the will & the way

Published by the Estate Planning & Fiduciary Law Section of the North Carolina Bar Association • Section Vol. 33, No. 1 • November 2013 • *www.ncbar.org*

The Chair's Comments

Jim Hardin

Thank you for the privilege and honor of serving as chair of our Estate Planning & Fiduciary Law Section this year. I thank my predecessor Sandy Clark of Raleigh for her invaluable guidance in the year just concluded. I also bid a fond farewell to Jane Weathers, our sections' staff liaison who served us with selfless dedication for decades and is now enjoying a well-deserved retirement. On behalf of the section I welcome her successor Jeremy Williams and look forward to working with him in the upcoming year.

Allow me to begin by celebrating the success of our section's Thirty-fourth Annual Estate Planning & Fiduciary Law Section Meeting held July 18-20, 2013 on Kiawah Island, South Carolina. The attendance this year was 299 counting both section members and sponsors and exhibitors, very near our record. The presence of 24 sponsors and 18 exhibitors, also near a record, is reflective of the desire of these vendors to have access to estate planning and probate practitioners. The section members and staff who worked so hard to make the Annual Meeting a success are too numerous to mention. As always, our meeting, one of the largest of such meetings across over 30 sections of the Bar Association, provides us an invaluable opportunity to receive cutting-edge CLE while at the same time renewing old acquaintances and making new ones not only with our fellow lawyers but with our sponsors and exhibitors. Many of you also manage to incorporate the meeting as part of a family vacation, a benefit you richly deserve if your organizational skills allow you to combine personal and professional renewal. Talk about work/life balance!

Some observers of our practice area have surmised that the significant increases in the applicable exemption amounts brought about by the American Taxpayer Relief Act ("ATRA") of January 1, 2013 have cast doubts on the future economic viability of estate planning and fiduciary law. Those doubters need look no further than the con-

Continued page 2

Constitutionality of Rule Against Perpetuities Repeal Revisited

Brown Brothers Harriman Trust Co., N.A. v. Benson – Constitutionality of Perpetual Trusts

By William R. Culp Jr. and Paula A. Kohut

In July of this year, there was considerable discussion at the North Carolina Bar Association's 34th Annual Estate Planning & Fiduciary Law Program about the current state of the rule against perpetuities as applied to trusts in North Carolina. Specifically, there was some discussion about the rule against perpetuities and **Brown Bros. Harriman Trust Co., N.A. v. Benson**, 688 S.E.2d 752 (N.C. Ct. App. 2010) (**Brown Bros.**). Several points were brought up that we felt

Continued page 3

Inside this Issue...

Don't Miss Your Section's Upcoming CLE! – See Page 15

the will & the way

Published by the Estate Planning & Fiduciary Law Section of the North Carolina Bar Association

Section Vol. 33, No. 1 • November 2013

Comments, *continued from page 1*

tinued popularity of our Annual Meeting to dispel such concerns. In addition to the Kiawah meeting, our section's members, over 1300 strong, also stay in active and productive dialogue on our section's ListManager, which is a further underpinning of our cohesiveness as estate planning, probate and trust lawyers. These are just a few of the examples suggesting that the best years of our section and our practice area are yet to come.

As always, the heart of our section's efforts lies in the work of our committees. At the Annual Meeting and in a recent email on our section's ListManager, my request for volunteers to serve on committees drew a robust response. Thanks to all of the new volunteers who are willing to set aside time from their practices to serve our members and the public. An overview of our committee chairs and committee activities is timely at the outset of this new year.

The AdHoc Committee chaired by Linda Johnson is already hard at work in making next summer's Thirty-Fifth Annual Meeting, on July 15-17, 2014 on Kiawah Island, another likely success. Those of you who have not booked your accommodations on Kiawah should do so right away as to be assured of a room or condominium. The Pro Bono Committee chaired by Jennifer Koenig continues to promote our section's talents to those individuals that would otherwise not be able to afford legal representation and provides valuable tools and material to the public.

Historically, our Legislative Committee has been one of our section's, and indeed the Bar Association's, most prolific. This year its chair, Rebecca Smitherman is working with her committee in studying proposals for new legislation. Rebecca and others in our section's leadership will be attending the Bar Association's Legislative Summit, planned for September 26-27 at the Bar Center in Cary.

Andrea Chomakos and Parrish Peddrick are the chairs of the CLE Committee and under their leadership the committee has already started to plan CLE programs over the next year including next year's Annual Meeting. The success of this committee is evident by the strong attendance at Seminars it implements each year.

The Estate Administration Manual Committee chaired by Heidi Royal continues to make revisions to the Administration Manual. The committee has worked diligently to keep this resource up to date and valuable for practitioners.

Mark Richardson is the new chair of the Newsletter Committee that provides the publication of The Will & the Way quarterly to our members. The Will & the Way continues to be another important tool whereby our section members interface during the year. Without exception the authors recruited by Mark and his committee strive for the highest level of legal scholarship in the articles they prepare, meeting or exceeding a standard we have come to expect with this valuable publication.

Our Ethics Committee chaired by Tanya Oesterreich considers legal issues related to the unauthorized practice of law and establishes policies governing ethical conduct in our area of the larger legal profession. The Membership Committee chaired by David Lewis promotes section membership and assures that our members receive back far more in value added than the modest section dues each pays. Amanda Creamer chairs the Technology Committee that strives to provide innovative ways to communicate and to improve our Section's website.

Our section's three Tax Forces provide valuable outreach to other centers of influence in our practice area. These Task Forces can use willing volunteers. This year our Task Force chairs are the following: Knox Proctor of the Joint Task Force with the North Carolina Bankers, Tim Jones of the Joint Task Force with the Clerks of Court and Tony Nicholson as the liaison with the Elder & Special Needs Law Section.

Thanks to all of you who have rendered valuable service in the past, as well as to so many of you who have expressed your willingness to serve as volunteers this year. You have all contributed to the fulfillment of our section's mission to better our area of the law both for ourselves as practitioners and for the public generally. I look forward to working with you!

~ Section Chair Jim Hardin
Charlotte, North Carolina

should be addressed, specifically, (1) whether the Supreme Court of North Carolina's dismissal of the **Brown Bros.** appeal was a decision on the merits, and (2) whether the question in **Brown Bros.** was ripe for decision, such that the court's decision was proper.

Procedural History | Effective Aug. 19, 2007, the North Carolina General Assembly passed the Act Defining Perpetuities and Suspension of Power of Alienation for Trusts, N.C.G.S. Section 41-23(h), repealing the Rule Against Perpetuities based on vesting with respect to trusts created or administered in North Carolina. After passage of the act, some practitioners were concerned that Article 1, Section 34 of the North Carolina Constitution, which states "[t]hat perpetuities and monopolies are contrary to genius of a free state and shall not be allowed," would act as a bar to the legislative repeal of the rule against perpetuities. However, that section only prohibits restraints on alienation, not trusts which allow for indefinite postponement of vesting. Brown Brothers Harriman Trust Co., N.A. (Brown Brothers Harriman) brought a declaratory judgment in connection with the administration of a dynasty trust. The North Carolina Court of Appeals affirmed the Business Court's grant of summary judgment in **Brown Bros.**, which found that (1) the Act Defining Perpetuities and Suspension of Power of Alienation for Trusts was constitutional, (2) the non-vested property interest to the beneficiaries of the dynasty trust in issue were valid, and (3) Brown Brothers Harriman could properly administer the Benson Trust as a perpetual or dynasty trust. The appellants petitioned the North Carolina Supreme Court for discretionary review and filed an appeal of right asserting that the case involved a substantial question arising under the North Carolina Constitution. The court dismissed the appeal and denied the petition in **Brown Bros. Harriman Trust Co., N.A. v. Benson**, 698 S.E.2d 391 (N.C. 2010).

Bosch Decision | A discussion on whether **Brown Bros.** firmly established the constitutionality of the rule against perpetuities repeal should start with **Commissioner v. Estate of Bosch**, 387 U.S. 456 (1997). In **Bosch**, the existence of a federal estate tax liability turned on the character of a property interest. The United States Supreme Court examined whether the Internal Revenue Service was conclusively bound by a rule of law established by a trial court in a prior proceeding in which the Internal Revenue Service was not a party. The court cited **Erie R. Co. v. Tompkins**, 304 U.S. 64 (1938), where it held that state law decided by the highest court in the state must be followed in a diversity case. The court in **Bosch** extended this rule to non-diversity cases, noting that a state's highest court is the best authority on the state's law.

In addition to the basic **Erie** rule establishing the supremacy of a state supreme court's interpretation of state law, the **Bosch** court noted a broader set of principles. William R. Culp and N. Lucille Siler stated the rules as follows:

(a) lower state court decisions should be attributed some weight but are not controlling, where the highest court of the state has not addressed the issue,

(b) "an intermediate appellate state court… is a datum for ascertaining state law which is not to be disregarded by a federal court *unless it is convinced by other persuasive data that the highest court of the state would decide otherwise,*" and

(c) that federal courts shall apply state law in accordance with the decisions of a state's highest court.

William R. Culp, Jr. and N. Lucille Siler, "U. S. Supreme Court Case Supports Constitutionality of Perpetuities Repeal," *The Will and the Way*, May, 2011 (citing **Bosch**, at 465 (emphasis in original)).

The Dismissal in Brown Bros. was a Final Decision on the Merits | As previously noted by William R. Culp, Jr. and N. Lucille Siler, the North Carolina Supreme Court's dismissal was a ruling on the merits by the highest court in North Carolina under the United States Supreme Court's principles in **R. J. Reynolds Tobacco Co. v Durham County, North Carolina**, 479 U.S. 130 (1986). In **Reynolds**, the United States Supreme Court only had jurisdiction to hear the appeal if the appeal of R.J. Reynolds lay from a final decision by the North Carolina Supreme Court on the merits. If the North Carolina Supreme Court's dismissal of the appeal constituted a determination that the state supreme court lacked jurisdiction over the appeal, as opposed to a decision on the merits, the United States Supreme Court had no jurisdiction to hear the appeal. **Reynolds**, at 138. The **Reynolds** appeal to the North Carolina Supreme Court, like the **Brown Bros.** appeal, was an appeal of right because of an asserted substantial constitutional issue.

The United States Supreme Court noted:

> It is one of those not infrequent cases in which decision of the merits of the case also determines jurisdiction. The petition was dismissed, not because the court was really without jurisdiction, for it could have taken it, but because the question was regarded as frivolous, which is a different thing from finding that the petition was not in character one which the court could consider.

Reynolds, at 139 (quoting **Matthews v. Huwe**, 269 U.S. 262, 265 (1925)).

In resolving the issue, the court annunciated a clear rule on this jurisdictional question: "***[S]o that practitioners may be certain of their ground… in the absence of positive assurance to the contrary from the North Carolina Supreme Court, we consider the court's dismissal of the Reynolds' appeal to be a decision on the merits.***" **Reynolds**, at 138 (emphasis added). The court noted that its treatment of "the North Carolina Supreme Court's summary dismissal as a decision on the merits accords [with the court's] view of its own summary dispositions." *Id.* at 139 n.7 (citing **Hicks v. Miranda**, 422 U.S. 332, 344 (1975)).

Continued page 4

Perpetuities, *continued from page 3*

The court in **Mandel v. Bradley**, 432 U.S. 173, 176 (1977), while noting that ascertaining the reach of summary decisions may present issues, stated the following:

> Summary affirmances and dismissals for want of a substantial federal question without doubt reject the specific challenges presented in the statement of jurisdiction and do leave undisturbed the judgment appealed from. They do prevent lower courts from coming to opposite conclusions on the precise issues presented and necessarily decided by those actions.

The court has also stated in **Washington v. Confederated Bands and Tribes of the Yakima Indian Nation**, 439 U.S. 463, 477 n.20 (1979), that a "summary dismissal of an appeal represents no more than a view that the judgment appealed from was correct as to those federal questions raised and necessary to the decision." Like a summary dismissal by the United States Supreme Court, the North Carolina Supreme Court's dismissal of the appeal of right in **Brown Bros.** was a decision on the merits which left the appellate court decision undisturbed.

The North Carolina Supreme Court decision in **State of North Carolina v. Fayetteville St. Christian School**, 261 S.E.2d 908 (N.C. 1980), provides an instructive example of a dismissal of an appeal of right asserting a substantial constitutional issue by the North Carolina Supreme Court. In the denial of the appeal the court provided "positive assurance" that the dismissal was not a decision on the merits consistent with the bright line rule in **Reynolds**. In **Fayetteville St. Christian**, the record and oral arguments revealed that the trial court's denial of the defendant's motion to dismiss and grant of a preliminary injunction constituted nonappealable interlocutory orders. The court dismissed the appeal, vacated the appellate court decision and remanded the case to the trial court. The court specifically noted that the constitutional arguments of the defendants (freedom of religion) required a fully developed factual record and that "[n]othing expressed herein should be construed as an expression of our own opinion on the constitutional issues attempted to be raised by defendants." *Id*. at 914.

An important takeaway from **Fayetteville St. Christian** is that when presented with a proposed substantial constitutional issue, the North Carolina Supreme Court knows how to dismiss an appeal of right while also providing positive assurance that the dismissal is not a decision on the merits. The **Brown Bros.** appeal of right was dismissed outright without any positive assurance that it was not a decision on the merits.

It is understandable why the **Brown Bros.** court did not find it necessary to do more than simply dismiss the appeal of right. The North Carolina Supreme Court held in **Yadkin Navigation Co. v. Benton**, 9 N.C (2 Hawks) 10, 13 (N.C. 1822) (involving the ability of stockholders to transfer shares and the opportunity for the public to invest in a corporation), that a "perpetuity" in the context of the passage of the North Carolina Constitution means "property locked up from the uses of the public, and which no person has power to alienate." Two years prior to **Yadkin**, the North Carolina Supreme Court similarly held in **Griffin v. Graham**, 8 N.C. (1 Hawks) 96, 130-32 (N.C. 1820), that an unconstitutional perpetuity only exists when property "is so settled that it cannot be undone or made void." Both of these cases were cited by the North Carolina Court of Appeals in **Brown Bros.**

Griffin involved a charitable trust established for the purposes of constructing and operating a school for indigent children. The decedent drafted the trust to continue forever, but he gave the trustees the power of alienation. The court in **Griffin** stated that "a perpetuity which the law would deem void must be an estate so settled for private uses that by the very terms of its creations there is no *potestas alienandi* in the owner." *Id*. at 132. Since the trustees in **Griffin** had the power to alienate the trust assets, there was not an unconstitutional perpetuity.

A repeal of the common law rule against perpetuities did not violate the North Carolina Constitution's prohibition against perpetuities because the common law rule against perpetuities deals with vesting and is only one method of restricting unreasonable restraints on alienation. N.C.G.S. Section 41-23(h) repealed the common law rule against perpetuities and the statute substituted another constitutionally permitted way to prevent unreasonable restraints on alienation.

Brown Bros. plainly rests on two previous North Carolina Supreme Court decisions, as discussed by the appellate court. Brown Bros., 688 S.E.2d at 755. As such, it is understandable why the Supreme Court of North Carolina did not provide positive assurances that its dismissal of **Brown Bros.** was not a decision on the merits.

The Issue in Brown Bros. was Ripe for Decision | Another question addressed during the discussion of the **Brown Bros.** decision at the 34th Annual Estate Planning & Fiduciary Law Program was whether the issue at hand was ripe for declaratory judgment. It was suggested that **Brown Bros.** may not have been ripe for a declaratory judgment action because the property in the trust at issue would have remained in trust for 90 years under N.C.G.S. Section 41-15(a)(2) if Section 41-23 was unconstitutional. Therefore, the issue of the constitutionality of the trust would not have been ripe for decision for another 90 years.

In **Brown Bros.**, the case was briefed, pled, and argued that Section 41-23 was unconstitutional as to the repeal of the common law rule against perpetuities but was constitutional as to the repeal of Section 41-15 as applied to trusts. The remainder beneficiaries argued that the assets of the trust would need to be distributed immediately as a result of the repeal of the 90 year wait and see period. In other words, it was argued that the trust was void because the common law rule against perpetuities should still be in place, and that Section 41-15(a)(2), providing for a ninety year rule, would not apply because it would have been repealed by Section 41-23. This created an important, current controversy. The trustee was entitled to seek declaratory judgment so as to settle this question arising out of the trust administration. Moreover, the record on appeal in **Brown Bros.** clearly established that the North Carolina Supreme Court considered the declaratory judgment to be "exceptional." Such a designation as "exceptional" allows a case to be heard in Business Court. By order of the Chief Justice of the Supreme Court of North Carolina, Chief Justice Sarah Parker, dated Aug. 28, 2008, the case was assigned to the Honorable Albert Diaz, Special Superior Court Judge for Complex Business Cases. **Brown Bros.**, 688 S.E.2d at 754; Rule 2.1, Gen. Rules of Practice, N.C. Superior and District Courts. •

William R. Culp Jr. is a member of Culp Elliott & Carpenter, P.L.L.C., Charlotte, N.C.

