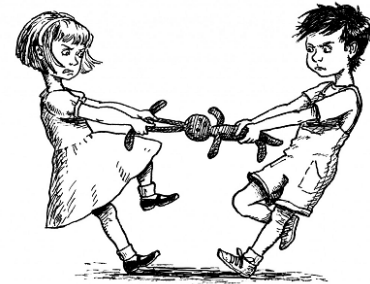


# The Kids Are Not Alright:

Exploring Dispute Avoidance and  
Resolution Techniques in  
Estate Planning



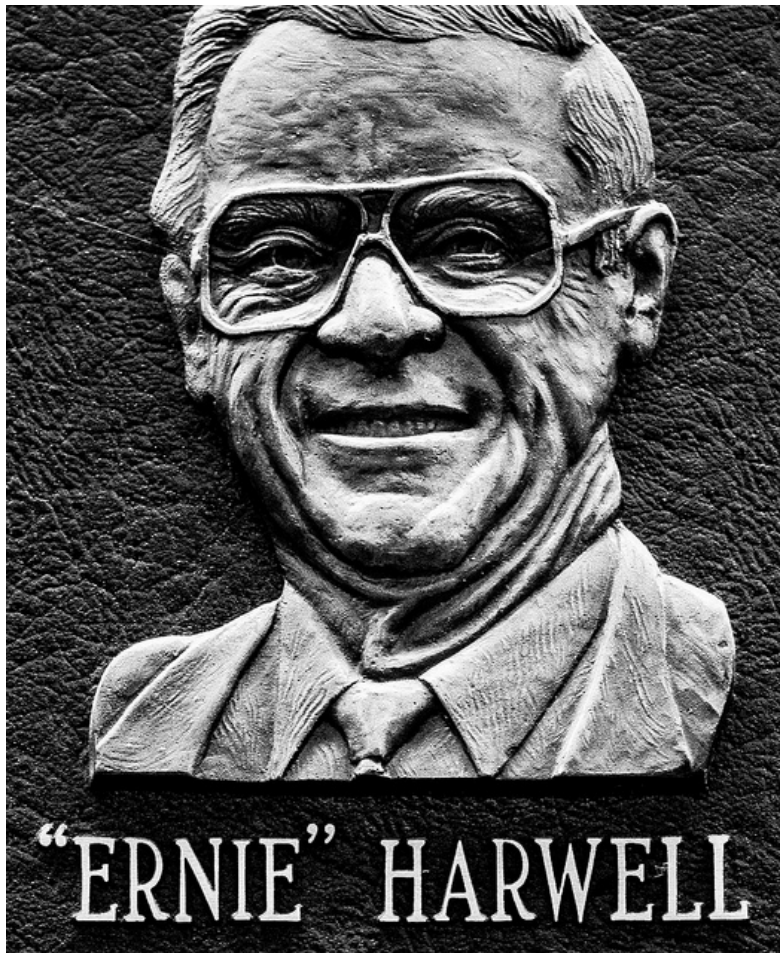
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Conejo Valley  
Estate Planning Council  
March 19, 2019  
Westlake Village Inn

## An Example of the Problem



- Married to Lulu for 70 years
- Ernie died in 2010
- Four kids publicly fighting with trustees and each other
  - 9 years; 7 separate cases; 8 attorneys, 2 judges
- Lulu died on March 1, 2019, penniless, with most of her children in debt

# The Consequences

- Waste of Resources
- Intent Thwarted
- Private Matters Made Public
- Destruction of Relationships
- Best Witnesses Gone
- Administration Delayed
- Justice is Slow and Not Guaranteed

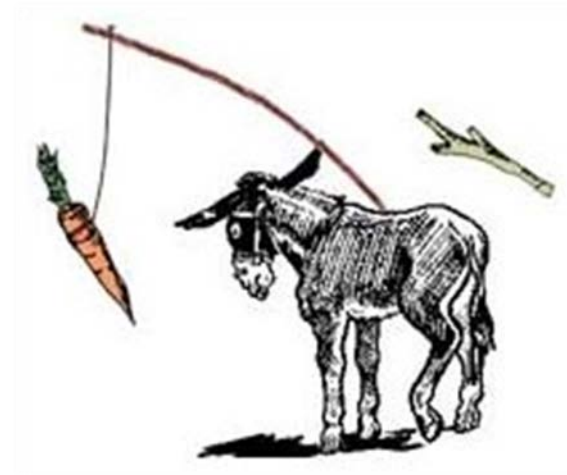
# Potential Tools

- Deterrence
  - By Punishment
  - By Reward
  - By Gathering Evidence
  - By Early Disclosure
- Dispute Control
  - Settlor Controlled Litigation
  - Alternative Dispute Resolution
  - By Collaboration
  - By Acquiescence



# Deterrence by Punishment and Reward

- Disinheriting Litigious Children/Beneficiaries
- Rewarding Cooperative Children/Beneficiaries



# No Contest Clause (*in terrorem* clause)

- What is it?
  - Essentially acts as a disinheritance device, i.e., if a beneficiary contests or seeks to impair or invalidate a trust or its provisions, the beneficiary will not take the gift or devise provided under the instrument.

