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Proposals for Revising Georgia's Probate Code

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Georgia Probate Notes

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A Message from the Publisher and Editor of *Georgia Probate Notes*

Dear Readers,

As we have on previous occasions, *Georgia Probate Notes* is joining with the Fiduciary Section of the State Bar of Georgia to publish this joint September/October, 2006 newsletter for the benefit of Georgia probate judges and Fiduciary Section members. The Chair of the Fiduciary Section, Alan Rothchild, and the Co-Chairs of the Section's Communications Committee, Richard Barnes and Ed Manigault, are to be congratulated on securing timely and interesting articles from Professor Mary Radford, Nick Djuric, and Ralph Morrison for this issue.

The production of this joint newsletter is made with the hope that fiduciary practitioners and probate court judges will become familiar with the problems faced by and aspirations of each group in doing its part in administering the law and by this understanding benefit the citizens of Georgia.

Marion Guess

GEORGIA PROBATE NOTES
MARION GUESS, PUBLISHER AND EDITOR

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Georgia Law Amended to Protect Cash Value of Life Insurance and Annuities from Creditors

Jeffrey M. Zitron
Menden, Freiman & Zitron, LLP

O.C.G.A. Sections 33-25-11 and 33-28-7 were amended effective May 5, 2006 to provide protection from creditors for the cash surrender value and proceeds of life insurance policies and annuity contracts. Advisors should be aware that the amendments do **not** provide blanket protection; rather, they provide some clarification, and in some instances confusion, over what is, and what is not, protected from creditors.

Life Insurance Proceeds Protected: When a Georgia resident dies leaving insurance on his or her life payable to a third party beneficiary, the proceeds are exempt from the claims of creditors of the insured. However, if the insurance proceeds are paid to the insured or the insured's estate, such proceeds will be subject to the claims of creditors of the estate.

Planning Recommendation: A client with creditor concerns should not designate him/herself or his/her estate as the beneficiary of life insurance. Such clients should review beneficiary designations on life insurance policies to assure that they have properly named primary and contingent beneficiaries to avoid creditor claims upon death. Typically, the default beneficiary under a life insurance policy in the absence of a named beneficiary is the estate of the insured, so beneficiary designations should not be left blank if creditor protection is an important objective.

That said, it will nonetheless remain common planning for an insured to name his or her estate as the beneficiary of a life insurance policy where there are no creditor concerns because, in many cases, this is the most effective way to implement a more sophisticated dispositive plan through the provisions of the insured's Last Will and Testament. In other cases, where it is not appropriate to name the estate as a beneficiary due to creditor concerns, but where a sophisticated dispositive plan is desired, it is often the best practice to form a trust, with the trustee named as owner and beneficiary of the policy. Again, be aware that the amendment to the law is not so much a change in Georgia law, as it is a clarification of the existing state of affairs.

Another planning consideration is that life insurance proceeds payable to a beneficiary with creditor problems will be subject to claims of the beneficiary's creditors. New O.C.G.A. Section 33-25-11(a) only protects proceeds from creditors of the insured. There is no protection afforded beneficiaries from their own creditors. Accordingly, where it is desirable to

protect insurance proceeds from a beneficiary's creditors, or for that matter, to protect the proceeds from the beneficiary's own improvident spending habits or where the receipt of insurance proceeds might disqualify the beneficiary from receiving needs based government assistance (such as Medicaid), it is best practice to establish a discretionary, spendthrift trust or "special needs" type trust to hold and administer life insurance proceeds for the benefit of such a beneficiary.

Georgia's bankruptcy exemptions provide limited protection of life insurance proceeds received by a debtor who was a dependent of the insured, but only to the extent "reasonably necessary for the support of the debtor and any dependent of the debtor." This exemption applies in bankruptcy as well as to intestate, insolvent estates where there is a living widow or child of the intestate. Unfortunately, to take advantage of this exemption, the debtor must be in bankruptcy or the beneficiary of an insolvent estate. This bankruptcy exemption was not affected by the new law however, given the minimal amount of planning required to establish a discretionary, spendthrift trust and the ability to protect 100% of the proceeds of a life insurance policy from creditors, most of our clients elect to take advantage of this type of planning.