Paula A. Kohut is the sole member of Kohut, pllc, Wilmington, N.C.

Estate Planning in a Non-Recognition State Post-Windsor

By Paula A. Kohut

Since June 26, 2013, federal agencies have begun the implementation of the United States Supreme Court's decision striking down the prohibition against federal recognition of same-sex marriages under Section 3 of the Defense of Marriage Act (DOMA) as unconstitutional under the Due Process Clause of the Fifth Amendment. **Windsor v. U.S.**, 133 S. Ct. 2675; 2013 U.S. LEXIS 4921 (2013). Most federal agencies have announced that marriages will be recognized based upon the law of the state (or country) of celebration, not state of domicile. So, residence in a non-recognition state, including North Carolina, will not necessarily preclude federal recognition of the marriage. Most importantly for estate planners, the Internal Revenue Service issued Revenue Ruling 2013-17 which recognized all marriages valid under the laws of the state (or country) of celebration on Aug. 29, 2013.

Internal Revenue Service | On Aug. 29, 2013, the Internal Revenue Service issued Revenue Ruling 2013-17 which amplified and clarified Revenue Ruling 58-66, 1958-1 C.B. 60 (federal recognition of common law marriages is determined upon the laws of the state of celebration despite the refusal of some states to give full faith and credit to common-law marriages established in other states). Rev. Rul. 2013-17, 2013-18 I.R.B. (Sept. 16, 2013).

The holdings in the ruling will be applied prospectively as of Sept. 16, 2013. However, "affected taxpayers also may rely on this revenue ruling for the purpose of filing original returns, amended returns, adjusted returns, or claims for credit or refund for any overpayment of tax… provided the applicable limitations period for filing such claim under Section 6511 has not expired." *Id*.

Revenue Ruling 2013-17 provides that:

1. For federal tax purposes, the terms "spouse," "husband and wife," "husband," and "wife" include an individual married to a person of the same sex if the individuals are lawfully married under state law, and the term "marriage" includes a marriage between individuals of the same sex.

2. For federal tax purposes, the Service adopts a general rule recognizing a marriage of same-sex individuals that was validly entered into in a state whose laws authorize the marriage of two individuals of the same sex even if the married couple is domiciled in a state that does not recognize the validity of same-sex marriages.

3. For federal tax purposes, the terms "spouse," "husband and wife," "husband," and "wife" do not include individuals (whether of the opposite sex or the same sex) who have entered into a registered domestic partnership, civil union, or other similar formal relationship recognized under the state law but not denominated as a marriage under the laws of that state, and the term "marriage" does not include such formal relationships.

For 2013 and later years, same-sex spouses must file married filing separately or married filing jointly. For 2012 income tax returns filed before the effective date of the ruling – Sept. 16, 2013 – same-sex spouses were not required to, but could file as unmarried, joint or as married filing separately. For returns filed after Sept. 16, 2013, same-sex spouses must file jointly or married filing separately.

As in **Windsor** itself, the recognition of same-sex marriages by the Internal Revenue Service will include federal transfer taxes and returns for the same. With respect to same-sex spouses residing in North Carolina and filing amended returns, adjusted returns, or claims for credit or refund for any overpayment of transfer taxes pursuant to Rev. Rul. 2013-17, North Carolina's Same-Sex Marriage Bans and DR-13-1 will be ripe for challenge (as discussed below in connection with income tax). Since North Carolina has repealed its estate tax and gift tax, such conflict should not arise prospectively in the context of transfer taxes.

What Windsor Did Not Decide | The Windsor decision did not directly address (1) whether state prohibitions of same-sex marriages are valid under the federal Constitution or (2) the constitutional validity of Section 2 of DOMA which provides that no state shall be required to give effect to the validity of a same-sex marriage recognized under the laws of another state. 28 U.S.C.A. §1738C. The Fourteenth Amendment's Equal Protection and Substantive Due Process Clauses, U.S. Const. amend. XIV, § 1 ("Fourteenth Amendment's Equal Protection and Due Process Clauses"), may prove to be a basis for challenging non-recognition of marital status pursuant to North Carolina's statutory and constitutional bans of same-sex marriage, N.C.G.S. § 51-1.2 and Amendment One, N.C. Const., art. XIV, §6 ("North Carolina's Same-Sex Marriage Bans"). *See* **Windsor**, 133 S. Ct. at 2695.

North Carolina Income Tax | On Oct. 18, 2013, three days after the October 15th deadline for extended returns, the North Carolina Department issued Directive DR-13-1 ***http://www.dor.state.nc.us/practitioner/individual/directives/pd-13-1.pdf*** advising that North Carolina will not recognize the new definitions of marriage in Rev. Rul. 2013-17 and same-sex married persons cannot file North Carolina income tax returns using a married filing jointly or married filing separately status. Instead, married same-sex couples filing North Carolina returns are directed to prepare "pro forma" federal returns as if they were not married and to calculate and file their state income tax returns as if they were not married. Given the additional tax and compliance burdens placed upon same-sex married persons, it is likely that North Carolina's Same-Sex Marriage Bans and DR-13-1 will be challenged by affected taxpayers as violating their liberty interests under the Fourteenth Amendment's Equal Protection and Due Process Clauses. *See* **Windsor**, 133 S. Ct. at 2695 and **Fisher-Borne v. Smith**, 1:12-CV-589 (M.D.N.C. 2012) (discussed below).

Regardless of DR-13-1, the Military Spouses Residency Relief Act of 2009 prohibits North Carolina from taxing the income of the spouse of a servicemember if (a) the servicemember is present in North Carolina solely in compliance with military orders; (b) the spouse is in North Carolina solely to be with the servicemember; and (c) the spouse is domiciled in the same state as the servicemember. 50 U.S.C.A. § 571. The Military Spouses Residency Relief Act of 2009 also prevents states from imposing personal (not business) property tax upon spouses of servicemembers. 50 U.S.C.A. § 571(d). Given the federal recognition of same-sex marriages by both the Department of Treasury and the Department of Defense, North Carolina's Same-Sex Bans and DR-13-1 should not prevent tax relief for all military spouses.

Other Federal Benefits and Residency in a Non-Recognition State | The following is a non-exclusive list of department and agency announcements to date:

Office of Personnel Management

The United States Office of Personnel Management now extends employee benefits to legally married same-sex spouses of federal employees and annuitants, *regardless of the employee's or annuitant's state of residency*. Benefits Administration Letter Number 13-203, July 17, 2013. ***http://www.opm.gov/retirement-services/publications-forms/benefits-administration-letters/2013/13-203.pdf***. Federal employees and retirees living in North Carolina who have been legally married in another state are entitled to benefits. Although a special enrollment period ended on Aug. 26, 2013, some benefits may be available through late elections during the six months period ending Dec. 26, 2013. In any event, changes in employee elections can be made during the normal annual election period known as Open Season.

Department of Defense

The Department of Defense announced that it will consider the words "spouse" and "marriage" to include same-sex spouses and marriages and will extend benefits based upon the recognition of a marriage in the place of celebration. Memorandum, Secretary of Defense, Aug. 13, 2013. ***http://www.defense.gov/home/features/2013/docs/Extending-Benefits-to-Same-Sex-Spouses-of-Military-Members.pdf***. In recognition of the fact that some states still ban same-sex marriages, members of the armed services wishing to enter into a same-sex marriage may obtain nonchargeable marriage leave of up to 10 days if they are assigned to a duty station more than 100 miles from a U.S state (or the District of Columbia) that allows same-sex couples to get married. Memorandum, Under Secretary of Defense, Aug. 13, 2013. ***http://www.defense.gov/home/features/2013/docs/Further-Guidance-on-Extending-Benefits-to-Same-Sex-Spouses-of-Military-M.pdf***.

Social Security Administration

Social Security comprises three basic benefits: spousal benefits (lifetime), spousal survivorship benefits and the lump sum death benefit. The Social Security Administration has issued three recent POMS involving benefit claims for same-sex spouses after **Windsor**. GN 00210.001 – Windsor Same-sex Marriage Claims – Introduction; GN00210.005 Holding Claims, Appeals, and Post-Entitlement Actions Involving Same-Sex Marriages or Legal Same – Sex Relationships other than Marriage; and GN 00210.100 Same-Sex Marriage – Benefits for Aged Spouses ***https://secure.ssa.gov/apps10/poms.nsf/lnx/0200210000***. In general, the Social Security Administration will recognize same-sex marriages for same-sex spouses legally married and residing in a recognition state (GNB00210.100 provides examples of various fact patterns). Additionally, domestic partnership, civil unions and other legal relationships may entitle a person to benefits (as takers in the event of intestacy). With respect to same-sex spouses living in non-recognition states, the Social Security Administration is reviewing how to apply **Windsor** with the Department of Justice. Regardless of any uncertainty as to eligibility, all persons who may be entitled to benefits, including same-sex spouses residing in North Carolina, should promptly apply as benefits are awarded based upon date of application. An attorney is not needed to apply, but clients should be sure to file a Request for Reconsideration within 60 days of a denial. The National Senior Citizen Law Center has a PowerPoint and recording of its presentation titled– "The Demise of DOMA" which is located at: ***http://www.nsclc.org/index.php/webinar-the-demise-of-doma-what-does-it-mean-the-impact-on-social-security-medicare-and-medicaid-for-same-sex-couples/.***

Department of State

In connection with the issuance of visas for same-sex spouses, the Department of State will recognize same-sex marriages based upon the state of celebration. However, civil unions and domestic partnerships will not establish eligibility at this time. ***http://travel.state.gov/visa/frvi/frvi_6036.html.***

Department of Labor

On Sept. 18, 2013, the Department of Labor announced in Technical Release 2013-04 that the definitions of "spouse and "marriage" under ERISA and regulations thereunder "will be read to refer to individuals who are lawfully married to one another under state law, including individuals married to a person of the same-sex who were legally married in a state that recognizes such marriages, but who are domiciled in a state that does not recognize such marriages." ***http://www.dol.gov/ebsa/newsroom/tr13-04.html.***

On July 29, 2013, prior to Technical Release 2013-04, the United States District Court of the Eastern District of Pennsylvania held that an employer's ERISA Plan and Pre-Retirement Survivor Annuity benefits were payable to the employee-participant's surviving same-sex spouse and not the participant's designated beneficiaries (her parents). **Cozen O'Conner v. Tobits**, 2013 U.S Dist. LEXIS 105507 (E.D. Penn. 2013). Although the employer was based in Pennsylvania and the Plan contained a choice of law provision designating Pennsylvania (a non-recognition state), the court held that ERISA's requirement that a spouse is entitled to survivorship benefits in absence of a written waiver included same-sex spouses in accordance with **Windsor** and that ERISA pre-empted any state law in Pennsylvania to the contrary.

On Aug. 15, 2013, the Department of Labor issued its facts Sheet #28F providing that qualification for leave under the Family and

Medical Leave Act will be based upon the laws of the state where the employee resides. ***http://www.dol.gov/whd/regs/compliance/whdfs28f.htm.***

Representation of Same-Sex Couples in North Carolina | Despite **Windsor**, there are still unresolved conflicts among federal recognition of same-sex marriages, state laws recognizing same-sex marriages and the law of non-recognition states such as North Carolina. What is clear is that a practitioner representing same-sex married persons in North Carolina cannot ignore the clients' marital status simply because they reside in North Carolina.

The following is a non-exclusive list of issues to be considered:

Place of Marriage

For same-sex couples residing in North Carolina who are contemplating marriage, the ability to obtain a divorce as a non-resident will be an important consideration as long as North Carolina's Same-Sex Marriage Bans are in effect and in absence of a decision allowing divorce despite non-recognition of same-sex marriages. *See*, **Christiansen v. Christiansen**, 253 P.3d 153 (Wyo. 2011) where the Wyoming Supreme Court allowed a same-sex couple to obtain a divorce finding the recognition of a same-sex marriage for the purposes of dissolution did not violate the Wyoming's ban of same-sex marriage. Assuming the purpose for banning same-sex marriage is to limit such marriages, it seems counterintuitive that some same-sex married couples in non-recognition states find themselves without the ability to obtain a divorce. Some jurisdictions have only permitted annulments. **In re Surnamer**, 2012 Ariz. App. Unpub. LEXIS 852 (Ariz. Ct. App. 2012). However, an annulment may not provide the same certainty as a divorce decree and requires disavowing a marriage legally celebrated.

It has been suggested that a practitioner representing same-sex couples contemplating marriage may want to inquire whether her clients want to get married or really married. Same-sex couples are well advised to celebrate their marriages in a state which allows divorce for non-residents if the marriage was celebrated in such jurisdiction and the spouses cannot divorce in their state of residence. The National Center for Lesbian Rights has an attorney's guide on this issue. ***http://www.nclrights.org/site/DocServer/Divorce_in_DOMA_states_Attorney_Guide.pdf?docID=9761.***

Federal Employees and U.S. Service Members

Given the adoption of a state of celebration rule for recognition of marital status for employee and retiree benefits, federal employees and U.S. Service Members who are in same-sex marriages but residing in North Carolina will have access to employee and retiree benefits. From an estate planning standpoint, assuring proper beneficiary designation and elections will be part of both the estate planning and estate administration process. Additionally, servicemembers and all spouses of servicemembers (both opposite sex and same-sex) will be entitled to the consumer and other protections afforded under the Servicemembers Civil Relief Act. 50 U.S.C. 501, et. seq. Finally, the Military Spouses Residency Relief Act of 2009 should preempt North Carolina's Same-Sex Marriage Bans and DR -13-1 and prohibit the imposition of income tax and personal property tax upon nonresident same-sex spouses of servicemembers.

Social Security Benefits

Despite the fact that the Social Security Administration has put all claims of same-sex spouses residing in non-recognition states on hold, clients should nonetheless file claims for spousal, survivor and death benefits to preserve their claims. The Social Security Administration encourages all such persons to apply. ***http://ssa-custhelp.ssa.gov/app/answers/detail/a_id/2503/kw/same-sex.***

Marital Liabilities in a Non-Recognition State

In North Carolina, liability for medical debts (and presumably other necessaries) cannot be disavowed during marriage (and may apply while separated). *See*, **North Carolina Baptists Hospitals v. Harris**, 319 NC 347, 354 SE 2d 471 (1987). In 2009, the North Carolina Court of Appeals held a wife in an opposite sex marriage who came into the marriage with assets and a good credit rating liable for her husband's unpaid medical debts incurred during the marriage despite the husband's Chapter 7 bankruptcy discharge of the debts and the fact that the husband brought few assets to the marriage. **Moses H. Cone Mem. Hosp. Operating Corp. v. Hawley**, 195 N.C. App. 455 (2009). Though North Carolina's Same Sex Marriage Bans presumably exempt same-sex married couples residing in North Carolina from such liabilities, same-sex couples contemplating marriage will want to consider potential future liability for implied marital liabilities should they move to a recognition state or North Carolina's Same-Sex Marriage Bans are found unconstitutional.

Property Agreements

Windsor did not rule that North Carolina's Same-Sex Marriage Bans are unconstitutional as the constitutionality of state marriage bans was not before the Court. Therefore, unlike prenuptial agreements, prospective same-sex couples should be wary of using agreements which recite a prurient or meretricious relationship as part of the consideration. Presumably, Amendment One does not affect the recognition of "agreements regarding the finances and property of an unmarried but cohabitating couple, whether express or implied, are enforceable as long as sexual services or promises thereof do not provide the consideration for such agreements." **Rhue v. Rhue**, 189 N.C. App. 299 (2009), quoting, **Suggs v. Norris**, 88 N.C. App. 539, 542-43, 364 S.E.2d 159, 162 (1988).

Challenges to State Marriage Bans

Since **Windsor**, lawsuits have been filed (or amended) in a number of federal courts challenging state bans of same-sex marriages, including the following:

Fisher-Borne v. Smith, Civ. 1:12-CV-589 (M.D.N.C. 2012). Originally filed as a challenge to the North Carolina Supreme Court's ban of second parent adoptions in **Jarrell v. Boseman**, 364 N.C. 537 (2010), the complaint was amended after **Windsor** to challenge North Carolina's Same-Sex Marriage Bans.

Obergefell v. Kaisch, 2013 U. S. Dist. LEXIS 102077 (S.D. Ohio 2013). Plaintiffs, James Obergefell and John Arthur, were residents of Cincinnati, lived together in a committed relationship for over

Continued page 8

Post-Windsor, *continued from page 7*

twenty years and were married in Maryland after the Windsor decision. John Arthur was dying of ALS and both travelled by a medical jet to be married in Maryland. Plaintiffs were granted a temporary restraining order prohibiting the local Ohio Registrar from accepting for recording a death certificate for John Arthur which does not record his status as "married" and/or does not record James Obergefell as Mr. Arthur's surviving spouse at the time of his death (which was imminent). **Obergefell**, at 21.

Stewart v. Heineman, Case No. DO2Cl30003157 (Lancaster County District Court, Penn.) Plaintiff, a same-sex spouse residing in Pennsylvania, a non-recognition state, is seeking recovery for loss of consortium.