*Donkin v. Donkin*, (2013) 58 Cal.4<sup>th</sup> 212

# Sample No Contest Clause

- If any beneficiary under this Trust Agreement (or any trust hereunder), singly or in conjunction with any other person or persons, shall (i) **directly contest, without probable cause, the validity of this Trust Agreement** (including any amendment hereto containing or amending this no contest clause) or of any other instrument, will, codicil, contract, agreement, trust, or beneficiary designation that a Grantor entered into during his or her lifetime and executed on or before the date of this Trust Agreement, or if later the date of any amendment to this Trust Agreement containing this no contest clause, and that relates to the disposition of such Grantor's assets upon his or her death (this Trust Agreement, any such trust amendments, and any other such documents collectively referred to as "Protected Documents"), or any provision of any Protected Documents, or seek to obtain an adjudication in any proceeding in court that any Protected Document is void, or seek to otherwise void, nullify or set aside any Protected Document or any provision of any Protected Document; (ii) **challenge in court any transfer of property on the grounds that it was not the Grantor's property at the time of the transfer**; (iii) **file a creditor's claim or prosecute an action based on it** respecting an alleged oral promise to make a gratuitous transfer, a lifetime gift or a pledge, or (iv) **file any other creditor's claim or prosecute an action based on it, without probable cause** (other than a written charitable pledge), then the right of such beneficiary to take any interest given to him or her by this Trust Agreement shall be determined as it would have been determined had such beneficiary predeceased the execution of this Trust Agreement without surviving descendants; provided, however, if the Surviving Grantor is the contestant, the Grantors' descendants shall not be barred by reason of the Surviving Grantor's actions. The Trustee is hereby authorized to defend, at the expense of the Trust, any contest or other attack of any nature on any Protected Document or any provision of any Protected Document.

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## Two Applicable Schemes

- Probate Code §§ 21300-21308 and 21320-21322 (the “old rule”)
  - Repealed in 2010
  - Still applies to instruments that became irrevocable prior to January 1, 2001
- Probate Code §§ 21310-21315 (the “new rule”)
  - Enacted in 2010
  - Retroactively applied to instruments that became irrevocable on or after January 1, 2001



# When the “Old Rule” Applies...

- What Constitutes a Contest
  - Direct or indirect contests
  - Must be specifically stated in instrument
  - Public policy limitations
  - Reasonable cause standard
- Features
  - Safe harbor petition
    - But see *Funsten v. Wells Fargo*
  - Probate Code § 3 Argument
  - Strictly construed to avoid forfeiture

# When the “New Rule” Applies...

- What Constitutes a Contest
  1. “Direct contest” brought without probable cause
  2. Challenge a transfer of property
  3. Filing of creditor’s claim
- Features
  - Probable cause as defense
  - Direct contest defined
  - Must be restated in Amendment
  - Common law still applies
  - Strict construction

# Is it a Contest?

- Beneficiary claims interest in property that testator gifted in trust instrument
- Beneficiaries claim that surviving spouse in AB Trust situation impermissibly diverted assets instead of funding subtrust
- Reformation petition to conform to extrinsic evidence of testator's intent
- Direct contest brought on multiple grounds, only some of which are supported by probable cause

# Conditional Gifts

- Precedent and Subsequent
- Cannot be Illegal
- Cannot be opposed to public policy
- Strictly construed
- Can be unfair



# Concerns with Conditions

- Will they be viewed as no contest clauses?
- Will they be enforceable?
  - Survival
  - Employment Requirements
  - “...so long as...”
- Will they adversely impact the administration of the estate?
- Are they too subjective to administer?
- Will they shift the power dynamic?
- Will they actually encourage litigation?

# Pre-Death Litigation: Mom and Dad on the Offensive



# Probate Code Section 17200

(a) Except as provided in Section 15800, a trustee or beneficiary of a trust may petition the court under this chapter concerning the internal affairs of the trust or to determine the existence of the trust.