In addition to assisting same-sex married persons in North Carolina with rights and benefits under federal law, practitioners should consider whether protective claims and challenges for spouses should be considered and asserted under state law. In such cases, it is a best practice to contact advocacy groups and practitioners experienced in such claims and challenges. •

Paula A. Kohut is the sole member of Kohut, pllc, Wilmington, N.C.

A Road Map for the New North Carolina Limited Liability Company Act

By Warren P. Kean

On Jan. 1, 2014, Chapter 57C of the North Carolina General Statutes (the "Old NC LLC Act") will be repealed and a new Chapter 57D will take its place (the "New NC LLC Act"). N.C. Sess. L. 2013-157 (enacting Senate Bill 439). This article provides an abstract of the fundamental principles that underpin the revised act and sets out guideposts to assist the reader's understanding of the act's design.

Transition Rules | While the New NC LLC Act replaces old Chapter 57C, care was taken to conform as much of the new act to the old act as possible. In addition, G.S. § 57D-11-03 provides certain transition rules designed to minimize the impact to existing limited liability companies caused by the repeal of the Old NC LLC Act. Particularly helpful is G.S. § 57D-11-03(e), which provides that references to the Old NC LLC Act made in articles of organization and operating agreements in effect before Jan. 1, 2014 generally are deemed to be made to their counterparts in the New N.C. LLC Act.

The Central Traffic Circle | The core of the New N.C. LLC Act insofar as the rules governing the ownership interests in a North Carolina limited liability company (referred to in G.S. § 57D-1-03(16) as an "LLC") is found in the following three sets of provisions: (1) G.S. § 57D-10-01, (2) Part 3 of Article 2 (G.S. §§ 57D-2-30 through 57D-2-32), and (3) G.S. § 57D-1-03(23). All analyses, in particular judicial analyses, under the New N.C. LLC Act with respect to the relative rights and obligations of the owners (and, to a lesser extent, non-owner managers or other company officials) of LLCs are expected to begin and, for most LLCs with comprehensive, well-written operating agreements, end with those provisions.

1. *The Operating Agreement Controls.* G.S. § 57D-10-01 makes it clear that the statute intends for an LLC's operating agreement to control the rights and duties of the LLC's owners and any other parties to the agreement. All judicial decisions involving disputes between the owners of an LLC are expected to begin with the following stated purpose of, and policy underlying, the New N.C. LLC Act:

> The purpose of this Chapter is to provide a flexible framework under which one or more persons may organize and manage one or more businesses as they determine to be appropriate with minimum prescribed formalities or constraints. It is the policy of this Chapter to give the maximum effect to the principle of freedom of contract and the enforceability of operating agreements.

The above statement of policy was added to the Old NC LLC Act in 2009 and is derived from Section 18-1101(b) of the Delaware Limited Liability Company Act. It serves as the premise for Delaware judicial decisions involving disputes between members of Delaware limited liability companies and was included in the North Carolina act for that purpose.

To apply G.S. § 57D-10-01 requires an understanding of the terms and concepts referenced therein, in particular: the definitions of "business" and "operating agreement" and what are the "minimum prescribed formalities or constraints" under the New NC LLC Act.

"Business" has essentially the same meaning that it has had since 1999 under the Old NC LLC Act. See N.C. Sess. L. 1999-189 that amended this definition. This definition makes it clear that an LLC may be utilized for any legal "purpose or activity, whether or not conducted or undertaken for profit." G.S. § 57D-1-03(3). For that reason the provisions concerning low profit limited liability companies (so-called "L3Cs") that were added to the Old NC LLC Act in 2011 were deleted as unnecessary.

2. *The Parameters of the Operating Agreement.* The definition of "operating agreement" in G.S. § 57D-1-03(23) is perhaps the most important and nuanced of the defined terms in the New NC LLC Act. The definition establishes the following principles:

> (a) The operating agreement need not contain the words "operating agreement" in its title or otherwise be referenced as such in the agreement. Instead, an operating agreement is any agreement that concerns the LLC to which each member or other

"interest owner" (as defined in G.S. § 57D-1-03(15)) of the LLC is a party "as an interest owner" and not in some other capacity (such as the sole member and manager of the LLC signing a lease on behalf of the LLC).

(b) The operating agreement, including any portion of the operating agreement, may be in any form: written, oral, or implied. This is a change from the Old NC LLC Act that required a "written operating agreement" to modify or eliminate many of the Old NC LLC Act's default rules. All requirements that any part of the operating agreement be in writing have been eliminated under the New NC LLC Act. As under the Old NC LLC Act, G.S. § 57D-1-03(23) makes it clear that the parties may agree on the form that an operating agreement and its amendments must take to be enforceable, such as only in a document signed by all (or other prescribed number) of the LLC's members.

(c) All LLCs will have an operating agreement because G.S. § 57D-1-03(23) provides that the articles of organization are deemed to be part of the operating agreement. Accordingly, as between the owners of an LLC, any conflict between the articles of organization and the operating agreement is to be resolved by the general rules of contract construction. Third parties, however, are entitled to rely on the public record of the Secretary of State (i.e., the LLC's articles of organization and annual reports). G.S. § 57D-2-30(d).

(d) When an LLC has only one economic interest owner, any document or record that economic interest owner intends to serve as the operating agreement will be the operating agreement.

3. *The Limitations of Freedom of Contract*. The guardrails contained in Part 3 of Article 2 of Chapter 57D provide the third leg of the foundation of the New NC LLC Act. Unlike the Old NC LLC Act that stated in each default rule that it applied only to the extent the operating agreement did not provide otherwise, G.S. § 57D-2-30 states that, as between the owners (and any non-owner managers or other company officials of an LLC), all of the provisions of the New NC LLC Act may be "supplemented, varied, disclaimed, or nullified" by the operating agreement except provisions that –

(a) deny members access to certain information (such as a copy of the LLC's operating agreement, the LLC's income tax returns or financial statements, the names and addresses of the interest owners, information from which a member's capital interest may be derived, and "any information from which the status of the business and the financial condition of the LLC may be ascertained"), but under no circumstances is the LLC to be compelled to disclose or make available "trade secrets or other confidential information of a nature that its disclosure would adversely affect the LLC" that can not be adequately safeguarded by other reasonable means (G.S. 57D-3-04(f)); or

(b) eliminate the right of a member to bring a derivative action or a demand for judicial dissolution unless an alternative remedy or means is provided to resolve disputes that would otherwise be the subject of such proceedings.

The other exceptions under G.S. § 57D-2-30(b) to the deference to be given to operating agreements include (i) the administrative provisions of the act (such as the process to be followed to form an LLC), (ii) the provisions relating to government officials (such as the Secretary of State and the Attorney General), and (iii) the rights of third parties (those who are not parties to the operating agreement), including the rights that creditors and other third parties may have with respect to wrongful distributions (those made when the LLC is insolvent or to the extent they cause the LLC to become insolvent).

In addition to the above-described mandatory provisions of the New N.C. LLC Act, G.S. § 57D-2-30(e) refers to contract law and agency law, as liberalized by other provisions of the act (e.g., G.S. § 57D-2-32(a), authorizing the assessment of penalties for the breach of the operating agreement), to police the parties' freedom to order their affairs as they may agree in the operating agreement. Specifically mentioned in that respect is the implied contractual covenant of good faith and fair dealing that has been the subject of many court cases in Delaware and other jurisdictions and the requirement that the terms of the operating agreement not be unconscionable at the time they are made.

Tour of the Side Streets | To navigate the provisions discussed above and the remainder of the New N.C. LLC Act, one must apply the following nomenclature found in G.S. § 57D-1-03, most of which is new:

1. *"LLC," "foreign LLC," and "limited liability company."* The New N.C. LLC Act refers to a domestic (N.C.) limited liability company as an "LLC," a foreign limited liability company as a "foreign LLC," and either an LLC or foreign LLC as a "limited liability company."

2. *"Interest owner," "member," "economic interest owner," and "ownership interest."* The default provisions of the Old N.C. LLC Act (as those of other limited liability company and partnership statutes) provided that members could freely transfer their economic rights but not their governance, information and other non-economic rights. The recipients of such economic-only rights are generally referred to as "assignees" in those statutes. The New N.C. LLC Act more directly provides for these different types of ownership interests. An owner who has only an economic interest (defined as an interest owner's rights in the "capital, income, losses, credits, and other economic rights and interests of the LLC") is referred to as an "economic interest owner" and may acquire that status either by acquiring only an "economic interest" from the LLC or by acquiring such an interest from another interest owner in a secondary transfer.

A "member" is defined as an owner who has been "admitted" as a member of the LLC and, therefore, has the non-economic rights of a member as provided in the LLC's operating agreement or, to the extent not otherwise modified or eliminated by the operating agreement, under the New N.C. LLC Act.

An "interest owner" is defined as either an economic interest owner or a member, and the entire interest of an interest owner is now referred to as an "ownership interest" instead of as a "membership interest" (the term used under the Old N.C. LLC Act).

As under the Old N.C. LLC Act, (i) persons other than interest owners may be parties to the operating agreement, (ii) members need not own economic interests (so-called noneconomic members), and (iii) persons may become members upon the occurrence of speci-

Continued page 10

fied events provided in the operating agreement (so-called "springing members"). G.S. §§ 57D-2-31, 57D-2-30, and 57D-3-01(c).

3. *"Capital interest," "contribution amount," and "distributions."* Terms related to an interest owner's economic interest include the "capital interest" and "contribution amount" of the interest owner and the "distributions" made in respect of that interest. "Capital interest" is defined as the interest owner's share of the owners' equity of the LLC, which is to be based on the LLC's consistently applied method of accounting. A member generally is entitled to information from which the member's capital interest may be derived under G.S. § 57D-3-04(a)(4)(i), and a member or economic interest owner is not entitled to withdraw any portion of the interest owner's capital interest except as provided in the LLC's operating agreement or as the members may otherwise agree. G.S. § 57D-5-05.

The "contribution amount" attributable to an "ownership interest" is not only the net value of the property or services contributed in respect of that ownership interest but also includes the net value of property and services that the interest owner is obligated to contribute in the future in respect of the ownership interest with adjustments being made if such promises are not fulfilled. G.S. §§ 57D-1-03(6) and 57D-4-01. Transfers, or obligations to transfer, property or to perform services to the LLC in exchange for cash or other consideration that are not made in respect of an "economic interest" and, therefore, are not included as part of the interest owner's contribution amount. The definition is important because in the absence of the operating agreement providing otherwise, the interest owners' economic interests (i.e., their shares of distributions) are to be based on the "contribution amounts" of their ownership interests. G.S. § 57D-4-03.

"Distributions" are defined as the payments made in respect of an ownership interest. Because "distributions" may need to be repaid under G.S. §§ 57D-4-05, 57D-4-06, and 57D-6-12 if they are made when the LLC is insolvent or to the extent they cause the LLC to become insolvent, payments by the LLC that otherwise constitute "distributions" under the act are not to be treated as such for purposes of the wrongful distribution rules if they are made as "compensation for services" or "in the ordinary course of business under a bona fide retirement plan or other benefits program." G.S. § 57D-1-03(9).

4. *"Managers" and "company officials."* The New N.C. LLC Act no longer requires an LLC's articles of organization to state whether the LLC is "member managed" or "manager managed," but as under the Old N.C. LLC Act, unless the operating agreement provides otherwise, the LLC will be managed by "managers," and each member by virtue of being a member will be a "manager" of the LLC. G.S. §§ 57D-2-30(a) and 57D-3-20. Because of the intended flexibility afforded LLCs and their owners, the New N.C. LLC Act makes it clear that an operating agreement may provide that the LLC is to be managed by persons other than "managers;" for example, by a board of directors and officers. G.S. §§ 57D-2-30(a) and 57D-3-20(d). For that reason, the New N.C. LLC Act refers to those persons who manage an LLC – be they "managers" or officials exercising their authority under some other title – as "company officials." G.S. § 57D-1-03(5).

5. *"Approve."* Members, organizers, and company officials are deemed to act by "approval" and may "approve" of a decision or other action to be taken by vote at a meeting or by "any other expression of assent to the action to be taken." G.S. § 57D-1-03(1). If the operating agreement does not provide otherwise, approval is to be made in the manner that members approve amendments to the operating agreement (i.e., under the default rule of G.S. § 57D-3-03(1), by unanimous consent, which under the default rules of G.S. § 57D-1-03(23) may be expressed in writing, orally, or by implication through conduct).

6. *"Transfer."* The last important term of art in the New NC LLC Act is "transfer." This term is defined broadly under G.S. § 57D-1-03(34) to include the transfer of legal, equitable, or beneficial ownership of an ownership interest or other property by any means. This term is important because a transfer of an ownership interest without the admission of the transferee as a "member" (or the assignee otherwise being a member) causes the ownership interest that is "transferred" to become an "economic interest." G.S. §§ 57D-5-02, 57D-3-01, and 57D-3-02. The definition provides the following examples of transfers of ownership interests: (i) gifts of ownership interests made during the interest owner's life or upon or after his or her death, (ii) the appointment of a personal representative of a deceased interest owner or a guardian for an interest owner who is judicially declared to be incompetent, (iii) the appointment of a bankruptcy trustee for the interest owner, and (iv) transfers made to a spouse or former spouse in connection with a divorce or under any other circumstances. G.S. §§ 57D-1-03(34).

Rules of the Road | Construction and other rules of general application are found in G.S. § 57D-10-02. To avoid placing qualifiers such as "reasonable" throughout the New N.C. LLC Act, G.S. § 57D-10-02(e)(1) provides that the provisions of the New N.C. LLC Act "are to be applied in a manner that is reasonable under the circumstances." G.S. § 57D-10-02(a), in coordination with G.S. §§ 57D-2-30(a) and (e), provides that unless the New N.C. LLC Act states otherwise (including as may be provided in the LLC's operating agreement) contract, agency, and other common law rules as well as rules of equity apply in governing the rights and obligations of interest owners and other parties to the operating agreement and company officials. Exceptions to the application of common law include the New N.C. LLC Act not being required to be strictly construed to the extent it conflicts with common law (G.S. § 57D-10-02(b)) and the right of the interest owners to provide for penalties for breach of the operating agreement (G.S. § 57D-2-32(a)).

Conclusion | The foregoing is not, nor is it intended to be, an exhaustive or comprehensive discussion of the New N.C. LLC Act. It is intended only as roadside assistance to give direction on how a practitioner may move more confidentially and safely through the New N.C. LLC Act.

Warren P. Kean is a member of K&L Gates LLP, Charlotte, N.C.

Summary of Proposed Overhaul of the N.C. LLC Act

1. Affirmation of Contractual Underpinnings of the North Carolina Limited Liability Company Act. The public policy underlying the North Carolina Limited Liability Company Act (the "Act") is stated in G.S. § 57C-10-03(e): "[I]t is the policy of [the Act] to give maximum effect to the principle of freedom of contract and to the enforceability of operating agreements." The revisions to the Act are proposed to more clearly, concisely, and effectively achieve and implement that stated public policy objective.

(a) No writing requirement. The revised Act would eliminate all requirements that any part of a North Carolina limited liability company's operating agreement be in writing. The revisions, however, do not go as far as the Delaware Limited Liability Company Act, which makes the "statute of frauds" inapplicable to Delaware limited liability company agreements. Under the revised Act, the operating agreement may be established in the same ways as any contract; i.e., by written, oral, or implied assent among the parties to the contract. As under the current Act, however, the parties may require that all of the components of the operating agreement be in a signed, written document or in any other prescribed form.

(b) Supplemental Nature of the Act. In furtherance of the foregoing, the revised Act would establish that its provisions concerning the internal affairs of North Carolina limited liability companies are intended to apply only if, and to the extent, other provision is not made in the operating agreement. Accordingly, parties are free to modify, waive, and nullify the rules of the Act that would otherwise govern their respective rights and duties. The limited extent to which that freedom of contract is restricted is set forth in Part 3 of Article 2 of the revised Act.

(c) Objective of the Revised Act. The objective of the proposed revisions is to provide certainty and a more detailed framework and structure to allow members of a North Carolina limited liability company to be confident that their management and ownership arrangements will be accommodated by and enforced under the Act. This flexibility is partially achieved through the introduction of certain new defined terms: (a) those relating to the management of the limited liability company: "company officials," (which may but need not be "managers"); (b) those relating to the two different types of owners of limited liability companies: "economic interest owners" (referred to under the current Act as "assignees") and "members," and in reference to either economic interest owners or members or both, "interest owners," and the interest held by either being referred to as an "ownership interest" instead of a "membership interest"; and (c) those relating to the economic interest of an owner: "contribution amount," "capital interest," and "economic interest."

(d) Clarification of Matters that May be Agreed Upon by the Members. In addition to the members being able to require the operating agreement to be in writing or other prescribed form, the revised Act would make it clear that the members' freedom of contract extends to decisions concerning the following matters:

(i) Management Duties. The duties of those responsible for the management of the company, including the scope or elimination of fiduciary and other duties, except nonwaivable contractual duties, including the implied contractual covenant of good faith and fair dealing and the requirement that the terms of the contract not be unconscionable at the time they are made;

(ii) Exculpation and Indemnification. The liabilities and other consequences to those managing the company for any breach or failure in the performance of their duties;

(iii) Penalties. The imposition of penalties and other remedies for breach of the operating agreement or the occurrence of proscribed events;

(iv) ADR. The right of the parties to select the manner in which they are to resolve their disputes, including having such dispute resolution procedures supplant the right to bring derivative actions or actions to cause the company to be judicially dissolved; and

(v) Information Rights. The right to establish certain rules and procedures concerning access that owners may have to certain information, while specifying the type of information that can not be denied members who comply with prescribed rules and procedures.

2. Foreign Limited Liability Companies.

The revised Act would harmonize, where appropriate, the rules under the LLC Act with their counterparts under the BCA. One such set of rules where this would be accomplished are those relative to foreign limited liability companies.

3. Clarifying, Modernizing, and Coordinating Provisions of the Act. The remaining revisions are more in the nature of clarifying (i.e., removing ambiguities), simplifying, and modernizing the Act and coordinating its provisions to accommodate the new concepts and features described above. These revisions include those described in the following non-exhaustive list:

(i) coordinating the terms relating to bankruptcy with the current United States Bankruptcy Code;

(ii) clarifying that the flexibility of the Act accommodates entities and arrangements such as low profit limited liability companies without the need to adopt separate sets of provisions such as those found in G.S. § 57C-2-03;

Continued page 12

(iii) providing that organizers may act by majority consent;

(iv) removing the requirement that the articles of organization state whether the LLC is "member-managed" or "manager-managed";

(v) clarifying that an LLC need not have any managers, instead management may be vested in persons having different titles and different powers and duties as may be provided in the operating agreement;

(vi) allowing managers to delegate responsibilities to other persons without the approval by the members unless the operating agreement provides otherwise;

(vii) providing that the term of a limited liability company is presumed to be perpetual unless other provision is made in the operating agreement (instead of in the articles of organization);

(viii) adopting rules of construction to eliminate repetition of phrases and qualifiers to make the Act easier to read and more user friendly;

(ix) clarifying and modernizing the default rules relating to capital contributions and excuses from performances and basing distributions on the proportional contributions (of services as well as capital) of the owners (including promises to make contributions in the future);

(x) conforming the default rules and procedures relative to derivative actions with those in the BCA;

(xi) the elimination of redundant and otherwise superfluous provisions, including (A) G.S. § 57C-10-03(b) and (c) (concerning the law of estoppel and agency when § 57C-10-05 broadly provides that rules of equity and law supplement those under the Act) and (B) § 57C-2-02(l)-(16) (illustrating the type of powers a limited liability company may exercise when the breath of the statement in that section that there are no limitations or restrictions to such power other than not engaging in illegal activities makes doing so unnecessary); and

(xii) consistent with the recent holding of the North Carolina Business Court in **Blythe v. Bell**, 2012 NCBC 60 (2012), the proposed bill would make it clear that unless the operating agreement provides otherwise, a member may freely transfer to another member all of his or her rights (governance and other non-economic rights as well as economic rights) in respect of the member's ownership interest.

In addition to the foregoing, the proposed bill would revise G.S. § 57C-3-02(b)(3) and 57C-5-05 to state that, unless the operating agreement provides otherwise, a member will cease to be a member upon the assignment of the member's entire economic interest in the company, regardless of whether the assignee is a member at the time the assignment is made. In the **Blythe v. Bell** decision, the North Carolina Business Court held that under the current Act an assignor of a membership interest retains the non-economic rights of that interest until the assignee is admitted as a member.

4. Other Changes of Note.
(a) Override of UCC §§ 9-406 and 9-408. Because the application of UCC §§ 9 406 and 9 408, as currently in effect, may allow a member to encumber his or her economic interest in breach of the operating agreement [which may result in the foreclosure of that interest under circumstances that may result in adverse tax consequences to the other members, the transfer of ownership of the economic interest to a corporation or other ineligible shareholder of an S corporation, for those LLCs that elect to be taxed as S corporations, or a technical termination under I.R.C. § 708(b)(1)(B)], the revised Act adopts the approach taken in states such as Delaware and Virginia (among other states, including those states that have recently restated their LLC Acts: Texas, Mississippi, and New Hampshire) to not have UCC §§ 9-406 and 9 408 apply to LLC ownership interests.

(b) Certificate of Existence. An example of the type of clean up undertaken by the revised LLC Act concerns the certificates of existence issued by the Secretary of State. While the current LLC Act provides that one may conclusively rely on a certificate of existence as to the existence of an LLC, one does so at his or her peril. This is because, as contrasted from a corporation under the BCA, the filing of articles of dissolution is not the event that causes an LLC to dissolve. Thus, the Secretary of State is not in a position to certify as to whether the LLC has dissolved. All she can do is certify as to the status of the LLC's filings made in her office, which certification will be conclusive evidence as to the accuracy of its contents.

(c) Deletion of Low Profit Limited Liability Company (L3C) Provisions. As under current law, the flexibility of the restated Limited Liability Company Act accommodates the organization of limited liability companies that qualify for "program related investments" under I.R.C. § 4944(c) by private foundations without the need for any additional or special provisions under Chapter 57D.

5. Concepts the Drafting Committee Elected to Not Recommend.
(a) Series or Cell Limited Liability Companies. The drafting committee carefully reviewed and considered the merits of adopting an elaborate set of provisions that have been adopted in 10 other states, allowing limited liability companies to create internally segmented liability "cells" or "series." Under those provisions, not only

are the members of the limited liability company shielded from personal liability for the debts and obligations of the limited liability company itself, but separately identified groups of assets of the company may be shielded from liabilities attributable to other groups of the company's assets. No uniform set of provisions have been adopted by the states allowing for "series" or "cell" limited liability companies. The drafting committee concluded that the confusion and potential abuse associated with such entities, together with the public policy of North Carolina against excessive fragmentation of an incorporated enterprise, outweigh the potential benefits that may be derived from Chapter 57D adopting a set of provisions to allow for such structures. *See* Allen Sparkman, "Series LLCs in Interstate Commerce," *Business Law Today* (American Bar Association Section of Business Law February 2013), citing **Pacific Employers Ins. Co. v. Industrial Accident Commission**, 306 U.S. 493, 501 (1939) in support for the conclusion: "a court in a non-series state could, without running afoul of the Full Faith and Credit Clause, refuse to uphold the internal liability shields of a series LLC on the ground that the forum state's legislature, by not enacting series legislation, had expressed a public policy that internal liability shields with a single entity should not be recognized." The drafting committee will continue to monitor developments in this area.

(b) Contractual Appraisal Rights. The drafting committee reviewed the contractual appraisal rights provisions of the Delaware Limited Liability Company Act and concluded that the flexibility of Chapter 57D accommodates the inclusion of such rights in an LLC's operating agreement without the need for any additional or special provisions under Chapter 57D.

(c) Statute of Frauds. Chapter 22 of the North Carolina General Statutes does not require agreements that cannot be performed within one year to be in writing, which was the subject of the Delaware Chancery Court decision in **Olson v. Halvorsen**, C.A. No. 1884-VCL (De. Ch. Ct. 2008). Thus, the drafting committee determined that a counterpart to Section 18-101(7), excluding operating agreements from the application of the "statute of frauds," was not necessary or appropriate. Other than to expressly acknowledge the intention of the General Assembly to promote the freedom of the parties to an operating agreement to arrange their business affairs (including their respective rights and duties) as they may agree and the other rules of construction and statements of public policy in G.S. 57D-10-01 (including sanctioning the assessment of penalties under LLC's operating agreement, G.S. 57D-2-32(a)), the Act does not provide additional or special rules for resolving situations in which overlapping or conflicting laws may apply. Instead, such situations are to be resolved under the rules applicable to statutory construction and conflict of laws.

See Senate Bill 439: Amend & Restate N.C. Limited Liability Co. Act,next page.

SENATE BILL 439: Amend & Restate NC Limited Liability Co. Act

2013-2014 General Assembly

Committee:	House Judiciary Subcommittee C	**Date:**	June 13, 2013
Introduced by:	Sens. Clodfelter, Barringer, Brunstetter	**Prepared by:**	Bill Patterson Committee Counsel
Analysis of:	Fourth Edition		

SUMMARY: The PCS to Senate Bill 439 rewrites the North Carolina Limited Liability Company Act.

CURRENT LAW: The North Carolina Limited Liability Company Act, codified as Chapter 57C of the General Statutes, governs the creation, operation, and dissolution of limited liability companies.

BILL ANALYSIS: Section 1 of the bill repeals Chapter 57C in its entirety, and Section 2 reenacts the Limited Liability Company Act as Chapter 57D, with revisions including:

- Operating agreements would not have to be in writing; they could be established in the same ways as any contract: written, oral, or implied assent among the parties to the contract.
- Rights and duties of parties as set forth in the Act could be freely modified, waived, or nullified by agreement.
- Unwritten provisions in the operating agreement would not be permitted to vary or nullify any inconsistent or contrary written provision in the operating agreement to the detriment of non-parties to the operating agreement to the extent that they reasonably relied upon the written provision. In the event of a conflict between the operating agreement and any document of an LLC filed by the Secretary of State, the operating agreement would prevail as to parties to the operating agreement and company officials, and the document filed by the Secretary of State would prevail as to persons who are neither parties to the operating agreement nor company officials to the extent of their reasonable reliance upon the filed document.
- The priority among multiple charging orders would be determined by the date of service of the charging order upon the LLC, except that a charging order in favor of a judgment creditor would relate back to the date of service upon the LLC of garnishment process previously issued in favor of that judgment creditor.
- Newly defined terms are added to provide a more detailed framework for carrying out the ownership and management of LLCs.
- Provisions relating to low-profit LLCs are deleted as unnecessary.
- Provisions are added to clarify matters that may be agreed upon by members, including:
    - Management duties
    - Exculpation and indemnification
    - Penalties
    - Alternative dispute resolution
    - Information access rights
- Provisions governing foreign LLCs would be harmonized with their counterparts under the Business Corporations Act.
- Various provisions of the Act would be clarified and coordinated with relevant State and federal law.

Sections 3 through 30 make various conforming changes to other statutory provisions.

Sections 31 and 32 exempt ownership interests in LLCs from UCC Article 9 provisions that might result in encumbrances to a member's economic interest in breach of the operating agreement, which could adversely affect the interest of the other members.

EFFECTIVE DATE: This act becomes effective January 1, 2014, except as otherwise provided in new Chapter 57D, Article 11 (Transition Provisions).

BACKGROUND: As introduced, Senate Bill 439 was the product of four years of work by the LLC Act Revisions Task Force of the North Carolina Bar Association's Business Law Section. The Senate committee substitute modified the original bill by:

- adding new subsections (c) and (d) to G.S. 57D-2-30, "Scope, function, and limitations of operating agreements," to address potential conflicts between inconsistent terms in unwritten versus written portions of an operating agreement and between inconsistent terms in an operating agreement versus a document of the LLC filed with the Secretary of State
- revising subsection (c) of G.S. 57D-5-03, "Rights of judgment creditor," to add provisions governing the priority of multiple charging orders served upon an LLC relating to the same member's economic interest

Realizing the Promise of Advance Directives:

A New Option for North Carolinians

"Life is pleasant. Death is peaceful. It's the transition that's troublesome." – Isaac Azimov

By John C. Moskop and Beth M. Gianopulos

Introduction | Patients nearing the end of life, and the representatives of patients who lack decision-making capacity, often face difficult decisions about whether to pursue life prolongation or relief of symptoms and quality of life as primary goals of treatment. More than 30 years ago, the North Carolina General Assembly enacted our state's first advance directives statute, the Right to a Natural Death Act, to help patients communicate their end-of-life treatment preferences.

Since that time, the Natural Death Act has been revised multiple times, and in 1991, state legislation recognized a second type of advance directive, the Health Care Power of Attorney. The current statutes include a set of model advance directive forms, but, these forms are still complicated and hard for the average layperson to understand. Even experienced attorneys struggle to explain the statutory model forms.

A Piedmont Triad Initiative | Advance care planning facilitators have long complained that the statutory model forms were too long and complicated, the literacy level of the forms was simply too high for many people, and some of the form options were very confusing. In the face of general dissatisfaction with the model forms, a group convened in early 2012 to explore options for improving advance care planning and advance directives in the Triad region. The group included representatives from Wake Forest Baptist Health, Novant Health, High Point Regional Health, Cone Health, and Hospice and Palliative CareCenter of Winston-Salem. Participants came from multiple disciplines, including physicians, hospital legal counsel, private elder law and estate planning attorneys, patient representatives, chaplains, and bioethicists.

After reviewing existing advance directive forms, the group chose to draft a new form for regional use. The new form was tested at several Triad medical centers and was strongly preferred by patients and facilitators to the statutory model forms used previously. The new form is now in use at three of the Triad's largest hospitals: Wake Forest Baptist Medical Center, Novant Health Forsyth Medical Center, and High Point Regional Hospital.

The New Advance Directive Form | The Triad working group had five major goals for its new advance directive form:

1. The form should be understandable by the vast majority of those who undertake this planning.

2. The form should be relatively brief and easy to complete.

3. The form should include all of the essential elements of the two main types of advance directives: living wills and health care powers of attorney.

4. The form should meet North Carolina statutory requirements for advance directives and thus provide the statutory protections for health care providers who honor advance directives.

5. The form should promote discussion of future treatment wishes, especially between the principal and the person he or she appoints as health care agent.

With these goals in mind, the Triad group crafted a new advance directive form with these major features:

1. Since most people who complete the planning process prepare both a living will and a health care power of attorney, the new form combines these two directives in a single document. This makes the document easier to complete and avoids the need for separate signatures and notarization. The document also clearly allows the principal to complete only one of the two directives, if he or she so prefers, by marking through the undesired directive. The advance directives statutes explicitly state that these two directives may be combined in a single document.

2. The language of the new form is simplified for easier understanding. Here are two examples of parallel passages:

Statutory model forms	New advance directive form
"I DO want to receive BOTH artificial hydration AND artificial nutrition (for example, through tubes) . . ."	"I DO want to receive tube feeding . . ."
"I, ______________, being of sound mind, hereby appoint the following person(s) to serve as my health care agent(s) to act for me and in my name (in any way I could act in person) to make health care decisions for me as authorized in this document."	"My name is ____________. My birth date is ___________. The person I choose as my health care agent is . . ."

3. The form is shortened to five pages, from the 10-pages of the statutory model forms. There are two pages of instructions that describe the purpose of the document and define key terms like "health

care agent" and "life-prolonging measures," one page for the health care power of attorney, one page for the living will, and the execution page for the signatures of the principal and the two witnesses and the notarization information.

Meeting Statutory Requirements | The Triad working group recognized that a major function of the North Carolina advance directives statutes is to encourage health care professionals to honor patients' directives by providing immunity from liability for professionals who do so. The working group drafted the new advance directive form with the clear intention to meet statutory requirements and thereby receive the statutory protections. The statutory requirements for living wills and for health care powers of attorney in North Carolina are described in the North Carolina Right to Natural Death Act (N.C.G.S. § 90-320 through 90-322) and the North Carolina Health Care Power of Attorney statute (N.C.G.S. § 32A-15 through 32A-27). Although statutory model forms exist, use of the model forms is optional. N.C.G.S. § 90-321(i); N.C.G.S. § 32A-24(d). Alternative forms also provide the statutory protections for health care professionals who honor them, as long as they meet certain statutory requirements. For instance, the statutes require that both living wills and health care powers of attorney be notarized and signed by two witnesses who meet specific requirements. N.C.G.S. § 90.321(c)(4).

Encouraging the Conversation | Although advance directives are clearly an important part of the advance care planning process, the members of the Triad initiative believe that these written plans are not the most important step in that process. It is neither feasible nor desirable to attempt to capture most people's considered and nuanced preferences regarding goals of care and treatment options near the end of life in a lengthy written document. Such a document would be both difficult for most people to prepare and difficult for physicians to understand and implement. The most important steps in the planning process are to choose a health care agent who is willing and able to carry out one's preferences and to engage in an extended conversation about treatment preferences in different circumstances.

The Triad initiative sought, therefore, to emphasize the importance of careful choice of one's health care agent and of thoughtful discussion about one's preferences with that agent. To guide people in these key steps in the planning process, the group developed an informal document for those who prepare health care powers of attorney to present to their chosen health care agents. That document includes a description of the role of the health care agent, including a list of the kinds of health care decisions agents are authorized to make. It also includes the following statement: "I am relying on you to make health care choices on my behalf if I am no longer able to do so. I ask that you make treatment choices for me based on my goals and desires about what kind of care I should receive. It is very important, therefore, that we take time to discuss my desires, goals, and hopes for medical treatment so that you will know what kind of care I want." At the bottom of the document is a space for the signature of the health care agent, immediately following the statement "I accept appointment as your health care agent." The Triad group believes that this document will encourage principals to engage in conversation with their health care agents and will encourage health care agents to take this responsibility seriously.