(b) Proceedings concerning the internal affairs of a trust include, but are not limited to, proceedings for any of the following purposes:

(1) Determining questions of construction of a trust instrument.

(2) Determining the existence or nonexistence of any immunity, power, privilege, duty, or right.

(3) Determining the validity of a trust provision.

# Lifetime Estate Plan Protection Statutes

- Alaska Stat. Ann § 13.12.530, et seq. (establishment of will validity before death)
- Ark. Code Ann. § 28-40-202, et seq. (establishment of the validity of a will before death)
- Nev. Rev. Stat. Ann. § 30.040 (providing for an action for declaratory judgment for construction or validity of a will or trust)
- N.D. Cent. Code Ann. § 30.1-08.1-01, et seq. (permitting testator to obtain a declaratory judgment of validity)
- Ohio Rev. Code Ann. § 2107.081 (permitting testator to obtain a declaratory judgment of validity)

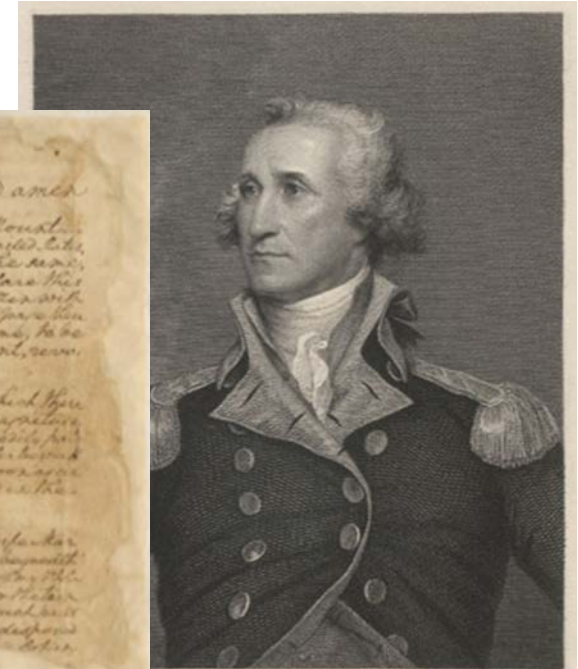


# Controlling Disputes Through Alternative Dispute Resolution

- Mediation – non-binding system in which dispute is brought before a neutral, who assists the parties in voluntarily reaching a compromise
- Arbitration – Parties submit abbreviated litigation structure to third-party, whose decision is binding
- Family Agreements
- Instrument Safe Guard Mechanisms
  - Trust Protector
  - Special Trustees
  - Tie Breaking Mechanisms

# Last Will and Testament of George Washington, 1799

- Any disputes that "unhappily" arose should be decided by three individuals, who would resolve the dispute "unfettered by Law, or legal constructions" and instead based on "their sense of the Testators [sic] intention."



and Mrs. the Bill South, Portret by Col. Trumbull belonging to Mr. Colgate.

GEORGE WASHINGTON.

*Geo Washington*

# Arbitration Benefits

- Time and Cost Savings
  - Abbreviated discovery and litigation procedures
  - Limited means of appeal
- Dispute and results remain private
- Control
  - Choice of Procedural Rules
  - Selection of Adjudicator
  - Adapt to Family Circumstances
- In multi-jurisdictional disputes, can reduce matters to one forum rather than multiple fora



# Key Questions

- Will there be enforcement issues?
- Does the arbitration clause impermissibly oust the jurisdiction of the court?
- Is the arbitration clause operable, effective and capable of being performed?
- Is the arbitration clause binding on all relevant parties, including those seeking to avoid arbitration?
- Does the arbitral procedure provide for representation of all potential parties?
- Is the subject matter arbitrable?

# Trust Arbitration Trends

- A rising national trend toward using arbitration to resolve internal trust disputes
  - Five States have laws favoring a settlor's power to mandate arbitration: AZ, FL, MO, NH & SD
  - In 2013, the Texas Supreme Court enforced an arbitration clause in a trust against the direct objections of a beneficiary of the trust in *Rachal v. Reitz*
  - ACTEC Created an Arbitration Task Force
- A rising international trend toward using arbitration to resolve internal trust disputes
  - International Chamber of Commerce Task Force on Trust and Arbitration
  - Statutory Arbitration Provisions in the Bahamas, Guernsey, Malta, Liechtenstein, Dubai, others
- Numerous Theories
  - Contract v. agreement
  - Third-party beneficiary
  - Equitable estoppel
- Various Mechanisms
  - Post-dispute arbitration agreement or mandatory pre-dispute arbitration clause