The Bottom Line | We believe that use of the new advance directive form described above will enable many more North Carolinians to complete the process of advance care planning and to realize its substantial benefits. Therefore, we recommend use of this form for anyone assisting in this planning process, including estate law and elder law attorneys and health system advance care planning facilitators. For a copy of the new form, please go to the website www.ncadvancecareplanning.com and look under "Documents for Download" at the top of the webpage. •

John C. Moskop, Ph.D. is the Wallace and Mona Wu Chair in Biomedical Ethics and Professor of Internal Medicine at the Wake Forest School of Medicine, and ***Beth M. Gianopulos*** is legal counsel at Wake Forest Baptist Medical Center.

Respect for Testator's Intent When Probating Out-of-State Wills

By Janice L. Davies

Until recently, a testator's intent was summarily ignored when a self-proving affidavit was not substantially in the form provided in N.C.G.S. § 31-11.6(a) unless, for instance, the subscribing witnesses to the will signed an affidavit for probate of the will. Compounding the result here was the requirement in N.C.G.S. § 31-46 that a will is only valid in North Carolina if it meets the requirements of the applicable provisions of law in effect in North Carolina at the time of its execution or at the time of the death of the testator. Therefore, the strict terms or the strict application of this substantial compliance provision for the self-proving affidavit in combination with the strict terms of § 31-46 had the effect of what may be described as a minor omission in the self-proving affidavit to rise to the level of a fatal flaw under North Carolina law.

For an example under former law, Testator executes a valid will under Florida law with his Florida counsel. Testator, who is one of many who visits our great state each year, moves to North Carolina and makes it his domicile or domiciliary state. Before Testator is able to have his will reviewed by North Carolina counsel, he suffers a significant medical event. His general durable power of attorney, health care proxy, and living will executed with his Florida counsel are helpful in managing his affairs before his death. When you review his will with the executor named in his will after Testator's death, you find that the self-proving affidavit omits the reference to the Testator being eighteen years of age or older when he executed his will.

Do not apply any deductive reasoning here, such as producing a copy of Testator's birth certificate to prove he was definitely over eighteen when he executed the will, because that production is, in my experience, not sufficient to meet the substantial compliance standard as it is applied for a self-proved, attested will to be valid in North Carolina. You are still hopeful that the witnesses may be located to sign the affidavit for probate of the will, but you are likely dreading the call to the Florida counsel who drafted the will to explain that North Carolina is one of approximately thirty-three states that requires substantial compliance with the self-proving affidavit form. It is also one of only four states and the District of Columbia that has a rigid validly of will or choice of law provision. And, the combination of the rigid choice of law provision and the substantial compliance provision for the self-proving affidavit may cause the will to be invalid to dispose of property, real and personal, or unable to be probated under North Carolina law without, for instance, locating the subscribing witnesses to sign an affidavit. In summary, the lack of the words "over eighteen" in a self-proving affidavit may rise to the level of a fatal flaw in the will in North Carolina.

Senate Bill 279 was signed by the Governor on June 12, 2013. In Sections 1.(f), (g) and (h) of Session Law 2013-91, N.C.G.S. §§ 31-11.6 (How attested wills may be made self-proved), 31-46 (Validity of will; which laws govern), and 28A-2A-17 (Certified copy of will of nonresident recorded), are updated to give North Carolina residents the same advantages available to a vast majority of other states' residents who die with out-of-state wills. The changes in § 31-11.6(a) provide, in pertinent part, that "[a]ny will may be simultaneously executed, attested, and made self-proved, by acknowledgment thereof by the testator and affidavits of the witnesses, each made before an officer authorized to administer oaths under the laws of the state where execution occurs and evidenced by the officers certificate, under official seal, in the following form or in a similar form showing the same intent…." By striking the word "substantially," it now says "in the following form," but the phrase "or in a similar form showing the same intent" is added to create flexibility. Flexibility, for example, in that if the self-proving affidavit omits the language stating a testator was over eighteen when he executed his will, you should now feel free to use your deductive reasoning and produce a birth certificate for the testator to show that the self-proving affidavit is in a similar form showing the same intent because the testator was over age eighteen when he executed his will.

You may still be concerned that the language in N.C.G.S. § 31-11.6(a), "in the following form, or in a similar form showing the same intent," may differ in its application from county to county in North Carolina. To further clarify the law governing how an attested will may be self-proved, subsection (d) was added to § 31-11.6, and it provides that "[a]ny will executed in another state and shown by the propounder to have been made self-proved under the laws of that state shall be considered as self-proved." This provision is similar to Fla. Stat. § 732.503(2). In an informal survey of a few estate and fiduciary law attorneys routinely practicing in Florida, they shared that they do not have issues with probating out-of-state wills before the Florida probate judges. One of them stated that, at most, he may simply add a few sentences to his standard application to open probate so that the probate judge is aware that the out-of-state will has a self-proving affidavit in conformity with the relevant state's law and provides a copy of the self-proving affidavit statute for that state. In essence, the court takes judicial notice that the self-proving affidavit is in conformity with the state where the will was executed. In North Carolina, it is the Clerk of Superior Court, our ex officio judge of probate, who would review the self-proving affidavit statute for the state where the will was executed. For your ease in presenting an out-of state will to the Clerk for probate in North Carolina, on the next page, you'll find a chart with the citation for the self-proving statutes for all states and the District of Columbia along with a notation if the self-proving affidavit is in such statutes.

During the process of updating and clarifying the laws related to out-of-state wills, it came to the legislative committee's attention that military wills were not being probated in some counties of North Carolina despite the existence of federal law, being 10 U.S.C. § 1044d. Subsection (a) of § 1044d provides "[a] military testamentary instrument (1) is exempt from any requirement of form, formality, or recording before probate that is provided for testamentary instruments under the laws of a State; and (2) has the same legal effect as a testamentary instrument prepared and executed in accordance with the laws of the State in which it is presented for probate." Subsections

(b) and (c) of § 1044d describe the requisite content and execution necessary for an instrument to be a military testamentary instrument. Subsection (d) of § 1044d states the requirements for a military testamentary instrument to be self-proved. With the intention of bolstering the local application of § 1044d in North Carolina for our soldiers, subsection (e) was added to N.C.G.S. § 31-11.6, which states "[a] military testamentary instrument executed in accordance with the provisions of 10 U.S.C. § 1044d(d) or any successor or replacement statute shall be considered as self-proved." Therefore, it is now crystal clear that if the military testamentary instrument is self-proved in accordance with §1044d(d) of the United States Code, it is self-proved for purposes of probate in North Carolina.

In N.C.G.S. § 31-46, Validity of will; which law governs, the provisions are expanded to allow for the so called out-of-state will to be valid under North Carolina law. As noted above, the will is valid if it meets the requirements of the applicable provisions of law in effect in North Carolina either at the time of its execution or at the time of the death of the testator. As expanded, the will is also valid "if (i) its execution complies with the law of the place where it is executed at the time of execution; (ii) its execution complies with the law of the place where the testator is domiciled at the time of execution or at the time of death; or (iii) it is a military testamentary instrument executed in accordance with the provisions of 10 U.S.C. § 1044d or any successor or replacement statute."

As another example of a self-proving affidavit that may have formerly failed for purposes of probate in North Carolina, Testatrix executes a valid will under New Jersey law with her New Jersey counsel. Testatrix dies domiciled in North Carolina. Testatrix never contacts North Carolina counsel for her will to be reviewed for North Carolina law. When you review the will for probate in North Carolina, you find that the will was notarized by the New Jersey counsel, the notarization by whom does not require a notary seal under the laws of New Jersey. In the past, your remedy was to find the witnesses so the subscribing witnesses to the will may sign an affidavit for probate of the will. That remedy is still available to you. However, you now have other remedies as well. You may present the self-proving statute for the State of New Jersey and the notary rules related to no seal is necessary when notarized by New Jersey counsel along with the application for probate in North Carolina. Alternatively, New Jersey counsel may be willing to sign an affidavit stating that the will is validly executed in New Jersey as of the time of execution.

To complete the updates for out-of-state wills, N.C.G.S. § 28A-2A-17, Certified copy of will of nonresident recorded, was revised. As revised, subsection (a) of § 28A-2A-17 provides that "[s]ubject to the provisions of subsection (b), of this section, if the will of a citizen or subject of another state or country is probated in accordance with the laws of that jurisdiction and a duly certified copy of the will and the probate proceedings are produced before a clerk of superior court of any county wherein the testator had property, the copy of the will shall be probated as if it were the original." Subsection (b) of § 28A-2A-17 states that "[f]or a copy of a will probated under the provisions of subsection (a) of this section to be valid to pass title to or otherwise dispose of real estate in this State, the execution of said will according to the laws of this State *either at the time of its execution or at the time of the death of the testator, or as otherwise recognized as valid under the provisions of 31-46,* must appear affirmatively, to the satisfaction of the clerk of superior court of the

State	Statute	Affidavit in Statute
Alabama	Ala. Code. §§ 43-8-132 and 133	Yes
Alaska	AS § 13.12.504	Yes
Arizona	A.R.S. § 14-2504	Yes
Arkansas	A.C.A. § 28-25-106	No
California	Cal. Prob. Code § 8220	No
Colorado	CRSA § 13.12.504	Yes
Connecticut	CGSA § 45a-285	No
Delaware	12 Del. C § 1305	Yes
D.C.	No Statute	No
Florida	FS § 732.503	Yes
Georgia	Ga. Code § 53-4-24	Yes
Hawaii	HRS § 560:2-504	Yes
Idaho	I.C. § 15-2-504	Yes
Illinois	755 ILCS § 5/7-2	No
Indiana	IC § 29-1-5-3.1	No, but criteria given
Iowa	I.C.A. § 633.279	Yes
Kansas	KSA § 59-606	Yes
Kentucky	KRS § 394.225	Yes
Louisiana	LSA-R.S. § 2885	No
Maine	M.R.S.A. § 2-504	Yes
Maryland	No Statute	No
Massachusetts	M.G.L.A. 190B § 2-504	Yes
Michigan	MCLA § 700.2504	Yes
Minnesota	Minn. Stat. § 524.2-504	Yes
Mississippi	Miss. Code § 91-7-9	No
Missouri	V.A.M.S. § 474.337	Yes
Montana	MCA § 72-2-524	Yes
Nebraska	Neb. Rev. St. § 30-2329	Yes
Nevada	N.R.S. § 133.050	Yes
New Hampshire	N.H. Rev. Stat. § 551:2-a	Yes
New Jersey	N.J.S.A. 3B:3-4	Yes
New Mexico	N.M.S.A. § 45-2-504	Yes
New York	NY CLS EPTL § 3-5.1	No
North Carolina	N.C. Gen Stat. § 31-11.6	Yes
North Dakota	NDCC § 30.1-08-04	Yes
Ohio	No Statute	No
Oklahoma	84 Okl. St. Ann. § 55	Yes
Oregon	No Statute	No
Pennsylvania	20 PA. C.S.A. § 3132.1	Yes
Rhode Island	R.I. Gen. Laws § 33-7-10	No
South Carolina	S.C. Code § 62-2-503	Yes
South Dakota	SDCL § 29A-2-504	Yes
Tennessee	T.C.A. § 32-1-104	No
Texas	Tex. Prob. Code § 59	Yes
Utah	Utah Code § 75-2-504	Yes
Vermont	14 V.S.A. § 109	No
Virginia	Pending 2012 Legislation (2012 Virginia Laws Ch. 614 (S.B. 115)); Formerly, VA Code Ann. § 64.1-7.1	Yes
Washington	RCWA 11.12.020	No
West Virginia	No Statute	No
Wisconsin	Wis. Stat. § 853.04	Yes
Wyoming	Wyo. Stat. 2-6-114	Yes

Out-of-State, *continued from page 19*

county in which such will is offered for probate, from the testimony of a witness or witnesses to such will, or from findings of fact or recitals in the order of probate, or otherwise in such certified copy of the will and probate proceedings." (*emphasis added*)

Another example may be best to describe how this change may allow for the testator's intent to be followed, not simply ignored for a minor omission in the self-proving affidavit. Testator died a resident of Florida and his self-proved, attested will was probated and his domiciliary estate administered in Florida. Almost ten years after the close of the domiciliary estate in Florida, Florida counsel determines that the ancillary administration was not completed in the North Carolina county in which Testator owned real property at the time of his death. A certified copy of the will and probate proceeding is obtained from the Florida counsel to file with the Clerk of Superior Court. Upon filing, you are informed that the self-proving affidavit in the Florida will omits the reference to Testator being of sound mind when he executed his will so it will be necessary to locate the witnesses to the will in order to have this will transfer the property to the beneficiaries under the will. Under the former North Carolina law, you are on the telephone with the Florida counsel trying to make her understand that North Carolina law will not respect the Florida self-proving affidavit because it is missing the words 'sound mind.' With the recent changes in North Carolina law, it should be quite obvious to the Clerk that the execution of the Florida will complies with the law of the place where Testator is domiciled at the time of death as described in N.C.G.S. § 31-46 and, therefore, is recognizable as valid for the application of N.C.G.S. § 28A-2A-17.

For many years and for years in the future, out-of-state counsel has recommended and will recommend that a testator have his or her will reviewed by counsel in his or her new domiciliary state. I do not expect that this legislation will eliminate the need for a testator to seek review of his or her will and update his or her estate plan after moving to our great State of North Carolina. It is still my understanding and belief that a will (and other estate planning documents) prepared by North Carolina counsel for a testator who has moved to our state should allow for ease of probate of the will and ease in administration of the estate. And, the self-proving affidavit is not the only reason to review a will (and other planning documents) for a new resident of North Carolina. For instance, the ease of distribution of tangible personal property at death is often facilitated by a written personal property memorandum. A testator who moves to North Carolina from, for instance, South Carolina is often uncomfortable with the possibility that his or her memorandum is precatory under North Carolina law (when it was mandatory in South Carolina) so there may be additional drafting for personal property in a testator's will. Also, for ease of administration at death, I believe that the administrative provisions of the will should refer to North Carolina law for this new resident. Further and not unique to an out-of-state will, a will should be reviewed for time to time for its other terms as well. Finally, based on my experience, I believe that a so-called in-state will prepared by North Carolina counsel for a testator who dies in North Carolina should allow for a more cost effective probate of the will and administration of the estate.

Our society is one in which a testator may live in more than one or two states during his lifetime. In the words of Wolfgang Amadeus Mozart, "A man of ordinary talent will always be ordinary, whether he travels or not; but a man of superior talent will go to pieces if he remains forever in the same place." As North Carolina has become a sophisticated hub for industry, technology, and medicine, its testators who die domiciled in North Carolina deserve for their wills to be respected, not simply ignored for some minor omission in the self-proving affidavit. A prudent, sophisticated testator will review his will with North Carolina counsel upon moving to North Carolina. If, however, a testator dies domiciled in North Carolina without doing so, North Carolina counsel now has more than one alternative or remedy to allow for the probate of an out-of-state will. •

Janice L. Davies is the member of Davies Law, PLLC. A special thanks to ***Andrew D. Tucker***, who is an associate at Davies Law, PLLC, for his contributions to this article.

Elderly Fraud

By Mike Anderson

"Our society must make it right and possible for old people not to fear the young or be deserted by them," penned Nobel-Prize winning author Pearl Buck in her autobiography, My Several Worlds: A Personal Record. "For the test of a civilization is the way that it cares for its helpless members."

By any measure, as the elderly segment of North Carolina's population rises, so too do incidents of abuse and exploitation. Session Law 2013-337, which was signed by the governor in July and is slated to take effect on Dec. 1, 2013, addresses these issues. Among its provisions, the act imposes upon financial institutions a *duty to report* suspected financial exploitation of the elderly. However, other provisions of the act seemingly – perhaps inadvertently – raise the bar for prosecutors seeking to hold criminally accountable those who exploit the elderly.

The Issue | Tales of elder abuse or exploitation stretch as far back as time itself. One such narrative is recounted in the Old Testament account of brothers Esau and Jacob. Their father, Isaac, had grown old and blind. Esau, the younger of the boys, conspired to trick his ailing father into bequeathing to him – rather than to the elder brother Jacob – the family birthright. Esau went so far as to fasten goatskins on his forearms, to simulate his older brother's hairier complexion, for when the blind Isaac embraced him. Such schemes and abuses are nothing new, but the ever-aging population provides increasing targets for would-be exploiters.

By the year 2030, according to the North Carolina Center for Public Policy Research, North Carolina's over-65 populace will nearly double, rising to 18 percent of all North Carolinians. (In four counties – Carteret, Cherokee, Clay, and Transylvania – the elderly will constitute *more than thirty percent* of the population; with 15 additional counties seeing *more than one-quarter* of their population over the age of 65.)

Perpetrators of elder fraud run the gamut, from sophisticated international schemes to the more ordinary, but equally dangerous, "wolves in the henhouse" such as relatives, caregivers, financial advisers, and even the occasional unscrupulous church or other charitable enterprise.