# Public Policy

- Effectuate Testator's Intent
- Avoid Dissipation of Assets
- Avoid Airing Family's "Dirty Laundry"
- Preserve Family Harmony

# Still Waiting on Supreme Court Guidance

- Code Civil Proc. § 1281
- McArthur v. McArthur
- Pinnacle Museum Tower Assn. v. Pinnacle Market Development (US), LLC
- “Expressly or implicitly” seeks benefits of instrument



# AAA Sample Arbitration Provision for Trust

- In order to save the cost of court proceedings and promote the prompt and final resolution of any dispute regarding the interpretation of my will (or my trust) or the administration of my estate or any trust under my will (or my trust), I direct that any such dispute shall be settled by arbitration administered by the American Arbitration Association® under its AAA Wills and Trusts Arbitration Rules and Mediation Procedures then in effect. Nevertheless, the following matters shall not be arbitrable: questions regarding my competency, attempts to remove a fiduciary, or questions concerning the amount of bond of a fiduciary. The arbitrator(s) shall be a practicing lawyer licensed to practice law in the state whose laws govern my will (or my trust) and whose practice has been devoted primarily to wills and trusts or at least 10 years. The arbitrator(s) shall apply the substantive law (and the law of remedies, if applicable) of the state whose laws govern my will (or my trust). The arbitrator's decision shall not be appealable to any court, but shall be final and binding on any and all persons who have or may have an interest in my estate or any trust under my will (or my trust), including unborn or incapacitated persons, such as minors or incompetents. Judgment on the arbitrator's award may be entered in any court having jurisdiction thereof.



# ICC Arbitration Clause for Trust Disputes

*“All disputes arising out of or in connection with this Trust [as defined in the trust instrument] shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators in accordance with the said Rules.*

*The settlor, the original trustee(s) and original [protector(s)][other original power holder(s)] hereby agree to the provisions of this arbitration clause, and each successor trustee and [protector][other power holder] by acting or agreeing to act under the Trust, also agree or shall be deemed to have agreed to the provisions of this arbitration clause.*

*Any beneficiary claiming or accepting any benefit, interest or right under the Trust, shall be bound by, and shall be deemed to have agreed to the provisions of this arbitration clause.”*

# ICC Arbitration Clause for Trust Disputes (continued)

- Confidentiality is of paramount importance in trust disputes.
- The ICC Arbitration Clause for Trust Disputes recognises this by including provisions on confidentiality within the clause itself:

*“Subject to the law governing the Trust and without prejudice to any other confidentiality obligation that may apply:*

- a) the arbitral proceedings, including the fact that they are taking place, have taken place or will take place, are private and confidential; and*
- b) any award or decision rendered by the arbitral tribunal or any settlement agreement between the parties shall be kept confidential and shall not be disclosed to any person, except to the extent that disclosure is required by law or pursuant to any rule, requirement or request of any regulatory or governmental authority or stock exchange, or is necessary or advisable in the administration of the Trust or for the implementation or enforcement of the award or decision.”*

# Deterrence By Evidence

- Medical Affidavits
- Letters Expressing Intent
- Videos
- Independent Review
- Third Party Witnesses and Experts
- Exclusion of Potential Influencers
- Establish patterns:
  - Consistent Lifetime Gifts
  - Commitments to Favored Charities

# Deterrence By Running the Statutes of Limitation

- Disclosures
- Lifetime transfers
  - Business Structures
  - Charitable Structures
  - Gifts
- Irrevocability
  - Third Party Fiduciaries

# Laches: *Drake v. Pinkham*, 217 Cal.App.4th 400 (2013)

- Probate Code § 15800: During the period a trust is revocable and the person holding the power to revoke is *competent*, the person holding the power to revoke, and not the beneficiary, has the rights afforded the beneficiaries, and the duties of the trustee are owed to the person holding the power to revoke
- Settlor's alleged incompetency takes the matter outside of § 15800
- Where a living settlor is alleged to be incompetent and the beneficiary is on notice of his/her claims, he/she must file or risk being barred from doing so under the doctrine of laches
  - Note: *Barefoot v. Jennings*, currently on appeal, could impact the child's standing under Probate Code Section 17200 to bring the contest

## Parting Suggestions...

- Ask sufficient questions at the intake stage to ensure that you are able to flag the issue of potentially litigious children
- Discuss all applicable deterrence and control options with your clients
- Highlight benefits, costs and risks
- Document your advice: A litigious child may also look for ways to attack you
- Check the current status of the law before implementation

# Thank You

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