New Provisions: Detection Provisions Targeting Financial Institutions | The act includes a host of new provisions designed to enhance *detection* of elder fraud. It inserts an entirely new Article 6A into Chapter 108A of the General Statutes ("Social Services"). Most importantly, N.C.G.S. Section 108A-115(a) (eff. Dec. 1, 2013) *requires* any financial institution (which includes, by specific definition, banks and trust companies) to make a report whenever it has "reasonable cause to believe that a disabled adult or older adult is the victim or target of financial exploitation." In N.C.G.S. Section 108A-113(8) (eff. Dec. 1, 2013), the act establishes a bright-line rule, defining an "older adult" as any customer aged 65 or older. Any such suspected exploitation must be reported to local law enforcement agencies under N.C.G.S. Section 108A-115(a)(2) (eff. Dec. 1, 2013), and financial institutions are afforded immunity for any such reports made in good faith under N.C.G.S. Section 108A-115(c) (eff. Dec. 1, 2013).

In N.C.G.S. Section 108A-114 (eff. Dec. 1, 2013), the act also encourages, but does not require, financial institutions to offer disabled or older adult customers the opportunity to submit a list of trusted persons. When such a list is submitted to the bank, the bank must also report suspected exploitation to the individuals on that list under N.C.G.S. Section 108A-115(a)(1) (eff. Dec. 1, 2013).

"Financial exploitation" is defined in N.C.G.S. Section 108A-113(3) as "the illegal *or improper* use of a disabled adult's or older adult's financial resources for another's profit or pecuniary advantage." This definition – particularly the "improper" descriptor – would seem to cover a broad swath of activity, beyond the most obvious forms of exploitation or theft.

The act also provides a subpoena and compliance process when investigating entities seek a potential victim's financial records. The new statutory language details how a financial institution should comply with a subpoena issued by a superior or district court judge or magistrate, and provides "safe harbor" immunity for complying financial institutions. The act also prevents any financial records procured through such elder fraud subpoenas from being utilized to support a criminal or civil case against the customer. And last but not least, it imposes upon financial institutions a "duty to notify" its clients when financial records are subpoenaed. Banks must make immediate notification to their customers by first-class mail unless the investigating authority specifically procures a "delayed notice" order in its application for subpoena.

Revising Existing Law: Shifting Standard for Criminal Liability | For all its added protections with respect to *detecting* elder fraud or exploitation, the act would appear to render criminal prosecutions in prototypical cases of elder exploitation more difficult. Section 14-112.2, currently titled "Exploitation of an elder adult or disabled adult," is rewritten in two subtle, yet important, ways.

The first change would actually broaden applicability of the law by punishing those who exploit any "older adult," now defined *per se* as an individual over the age of 65, rather than the present definition of a vulnerable "elder adult" in Section 14-112.2(a)(2) as one "who is not able to provide for the social, medical, psychiatric, psychological, or legal services necessary to safeguard the person's rights and resources . . .."

However, the other revision alters the *mens rea* requirement in a manner that would appear to raise the bar for prosecutors, at least in certain cases. Under current statutory language in N.C.G.S. Section 14-112.2(b), persons who stand in a position of trust or confidence with an elder adult (or who have a business relationship with an elder adult) are criminally liable if they "knowingly, by deception or intimidation" obtain or use the elder's assets for benefit of someone other than the elder person. Subsection (c), however, which appears

Continued page 22

to apply to *any person* whatsoever, establishes liability merely where such a person "knows or reasonably should know that an elder adult or disabled adult lacks the capacity to consent" to the use of his or her funds for another's benefit.

The broader language of subsection (c) ("know or reasonably should know . . . lacks the capacity") is removed under the act, replaced – seemingly in an attempt to mirror the language of subsection (b) – with a *mens rea* requirement of "knowingly, by deception or intimidation." N.C.G.S. § 14-112(c) (eff. Dec. 1, 2013). The act does reconcile a seeming inconsistency, whereby the populace at large is held to a more stringent standard ("know or reasonably should know") than are persons in positions of trust and confidence ("knowingly, by deception or intimidation"). But it does so by settling for the facially less protective standard.

To be fair, in some circumstances the new language might trigger broader liability. It provides a new statutory remedy for ordinary consumer fraud-type conduct against any person over the age of 65, regardless of that person's mental capacity. But those individuals are already protected by consumer-fraud statutes applicable to victims across the board. In those prototypical exploitation scenarios where elderly adults need special protection most, this language would appear to lower the bar.

By way of illustration, one can conceive any number of scenarios whereby liability could be established under current language, but not under the new language set to take effect. For instance, imagine a relative or caregiver who is plainly aware of an elderly person's lack of capacity but nonetheless procures substantial "gifts." Or a televangelist — like the one whose tale was recounted during testimony before the Elderly Task Force on Fraud Against Older Adults, whose work precipitated this act — who procured exorbitant donations from a vulnerable elderly couple, effectively wiping out their estates and deeding himself their very home. Either such instance of exploitation might arguably be completed without "deception or intimidation." In fact, by their very nature a vulnerable elderly adult might not *need* to be deceived in order to be persuaded to part with their fortune. This statute would appear to lessen protection against such undue influence-style exploitation.

Criminal prosecutions under Section 14-112.2 are already rare. Fiscal-year 2011-12 saw just 17 convictions, statewide. Some might argue this is fitting. In all but the most extreme cases, perhaps civil litigation is the more appropriate forum to redress such behavior. (To be sure, many "undue influence" or exploitation cases exist in a "gray area" more befitting civil, rather than criminal, redress.)

But the very nature of these exploitation fact patterns oftentimes renders civil litigation ineffective or toothless. Fraud is often detected only after a victim's estate has been all but wiped out. The perpetrator has often spent, or squirrelled away, the misappropriated funds. And the victim's ensuing lack of resources make it very difficult to finance recovery litigation. (Add yet another layer whereupon, by the time the fraud is detected, the individual is often deceased or adjudicated incompetent, putting it in the hands of a risk-averse court-appointed fiduciary to finance and pursue an asset-recovery litigation.)

In sum, civil recovery is often an imperfect remedy in cases of elder fraud. And the act, for all its other merit, seems to make criminal recourse – in prototypical exploitation scenarios – even more difficult.

Summary & Practice Pointers | For banks, trust companies, and other financial institutions, the act imposes new duties and responsibilities, but also provides some reassuring safe harbors and immunities. Banks and trust companies would be well-advised to:

- consider the "suggestion" from the statute to create a "trusted persons" list for their vulnerable customers;
- familiarize themselves with the duty-to-report provisions;
- train staff members on recognizing indicia of abuse or exploitation;
- understand their duty to respond to subpoenas for financial records; and,
- establish protocols for making written notice to customers when records are subpoenaed, as well as understanding and recognizing "delayed notice" language in subpoenas.

For our part, practitioners can assist our clients by:

- counseling vulnerable clients on the option for providing "trusted persons" lists to financial institutions;
- being prepared to counsel individual clients on their rights, protections, and duties when they or a loved one are the subject of an elder fraud investigation;
- to the extent appropriate, helping clients (and trusted loved ones) recognize signs of potential abuse and exploitation; and,
- helping institutional clients understand the new compliance issues created under the act. •

Mike Anderson is an attorney in Davidson, North Carolina, whose practice includes fiduciary litigation.

Recent Developments

By John R. Cella Jr. and Ansley Chapman Cella

Federal Case Law Developments

No Loss of Exempt Status When IRA Funds Withdrawn and Re-deposited Within 60 Days.

In **In re: Rudd**, 2013 Bankr. LEXIS 2387 (Bankr. E.D.N.C. June 12, 2013), the Bankruptcy Court determined that $25,000 withdrawn from debtor's Simple IRA for personal living expenses and re-deposited within a 60-day period thereafter was not a prohibited transaction under Code Section 4975, nor did it cause the entire $246,973.91 IRA balance to lose its exempt status.

Claim for Refund Filed One Day Late Was Barred.

In **Estate of Langan v. United States**, 111 Fed. Cl. 654 (Fed. Cl. 2013), the taxpayer's counsel did not mail the estate tax refund complaint until Thursday at 11 p.m., which was the day before the expiration date of the statute of limitations. The complaint arrived on the following Monday. Taxpayer claimed that the complaint was properly placed in the mail but later admitted that the complaint arrived late. The Court granted the government's motion to dismiss.

Same-Sex Marriage Valid in State of Marriage and Recognized in State of Domicile Upon Death Qualifies Surviving Spouse for Estate Tax Marital Deduction in Estate Tax Refund Claim.

In **United States v. Windsor**, 133 S. Ct. 2675 (2013), a same-sex couple married in Canada resided in New York at the time of the decedent's death. The decedent left her entire estate to her surviving same-sex spouse (Windsor). Upon filing IRS Form 706 Windsor, as Executor, paid $363,053 in federal estate taxes and sought a refund. The IRS denied the refund, concluding that under the Defense of Marriage Act (DOMA) the marriage of decedent and Windsor did not qualify as a "marriage" for purposes of federal law, nor did Windsor qualify as a "spouse" as used in the term "surviving spouse" under the marital deduction rules of Code Section 2056(a). The United States Supreme Court upheld the findings of the District Court and Second Circuit Court of Appeals that the DOMA definition of marriage as "only a legal union between one man and one woman as husband and wife" and definition of "spouse" as "a person of the opposite sex who is a husband or a wife" were unconstitutional deprivations of the equal liberty of persons protected under the Constitution's Fifth Amendment. Accordingly, Windsor, as a surviving spouse in a lawful marriage, became entitled to the refund.

Executor Who Relied on CPA's Erroneous Advice that Estate Tax Return Extended for One Year Did Not Show Reasonable Cause In Filing Return Three Months Late.

In **Knappe v. U.S.**, 713 F.3d 1164 (9th Cir. Cal. 2013), cert denied Oct. 15, 2013, the decedent named a longtime friend and successful businessperson as her executor. The executor had no prior experience serving as an executor, so he hired a CPA who had worked as a corporate tax accountant for the executor's company for many years. At the executor's request, the CPA completed and filed IRS Form 4768, an "Application for Extension of Time to File a Return and/or Pay US Estate (and Generation-Skipping Transfer) Taxes". Form 4768 gives taxpayers the option of seeking an extension of time to file the estate tax return, an extension of time to pay estate taxes, or both. Part II of the instructions provides that the executor may apply for an automatic extension of time to file the return. An executor who is out of the country may apply for an additional six-month extension. Part III, Extension of Time to Pay, provides that an extension of time to pay of up to twelve months may be granted in the Service's discretion. The CPA filed for a 12-month extension of time to pay estate taxes and for an automatic six-month extension of time to file but incorrectly advised the executor that both extensions were for one year (not six months). The executor reviewed the IRS-approved extension request but only noted the due date for the extension of time for payment (twelve months), and filed the estate tax return within that period, but several months late. The IRS assessed penalties against the estate. The executor requested an abatement of the penalty asserting that his reliance on the CPA's erroneous advice was reasonable cause for the late filing. The IRS denied the request. The executor's administrative appeal of the decision was also denied. The executor paid the full penalty amount and filed a claim for refund which was denied. The executor filed a refund action alleging that his reliance on CPA was reasonable cause to excuse the penalty. The Court distinguished between substantive and non-substantive tax matters in considering whether the executor had reasonable cause to rely upon the CPA's advice. The Court reasoned that because the instructions and governing statute on the time to file an estate tax return were clear, the matter is a non-substantive matter. The Court held that the executor failed to exercise ordinary business care and prudence by relying on the CPA's erroneous advice on a "non-substantive" matter. Furthermore, it was the executor's non-delegable duty to ascertain the correct extended filing deadline.

Assumption of Potential Code Section 2035(b) Estate Tax Liability is Calculable for Purposes of Reducing Value of Net Gift.

In **Steinberg v. Commissioner**, 141 T.C. 8 (Sept. 30, 2013), an 89 year-old taxpayer made gifts of cash and marketable securities to her four daughters, subject to an agreement whereby the daughters agreed to pay any Federal gift taxes imposed on the value of the gifts. The donees also agreed to pay any Federal or State estate taxes imposed on the value of the gift taxes paid on the gifts within three years preceding death under Code Section 2035(b). The taxpayer and her daughters executed the net gift agreement after several months of negotiation using separate counsel. The taxpayer hired an appraiser to calculate the fair market value of the property transferred to the daughters. The appraiser calculated the fair market value of the gifts first, and then reduced that value by (1) the value of the gift taxes paid by the daughters, and (2) the actuarial value of the assumption of potential Code Section 2035(b) liability if taxpayer died within three years (based, in part, upon annual mortality rates in each of the three years following the gift). The appraiser determined that the aggregate fair market value of the net gift was $71,598,056 (including a discount of $5,838,540 for the value of assumed potential Code Section 2035(b) estate tax liability). The taxpayer timely filed IRS Form

Continued page 24

709 (with a copy of the net gift agreement) reporting the $71,598,058 value of the gift and total gift tax of $32,034,311. The Service mailed a notice of deficiency, which disallowed the discount for the assumption of potential estate tax liability. The taxpayer filed a petition in Tax Court and the Service filed a motion for summary judgment. The sole issue asserted by the Service was that the daughters' assumption of potential Code Section 2035(b) estate tax liability did not increase the value of the petitioner's estate and therefore did not constitute consideration in money or money's worth (under Code Section 2512(b)) in exchange for the gifts. The opinion contains a comprehensive history of net gifts and Code Section 2035(b). The Tax Court rejected its own analysis in McCord that the value of the contingency was "too speculative" to be determined. While the Tax Court in McCord was later reversed by the 5th Circuit Court of Appeals, the case at hand was not within the 5th Circuit, and therefore not bound by that reversal. Consistent with the appellate McCord decision, the Tax Court found as a matter of law that the actuarial value of the assumption of estate tax liability was not precluded from treatment as consideration in money or money's worth for purposes of determining the value of the "net net" gift.

IRS Terminates Estate Tax Payment Plan Under Code Section 6166 for Missed Installment Payments While Valuation of Estate Asset is Pending.

In **Estate of Adell v. Commissioner**, T.C. Memo. 2013-228 (Sept. 30, 2013), the Tax Court upheld the IRS's decision to terminate a Code Section 6166 estate tax installment payment plan on account of the estate's failure to make two required annual payments. The estate had applied for an extension to make the interest payments in two of the first five years of the estate's fifteen-year estate tax payment plan. Successive personal representatives had been replaced during that time and were involved in a number of actions involving recovery of estate assets from predecessors. In addition, one of the estate's assets reported as $9.3 million on the IRS Form 706 was subject to a proposed adjustment to $92 million by the Appeals officer. The estate tax installment payments were not made when due, and the Service issued a final notice and demand for estate tax installment payments. The Service then issued a preliminary determination letter terminating within 30 days the Code Section 6166 election. During discussions relating to the estate's protest to the proposed adjustment, no attempt by estate's counsel was made to address the termination of the Section 6166 election. After receiving notification that the Code Section 6166 election had been terminated, the estate filed a petition claiming that the termination of the Code Section 6166 election was an abuse of discretion given the uncertainty of the amount of estate tax owed by the estate. The estate took the position that the case should not be tried until the valuation matters had been resolved. Finding that the disputed value of the estate asset was not material to the abuse of discretion analysis, the Tax Court upheld the IRS's termination of the estate tax installment payment plan.

Federal Administrative Developments

IRS Releases Interest Rates to be Used By Estates For Special Use Farm Real Property Under Code Section 2032.

In **Revenue Ruling 2013-19** (Sept. 23, 2013), the Service issued the 2013 interest rates to be used in computing the special use value of farm real property under Code Section 2032A. The rates range from 4.99% to 5.49% depending upon the state in which the property is located.

Windsor Extended to Recognize Valid Same-Sex Marriages in Every State for All Federal Tax Purposes as of September 16, 2013 and Retroactively for Open Tax Years.

In **Revenue Ruling 2013-17** (Aug. 29, 2013), two months after **Windsor**, the Department of Treasury and the Internal Revenue Service issued Revenue Ruling 2013-17 extending the application of **Windsor** to apply "spouse" and "marriage" to same-sex spouses for all federal tax purposes and in all states, not just those states such as New York that recognize same-sex marriage. The marriage must have been valid in the state, territory, or foreign country where the couple was married. Specifically, the ruling held that Internal Revenue Code terms "spouse" and "marriage" include, respectively, "an individual married to a person of the same sex if the couple is lawfully married under state law" and "a marriage between individuals of the same sex." Consistent with **Windsor**, where taxpayer sought a refund based on application of the marital deduction to a same-sex spouse, the Service's ruling further addressed Code references to "husband and wife" found no evidence that Congress intended to exclude any couple legally married under state law. The Service pointed out that individuals of the same sex are lawfully married for Code purposes as long as they were married in a state authorizing same-sex marriages without regard to domicile or subsequent changes thereto. A significant consideration is the need for uniformity, stability, and efficiency in the application of the Code. Otherwise taxpayers, the Service, and third parties such as employers and plan administrators would risk costly errors and delay. The Service clarified that marriage does not extend to "registered domestic partnerships, civil unions, or other similar formal relationships recognized under state law that are not denominated as a marriage under that state's law." Furthermore, parties to such non-marriage designations regardless of sex thereof do not fall within the Code's terms "spouse", "husband and wife", "husband", and "wife". The prospective effective date is September 16, 2013. On or after that date same-sex legally married same-sex couples must file "married filing jointly" or "married filing separately," and may file refunds claim for all open tax years (2010, 2011, 2012) for any taxes paid (income, gift, estate, etc.). This specifically includes income tax with respect to employer-provided health coverage benefits or fringe benefits provided by the employer and excludable from income based on marital status. The Service expects to provide further guidance on application of **Windsor** to employee benefit plans and similar arrangements.

IRS Consolidates Revenue Procedures To Provide Exclusive Relief Method For Late S Corporation, ESBT, QSST, QSub, and Entity Classification Elections.

In **Revenue Procedure 2013-30, 2013-36 IRB 173** (Aug. 14, 2013), the IRS consolidated several revenue procedures into one that sets forth the exclusive method for taxpayers to request relief for late S Corporation elections, electing small business trust (ESBT) elections, Qualified Subchapter S Trust (QSST) elections, Qualified Subchapter S Subsidiary (QSub) elections, and late entity classification elections intended to have the same effective date as that for an S corporation election. The Service included a helpful flowchart for application of the new procedures.

Property Transferred to Revocable Trust is Subject to Federal Tax Lien.

In **Chief Counsel Advice 201324017** (June 14, 2013) the IRS addressed whether a federal tax lien (FTL) attaches to property held in the name of a revocable trust. Taxpayer transferred property to a revocable trust. Under Code Section 6321 the FTL attaches to all the taxpayer's property and rights to property. Under Code Section 676 the grantor of a trust is treated as the owner of the trust when the power to re-vest in the grantor is exercisable by the grantor or a non-adverse party, or both. The Service also cited the trust law principle that revocable trust assets are treated as property of the settlor of the trust. Accordingly, the property transferred by the taxpayer to his revocable trust is treated as the taxpayer's property for lien attachment under Code Section 6321.

Policy Dividends Alone are Not Incidents of Ownership in Life Insurance Policies.

In **Chief Counsel Advice 201328030** (July 12, 2013) the IRS addressed whether at death a decedent insured possessed an incident of ownership in life insurance policies such that the proceeds are includible in the decedent's gross estate under Code Section 2042. Decedent and former spouse had executed a property settlement agreement that required decedent to maintain life insurance policies for the sole benefit of the former spouse. Decedent paid premiums but could not borrow against or pledge the policies. Policy dividends belonged exclusively to decedent. Upon decedent's death the insurance company paid the policies' proceeds to former spouse, and the executor included the proceeds as part of decedent's gross estate on Form 706. Under Code Section 2042(2) the gross estate includes property received by all beneficiaries (other than decedent's estate) as insurance under life insurance policies with the decedent as insured and in which decedent at death possessed any incidents of ownership. The Treasury Regulations provide that the term "incidents of ownership" refers to the rights of the insured or the insured's estate to the economic benefits of the policy. The Service cited the Tax Court's previous holdings that the right to dividends that may be applied against current premiums is a mere reduction in the amount of premiums paid, not a right to a policy's income. Decedent had agreed to maintain the policies solely for the spouse's benefit. Furthermore, according to the Service, even though the policies' dividends technically "belonged" to decedent, the right to dividends, by itself, was not an incident of ownership that would cause inclusion under Code Section 2042(2).

Service Addresses Estate and Gift Tax Consequences of Sale of Stock in Exchange for Notes Including SCINs.

In **Chief Counsel Advice 2013300033** (July 26, 2013) decedent updated his estate plan in the year before the year of his death. In a series of transactions he sold and made gifts of stock to several newly established grantor trusts for family members ("new trusts"). At some point over the period of the sale and gift transactions he became ill and died less than six months after the diagnosis. In the first set of transactions decedent funded grantor trusts with common voting and preferred non-voting stock. Before the funding he substituted common and preferred shares for preferred shares held by existing grantor trusts ("old trusts"). Appraisers valued the stock for purposes of the substitutions and transfers to the new trusts. In the second set of transactions the decedent substituted common and preferred shares for other shares held in the old trusts for the benefit of family members. At the same time, after completing the substitutions, he made a gift of shares to a grantor-retained annuity trust ("GRAT"). Decedent died before the end of the GRAT term, and the GRAT assets that were part of the gross estate passed to charity. On the same date as the second set of transactions decedent entered into a third set of transactions. He transferred stock to the "new trusts" in exchange for promissory notes with a term based on the Code Section 7520 life expectancy tables. Some notes had face amounts equal to the appraised value of the transferred stock to the grantor trusts, with interest payable annually and principal payable at the end of the term. Other notes were self-canceling installment notes ("SCINs"), i.e., the grantor trust, as maker, was relieved from making payments on the note if the holder (decedent) dies before all payments come due. The face value of the SCINs were roughly double the value of the stock to reflect the risk that principal and interest would not be paid to decedent upon death before the end of the note term. The fourth set of transactions entailed decedent's transfer of stock to the old trusts. In exchange he received notes with a face value equal to the appraised value of the stock. The term was based on the Code Section 7520 life expectancy tables, with interest payable annually and principal payable at the end of the term. Instead of the higher face value these notes had a higher interest rate. Decedent died before receiving any principal or interest on these notes. At the same time as the fourth set of transactions, decedent entered into a fifth set of transactions that created another GRAT and funded it with stock and promissory notes received from the previous sales. Shortly after the fourth and fifth set of transactions decedent was diagnosed with an illness and died less than six months thereafter.

The decedent's estate filed IRS Form 709 (gift tax return) setting forth the GRAT-related taxable gifts and corresponding gift tax, some non-taxable gifts, and the SCIN transactions with no gift taxable gift reported. The estate also filed IRS Form 706 (estate tax return), which set forth on Schedule G (i) the non-self-cancelling promissory notes at face values plus accrued interest, and (ii) the value of the GRATs, but not the SCINs.

The issues were (i) whether decedent's transfers of stock to grantor trusts in exchange for SCINs constituted a gift; (ii) how to determine the fair market value of the SCINs; and (iii) if the transfers did not constitute a gift, the estate tax consequences of the cancellation of the SCINs upon the decedent's death.

Continued page 26

With respect to the first issue, whether the transfer of stock in exchange for SCINs constitutes a gift, the Service looked to whether the value of the notes is equal to the value of the stock. If the FMV of the promissory notes is less than the FMV of the property transferred to the grantor trusts, then the difference is a deemed gift under Code Section 2512(b). Treasury Regulations Section 25.2512-4 provides that the FMV of secured or unsecured notes is presumed to be the unpaid principal plus accrued interest to date of the gift unless the donor establishes a lower value by satisfactory evidence (e.g., interest rate, maturity date, uncollectible, insufficient security). Treasury Regulations Section 25.2512-8 provides that a sale or exchange in the ordinary course of business will be considered as made for adequate and full consideration in money or money's worth. In this case, the Service noted that the face value and length of payment must be reasonable based on the circumstances. The total face value of the notes was almost twice the amount of the stock to take into consideration the self-cancelling nature of the notes. The notes called for interest-only payment until a balloon payment at the end of the term. The decedent died less than six months after the transfer and did not receive interest or principal payments prior to death. The Service distinguished the facts from those in **Estate of Costanza v. Comm'r,** 320 F.3d 595 (6th Cir. 2003) where a business was sold to a taxpayer's son for a SCIN which called for regular payments of interest and principal necessary to provide a steady stream of income to the taxpayer. In that case there was a bone fide arrangement because the decedent expected repayment and intended to enforce the collection. In this case, the Service noted that a steady stream of income was not contemplated, the decedent had substantial assets, and that the decedent did not require income from the notes to cover his living expenses. The Service concluded that the arrangement was nothing more than a device to transfer the stock to other family members at a lower value than the fair market value of the stock.

With respect to the second issue, how to determine the fair market value of notes with a self-cancelling feature, the reported value of the notes was based on a term chosen within the decedent's life expectancy and then either the face amount or interest rate was adjusted to account for the value of the self-cancelling feature. The Service noted that unlike annuities, life estates, term or remainder interests, where is it appropriate to base valuation on the decedent's life expectancy, the FMV of promissory notes is based on a willing-buyer willing-seller standard and should take into consideration decedent's medical history on the date of the gift.

With respect to the third issue, the consequences of the self-cancelling feature upon death, Code Section 2033 includes the value of all property to the extent of the decedent's interest at the time of death and Code Section 2038 includes the value of any interest which the decedent has transferred (except in the case of a bone fide sale for an adequate and full consideration) the enjoyment of which is subject to change through the exercise of a power by decedent. The Service compared the facts to a case where the decedent made a loan to his son a month before his death for the stated purpose of satisfying a debt of his sister's estate. Estate of Musgrove v. United States, 33 Fed. Cl. 657 (1995). In **Musgrove** the court concluded that the property was includible in the decedent's estate because he had retained the note at his death, never demanded repayment, and controlled the son's use of the money (to pay the debt on the sister's estate). In the ruling, the Service noted the similarities – the use of a SCIN by a person in poor health, right before death. The Service concluded without analysis that there were no estate tax consequences associated with the cancellation of the notes upon the decedent's death.

***Fractional Funding of Charities' Share of Residuary with IRAs Naming Estate as Beneficiary is not a Transfer of IRD Taxable to Estate*.**

In **PLR 201330011** (July 26, 2013), the IRS addressed the distribution of several IRAs in fractional shares between charitable residuary beneficiaries of a decedent's revocable trust. The estate was the beneficiary of each IRA. The terms of the decedent's will provided for distribution of assets to the decedent's revocable trust. The decedent's revocable trust provided that two charities receive fractional shares of the residue of the decedent's estate. Code Section 691(a)(2) provides the general rule that when the right to receive IRD is transferred by an estate, the full fair market value of the right to receive IRD is included in the estate's income. Treasury Regulations Section 1.691(a)-4(b) provides an exception for transfers of the right to receive IRD to a specific or residuary legatee, in which case the recipient, not the estate, includes items of IRD in income only in the tax year in which the income is received. The transfer of the IRAs to the charities will not result in IRD taxable to the estate; rather, the charities will include IRD in their gross income when distributions actually received.

Trust Transfer of Policy on Husband and Wife is Not a Transfer for Valuable Consideration.

In **PLR 201332001** (Aug. 9, 2013), the Service addressed the transfer of a life insurance policy insuring the lives of husband and wife from a trust for the benefit of children distributable outright at the death of the surviving spouse to a perpetual trust for the benefit of the children with special needs provisions for one of the children. Husband and wife were partners of a partnership. The transfer was for consideration equal to the interpolated terminal reserve value of the policy. The latter trust, a grantor trust for income tax purposes, will own the policy that, in turn, will be treated as owned by the Grantor husband. The portion of the life insurance policy insuring the life of the wife will be treated as transferred to the husband as a partner in the partnership with the wife as partner. Accordingly, the transfer was excepted from the transfer for value rule of Code Section 101(a) because it was a transfer to an insured and to the partner of the insured for income tax purposes.

Valid Disclaimer of pre-1977 Trusts Within Nine Months of Learning of Transfers.

In **PLR 201334001** (Aug. 23, 2013), the Service addressed a disclaimer of a remainder interest in each of four trusts created before the Jan. 1, 1977, the effective date of Code Section 2518. Taxpayer proposed to execute the disclaimers within nine months after learning of the transfers creating the interests. The Service cited Regulation Section 25.2511-1(c)(2) and case law, which for pre-1977 interests generally requires that the refusal to accept ownership be made within a reasonable time after knowledge of the existence of the transfer, not after distribution or vesting of the interest. As long as the disclaimers complied with the applicable regulation and were valid under state law, the taxpayer's disclaimers of interests in the trusts would not be taxable gifts under Code Section 2501.

QTIP Election Not Necessary to Reduce Estate Taxes to Zero is Void.

In **PLR 201338003** (Sept. 20, 2013), the Service addressed a QTIP election that was not necessary to reduce estate taxes to zero. The decedent left his residuary estate to a revocable trust that became irrevocable upon his death. Pursuant to trust terms the Trustee was directed to fund a marital trust and a credit shelter trust. Under the terms of the credit shelter trust, the Trustee was directed to distribute income and principal to the surviving spouse and children. Spouse, as executrix of the estate, allocated the residuary estate to the credit shelter trust (not enough to fund marital trust) and filed IRS Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return listing the credit shelter trust as QTIP property. Code Section 2044 provides the value of the gross estate includes the surviving spouse's QTIP property. Code Section 2519(a) and (b) provides that disposition of all or part of the QTIP property is treated as a transfer of all interests in the property other than the qualifying income interest. Code Section 2652(a) provides that the surviving spouse will be treated as the transferor of the QTIP property for generation-skipping transfer (GST) tax purposes in the absence of a "reverse QTIP" election under Code Section 2652(a)(3). Under Rev. Proc. 2001-38, 2001-1 C.B. 1335, the Service will treat a QTIP election as null and void for purposes of Code Sections 2044(a), 2056(b)(7), 2519(a), and 2652 where the election was not necessary to reduce estate tax liability to zero. In this ruling the estate tax liability would have been zero without the QTIP election, so the Service ruled that the election was null and void for estate, gift, and GST purposes.

Division of IRA into Three sub-IRAs for Intestate Beneficiaries Is Not a Transfer of IRD Taxable to Estate; 5-Year Rule Applies.

In **PLR 201338028** (Sept. 20, 2013), the Service addressed the death of a 68 year-old IRA owner whose failure to name beneficiaries resulted in the (intestate) estate as beneficiary. The IRA owner died before reaching his required beginning date, and the IRA did not have a designated beneficiary, so the five-year rule applied to distributions from the IRA as later divided. The division into separate IRAs for each heir was not a "transfer" of IRD for income tax purposes, so amounts were taxable only as distributed from each separate IRA to the corresponding heir. The Service also noted that nothing in the Code Section 401(a)(9) or the corresponding Treasury Regulations precluded posthumous division of an IRA into more than one IRA.

North Carolina Case Law Developments

Court of Appeals Affirmed Order to Disqualify Counsel from Representing Fiduciary in Individual Capacity.

In **Williams v. Williams**, 746 S.E.2d 319 (N.C. Ct. App. Aug. 6, 2013), heirs sought damages and declaratory relief against Defendant in both individual and fiduciary capacities. Plaintiff heirs were decedent's siblings, and Defendant (Amber) had represented to the Clerk that she was decedent's daughter and sole heir-at-law. Amber had bank add her name as a co-owner of a survivorship account, and she retained counsel to prepare a durable power of attorney naming her as decedent's attorney-in-fact. The Clerk appointed Amber as administratrix; thereafter the siblings petitioned for Amber's removal. The Clerk determined that Amber was not an heir but allowed her to continue serving as administratrix. Thereafter the siblings filed suit asserting claims against Amber in both individual and fiduciary capacities. On behalf of Amber in fiduciary capacity, law firm moved to dismiss, then siblings moved to disqualify law firm from the fiduciary representation. The trial court found that law firm had represented Amber in both capacities and disqualified it from individual representation. The Court of Appeals found no abuse of discretion and noted as persuasive N.C. St. B. Ethics Op. RPC 137 (Oct. 23, 1992) (lawyer who formerly represented estate cannot later defend the former PR against estate's claim) and N.C. St. B. Ethics Op. RPC 22 (Apr. 17, 1987) (in absence of heirs' consent lawyer cannot represent administratrix in both fiduciary and individual capacities where interests in the two roles conflict).

Civil Cause of Action for Perjury Not Available in Fraudulent Will Matter.

In **Gilmore v. Gilmore**, 748 S.E.2d 42 (N.C. Ct. App. Sept. 17, 2013), three defendants (Sherrie, Deana, and Milton) conspired to create a fraudulent will for Sherrie's husband, Jackie. Deana and Milton signed the paper as witnesses knowing that Jackie did not sign the paper, did not ask them to sign as witnesses, and did not indicate that he intended the paper to be his will. After Jackie died Sherrie submitted it for probate falsely stating that it was Jackie's will and that under oath and penalties of perjury she believed that the paper was Jackie's will. Deana and Milton further signed the affidavit of subscribing witnesses under penalties of perjury. Plaintiffs moved to revoke probate, and defendants gave false testimony at the hearing. Plaintiffs filed an amended complaint asserting claims for fraud, conspiracy to commit fraud, a pattern of racketeering activity in violation of N.C. RICO, and obstruction of justice. The court denied judicial notice of the criminal charges and the trial court's revocation of probate of the purported will. The court granted defendants' 12(b)(6) motion to dismiss for failure to state a claim. It reaffirmed the well-established principle that perjury and subornation of perjury, though indictable criminal offenses, do not give rise to a civil cause of action in North Carolina.

Three-Year Statute of Limitations Barred Claim for Fraud; Existence of Fiduciary Relationship Alone Was Not Sufficient to Extend Statute of Limitations to Ten Years for Constructive Fraud; Modification of Testamentary Trust Action was Impermissible Because Not Filed as a Caveat.

In **James v. Schoonderwoerd**, 2013 N.C. App. LEXIS 943 (N.C. Ct. App. Sept. 17, 2013), the Court of Appeals addressed whether the three-year statute of limitations was appropriately applied to bar claims for constructive fraud and trust termination and modification in a case against an attorney-in-fact and trustee acting under documents prepared by and executed with an attorney. The clients, a husband and wife, had a daughter with two children and a son with no

Continued page 28

children. The daughter contacted an attorney about meeting with her parents to prepare and execute estate planning documents. The attorney met with the couple and daughter (separately) over the course of several months in 2001. During that time the attorney met with and discussed credit shelter planning with the clients and explained that they would have to execute deeds dissolving tenancy by the entirety ownership of their four tracts of real property. The daughter, and later the daughter's son, were named as sole attorneys-in-fact. The wills named the daughter, her children, and the son as beneficiaries of a testamentary trust with the surviving spouse and grandson named as co-trustees. The clients also executed deeds changing the ownership of the properties to tenants-in-common. The wills were subsequently amended two months later by codicil to change the beneficiaries of the testamentary trust to only the clients' children. The husband died in 2003, and while the estate was open, the wife sold one of the properties, signing the deed both in her individual capacity and as co-trustee of the trust. She received one-half of the sale proceeds in her individual capacity. In 2004, one year after her husband's death, the wife met with a new attorney to understand the will and trust. As a result of the meeting, she asked the new attorney to prepare a new will leaving all her property to her son. She signed the new will in 2004 and then tried several times from 2005 to 2008 to gain control of the trust assets until filing an action in 2010, almost six years after her meeting with the new attorney to explain the terms of the will and trust. Upon deposition, she testified that she did not remember meeting with the attorney and was on seventeen medications during the time. Her husband's neurologist testified that the husband suffered from vascular dementia and that he expected him to have "significant cognitive impairment" that would not allow him to execute legal documents. The wife testified that neither she nor her husband understood the wills and deeds that they executed in 2001. The attorney testified that their daughter told him in 2001 that her parents were "very competent" and he testified that he found the wife to be very competent when she executed the will in 2001. The elements of a constructive fraud claim necessary to extend the statute of limitations to 10 years are (1) a relationship of trust and confidence, (2) the defendant took advantage of that position to better himself, and (3) injury to the plaintiff. The court noted that the only transactions in question were the power of attorney naming daughter in 2001, power of attorney naming daughter's son later in 2001, and deeds terminating tenancies by the entirety in 2001. The constructive fraud claim surrounding the execution of the 2001 will could not be brought because this action can only be brought by caveat. The court noted that the mere existence of the fiduciary relationship evidenced by the powers of attorney was not enough when the individuals named never acted under the power of attorney to transfer the principal's property. Finally, the court did not find that execution of the deeds benefited the daughter or her son. The court found it clear that husband intended to benefit both of his children by executing the will, and that to the extent the wife wanted to revise her documents to change the disposition of her assets, she may do so, but the court would not allow the transfer of assets in trust that would be to the detriment of the husband's trust beneficiaries. With respect to the modification and termination of trust claim, the Court supported the finding of summary judgment, citing cases supporting the proposition that the action was an impermissible collateral attack of the terms of a will and should have been brought as a caveat action. Finally, the court affirms the dismissal of the fraud action by finding that the wife had reason to discover the alleged fraud when she met with the new attorney in 2004. She did not file a complaint until 2010, which was after the three-year statute of limitations had run.

The Statute of Limitations Barred Actions for Fraud and Breach of Fiduciary Duty.

In **Robert K. Ward Living Trust v. Peck**, 2013 N.C. App. LEXIS 961 (N.C. Ct. App. Sept. 17, 2013), the successor trustee of a trust brought an action for fraud and breach of fiduciary duty against the former trustee (the attorney who drafted the trust) more than six years after the trustee resigned as trustee. The actions were barred by the expiration of the five-year statute of limitations.

North Carolina Administrative Developments

Application of Windsor and Revenue Ruling 2013-17 in North Carolina Prohibits Same-Sex Couples from Filing as Married and Will Require Separate Calculation and Reporting for State Income Tax Purposes.

In NCDOR Directive PD-13-1 (Oct. 18, 2013), the NCDOR addressed the impact of IRS Revenue Ruling 2013-17 on filings for North Carolina individual income and withholding tax purposes. NCDOR will not follow the new definitions in Rev. Rul. 2013-17 because North Carolina does not recognize same-sex marriages as valid. Individuals who enter into a same-sex marriage in another state cannot file as married filing jointly or married filing separately, but must file as single or head of household or qualifying widower. Such individuals must prepare a pro forma federal return to determine each individual's adjusted gross income, deductions, and tax credits allowed under the Code for the filing status used for North Carolina purposes and then attach a copy of the pro forma return to the North Carolina return.

North Carolina Legislative Developments

Session Law 2013-81 (increasing year's allowance for a surviving spouse) | N.C.G.S. § 30-15, -29. Effective for estates of persons dying on or after January 1, 2014, the surviving spouse's year's allowance increases from $20,000 to $30,000.

Session Law 2013-91 (updating and clarifying provisions of laws governing estates, trusts, guardianships, powers of attorney, and other fiduciaries) | N.C.G.S. § 28A-18-2(a). The wrongful death recovery provisions were amended to correct the reference to the State Health Plan subrogation rights and to clarify that claims for the decedent's burial expenses and reasonable hospital and medical expenses are subject to the approval of Clerk of Superior Court.

N.C.G.S. § 28A-29-1, -2(a). The relatively new provisions on notice to creditors without estate administration were amended to describe in more detail when the procedure can be used. Generally speaking, if no application or petition for appointment of a personal representative is pending or has been granted, a qualified person or trustee of decedent's revocable trust can invoke the procedure in one of five situations: (i) the decedent died testate or intestate and left no personal property subject to probate and no real property devised to the personal representative; (ii) administration by collection by affidavit; (iii) administration by summary administration; (iv) estate consisting solely of a motor vehicle transferable under N.C.G.S. § 20-77(b); or (v) the decedent left assets that may be treated as assets of an estate for limited purposes under N.C.G.S. § 28A-15-10.

N.C.G.S. § 30-3.1. The elective share provisions were amended to determine the surviving spouse's share based simply on the length of the marriage, not on the existence or number of lineal descendants and whether the spouse is a second or successive spouse. Effective for estates of decedents dying on or after Oct. 1, 2013, the applicable share of the Total Net Assets is as follows:

Provision	Length of Marriage	Applicable Share Percentage
N.C.G.S. § 30-3.1(a)(1)	< 5 years	15%
N.C.G.S. § 30-3.1(a)(2)	≥ 5 years but < 10 years	25%
N.C.G.S. § 30-3.1(a)(3)	≥ 10 years but < 15 years	33%
N.C.G.S. § 30-3.1(a)(4)	≥ 15 years	50%

N.C.G.S. § 30-31. The Year's Allowance provision was amended to clarify that the Clerk of Superior Court may order the estate to pay the surviving spouse's attorney's fees and costs and that such amounts are paid as administrative expenses of the estate.

N.C.G.S. § 31-11.6. The provisions setting forth how attested wills may be made self-proved were amended to expand as self-proving those wills shown by the propounder as self-proving under the laws of another state. Furthermore, military testamentary instruments executed in accordance with 10 U.S.C. § 1044d(d) are considered self-proved.

N.C.G.S. § 31-46. The will validity provisions were expanded to include as valid wills executed in compliance with the laws of the place where executed at the time of execution, wills executed in compliance with the laws of the decedent's domicile at execution or at death, or military testamentary instruments executed in accordance with 10 U.S.C. § 1044d(d). The provisions on non-resident decedent wills also were updated to include the additional executed wills considered valid under N.C.G.S. § 31-46.

N.C.G.S. § 36C-1-114. This is a new section of the trust code that codifies a trustee's insurable interest in a person insured under a trust-owned life insurance policy. On the date the policy is issued, the insured must be either the settlor or a person in whom the settlor has an insurable interest upon issuance of the policy. In addition, the policy proceeds must be primarily for the benefit of one or more trust beneficiaries that have an insurable interest in the insured's life. This new provision does not limit any existing common law or statutory right to insure, and it must be construed liberally to sustain insurable interest.

N.C.G.S. § 36C-5-505(c). This provision was amended to clarify that the settlor's spouse is a person to whom the settlor was married at the time the irrevocable intervivos trust was created, notwithstanding a subsequent dissolution of the marriage.

N.C.G.S. § 36C-8-816. Among the trustee powers is the power to exercise federal, state, and local tax elections. This provision was expanded to include consideration of discretionary distributions to a beneficiary as made from capital gains realized during the year.

N.C.G.S. § 36C-8-816.1(c)(3). The decanting statute was further clarified. With respect to the trustee's power to appoint to a second trust, the existing provision prohibiting the second trust terms from reducing a beneficiary's fixed income, annuity, or unitrust interest in the original trust was amended to require that such interest actually have come into effect with respect to such beneficiary.

N.C.G.S. § 36C-8-816.1(c)(8), -(e)(2). With respect to the exercise of the power to appoint principal or income to a second trust, the references to N.C.G.S. § 41-23 (Perpetuities and Suspension of Power of Alienation for Trusts) were updated such that the limitation specifies the permissible period allowed for the suspension of the power of alienation of the original trust and the time from which the permissible period is computed.

N.C.G.S. § 1C-1601(a). The provisions exempting IRAs from creditor claims were amended to clarify that after the IRA owner's death IRA assets remain exempt if held by one or more subsequent beneficiaries via direct transfer or eligible rollover excluded from gross income. The new provision specifically includes direct transfers or eligible rollovers to "inherited" or "beneficiary" IRAs.

N.C.G.S. § 32-72(d). The provisions addressing directed fiduciaries other than trustees were expanded beyond the power to direct or consent to a fiduciary's actions to include all powers with respect to actions of a fiduciary. An additional exception to the rule that persons who hold such powers are fiduciaries was added to beneficiaries who hold such powers was added to provide that the beneficiary who has the power to remove and appoint a fiduciary is not a fiduciary.

N.C.G.S. § 35A-1251, -1336.1, -1341.1. With respect to gifts by incompetents that require judicial approval, the prerequisite that the gift not exceed the federal gift tax annual exclusion was expanded to provide that the gift may qualify either for the federal annual gift tax exclusion under Code Section 2503(b) or is a qualified transfer for tuition or medical expenses under Code Section 2503(e). The general provision that a guardian of the estate of an incompetent ward not

Continued page 30

Developments, *continued from page 29*

alter the ward's estate plan was expanded to allow the guardian to incorporate tax planning or public benefits planning into the existing estate plan, which may include leaving assets in trust.

N.C.G.S. § 78C-2, -8. The Dodd-Frank Act replaced the "private adviser" exemption for individuals with fewer than fifteen clients with a rule that now gives the SEC the ability to define "family offices." The provisions that incorporated the (now repealed) federal law were revised to preserve the exemption at the state level for private advisers who had fewer than fifteen clients during the preceding 12 months.

Session Law 2013-132 (amending laws governing credit unions)
N.C.G.S. § 54-109.58(e)-(h). A credit union is not liable for complying with a writ of execution, garnishment, attachment, levy, or other court-ordered process to seek funds held in the name of any joint tenant. A joint account with right of survivorship at a credit union may be established by election by the joint tenants on a signature card or explanation in a separate document. Any joint tenant may terminate the account, and where an account is held by two or more individuals, the account will remain in the name of the remaining tenants, but the removed joint tenant will remain liable for any debts incurred in connection with the joint account during the period in which named as a joint tenant.

N.C.G.S. § 109.60A, -B. These provisions govern the administration of share, deposit, and custodial share accounts opened by or on behalf of minors.

N.C.G.S. § 109.62, -62A. These new provisions govern the administration and disposition of an account for a principal, decedent, or incompetent by the respective agent or duly qualified representative.

N.C.G.S. § 109.82. The investment of funds is expanded beyond the form of investment allowed by the State Treasurer to include investment in corporate bonds with an A+ rating.

Session Law 2013-157 (amending and restating the North Carolina Limited Liability Company Act) | Chapter 57D of the North Carolina General Statutes contains the restated North Carolina Limited Liability Company Act.

Session Law 2013-198 (modernizing provisions relating to children born out of wedlock) | N.C.G.S. § 29-19. The existing requirements for a child born out of wedlock to inherit from the child's father are expanded to also allow a child born out of wedlock to inherit from such child's father if the father died within one year of the child's birth and who is established to be the father by DNA testing.

Session Law 2013-316 (simplifying North Carolina tax structure including elimination of North Carolina estate tax).

Session Law 2013-378 (clarifying notice requirements and creditor status relating to Department of Health and Human Services, Division of Medical Assistance (Medicaid)) | N.C.G.S. § 108A-70.5(b)(2). DHHS has all rights as an estate creditor, including the right to be appointed as collector.

N.C.G.S. § 28A-14-1(b). This provision requires that a copy of notice to creditors be delivered or mailed to DHHS if decedent was receiving medical assistance at the time of death.

N.C.G.S. § 28A-19-6(a). DHHS is a 6th class creditor for purposes of determining claims against an estate.

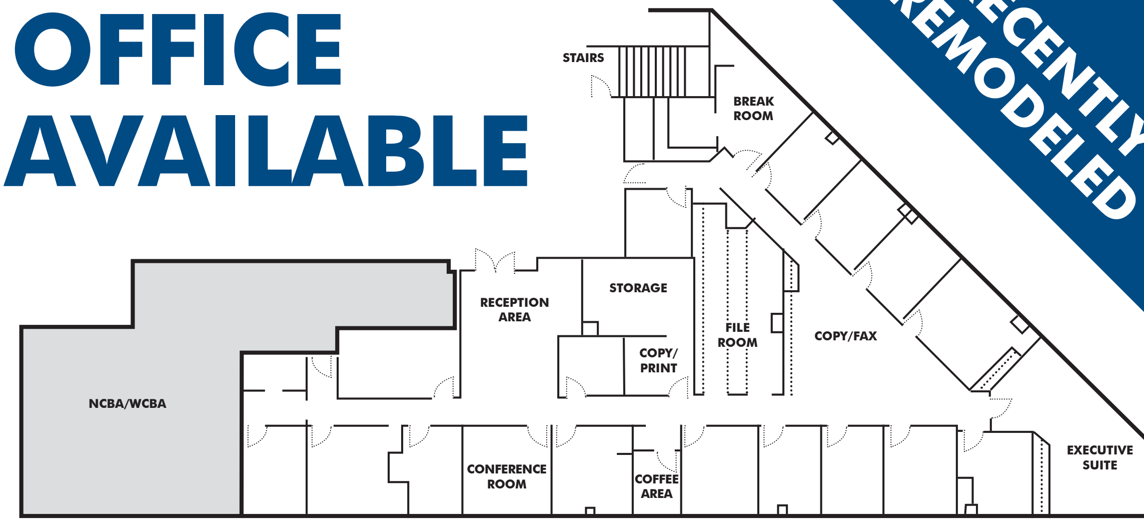
N.C.G.S. § 36C-8-818. The trustee of a revocable trust established by a person who is receiving medical assistance (to the trustee's knowledge) at time of death is required to provide notice to DHHS within 90 days of such person's death. •

Mr. and Mrs. Cella are shareholders of Manning, Fulton & Skinner, P.A., Raleigh, N.C.

RECENTLY REMODELED

PRIME OFFICE SPACE AVAILABLE

Private Upper Level Space with Executive Suite



THE N.C. BAR CENTER ON LAKE CRABTREE

8000 Weston Parkway, Cary (27513) between Harrison & Evans

Space Available | Flexible Lease Options to over 6,400 sq/ft.

Perfectly Suited Location for Legal Professionals and Law-Related Enterprises serving the Legal Community
Acclaimed Class-A Business Facility Replacing Major Tenant



- **Suites, Window Offices**
- Superb Amenities
- Conference Facilities
- **Private Conference Room**
- Storage and Work Space
- Break Room With Kitchen
- Keyless Entry Security System
- Computerized Energy Management
- **Luxurious Reception Area**
- Parking (4 spaces per 1,000 rentable sq/ft)

Contact Tom Purdy (*barcenter@ncbar.org*) or 1.800.662.7407
Additional information available at ***www.ncbar.org/barCenterSpace***

Home of the North Carolina Bar Association and NCBA Foundation, Lawyers Insurance Agency,
Wake County Bar Association and 10th Judicial District Bar

NORTH CAROLINA BAR ASSOCIATION
SEEKING LIBERTY & JUSTICE
North Carolina Bar Association
P.O. Box 3688 | Cary, NC 27519-3688

Nonprofit Org.
U.S. Postage
PAID
Raleigh, N.C.
Permit #297

Thank you for joining us!

Is there something you would like to see in the next newsletter? Let us know!

NCBA

Contact The NCBA

Call toll-free 1.800.662.7407
Email ***newsletter@ncbar.org***
Visit us at ***www.ncbar.org***