Life Insurance – Cash Value Protected: Subparagraph (c) of the newly amended Section 33-25-11 provides that the cash surrender value of a life insurance policy is not liable to attachment or garnishment by any creditor of the insured. This codifies Georgia case law set forth in Farmers' and Merchants' Bank vs. National Life Insurance Company, et al., 131 S.E. 902 (1926). Yes, that's right, Georgia case law going back to 1926 apparently protected the cash surrender value of a life insurance policy from garnishment by a creditor of the insured.

While it is nice to know that Georgia now has a statute which specifically protects the cash surrender values of life insurance policies from creditors, be aware that there are exceptions. For example, if it can be shown that the purchase of the policy was made with the intent to defraud creditors, the Georgia statute will not protect the cash surrender value. Interestingly, the statute refers to "the purchase, sale, or transfer of the policy…" but does not refer specifically to the payment of premiums on the policy subsequent to the initial purchase. Could this be a loophole that would allow a person with an otherwise legitimate life insurance policy to subsequently make premium payments to increase the cash value for the purposes of defrauding creditors? Probably not, but it remains to be seen what a debtor might do to protect assets.

Bankruptcy Exception: Cash Value Protected…Not!: A more significant problem with the protection provided by the revised statute is that in bankruptcy, Georgia only protects the first $2,000 of cash surrender value of any unmatured life insurance contract owned by the debtor. That's right, while the cash surrender values of life insurance policies have unlimited protection from garden variety creditors outside of bankruptcy, only a meager $2,000 of cash value is exempt if the debtor is in bankruptcy. So, you might ask, why would the statute have been amended in a way that produces such a strange result? Well, the amendment (which does not apply in bankruptcy) was adapted from Florida Statute 222.14 which grants blanket creditor protection to life insurance cash surrender values, both in and out of bankruptcy. Georgia, unlike Florida, has two completely different sets of exemptions, one set that applies for debtors

who are in bankruptcy, and another set that applies for debtors who have not filed bankruptcy. If the Georgia legislature intends to protect life insurance cash values from creditor claims, a further amendment to our bankruptcy exemption statute, O.C.G.A. Section 44-13-100 (a)(9), will be required. Stay tuned for further developments.

Annuities and Creditor Protection: O.C.G.A. Section 33-28-7 was amended to read as follows:

> The *proceeds* of annuity, reversionary annuity, or pure endowment contracts issued to citizens or residents of this state, *upon whatever form*, shall not in any case be liable to attachment, garnishment, or legal process in favor of any creditor of the person who is the *beneficiary* of such annuity contract unless the annuity contract was assigned to or was effected for the benefit of such creditor or unless the purchase, sale, or transfer of the policy is made with the intent to defraud creditors. (*Emphasis added.)*

A quick reading of the new statute seems to reflect broad creditor protection for annuities. It protects proceeds of annuities "…upon whatever form…."

Planning Considerations with Annuity Payments: Georgia, like most states, does not allow a person to create an asset protection trust for him/herself; however, perhaps the Georgia legislature has opened a door for estate planners to accomplish significant asset protection with planning strategies that involve annuity payments. For example, significant asset protection may now be available through common estate planning techniques such as GRATs (grantor retained annuity trusts), CRATs (charitable remainder annuity trusts) or even private annuities. Each of these planning strategies involves converting otherwise unprotected assets into a stream of annuity payments that may now, incidentally, be protected from creditors.

Unfortunately, the new statute raises as many questions as it answers. First of all, the statute protects the "proceeds" of an annuity. Does this mean the statute also protects the cash value of the annuity, or just the annuity payments? Second, the annuity statute protects the proceeds of an annuity from any creditor of the "beneficiary." So what does that mean with respect to claims filed by creditors of the annuity owner?

Let's turn again to the source of the confusion. The new annuity statute, like the insurance statute discussed above, was adapted from Florida Statute 222.14. However, our new annuity statute has neither the same language nor the legislative history of the Florida Statute. The Florida Statute reads as follows:

> *Exemption of cash surrender value of life insurance policies and annuity contracts from legal process.* – The cash surrender values of life insurance policies issued upon the lives of citizens or residents of the state and the proceeds of annuity contracts issued to citizens or residents of the state, upon whatever form, shall not in any case be liable to attachment, garnishment or legal process in favor of any creditor of the person whose life is so insured or of

> any creditor of the person who is the beneficiary of such annuity contract unless the insurance policy or annuity contract was effected for the benefit of such creditor.

Is the cash surrender value of an annuity protected? First, (for what it's worth) the heading of the Florida statute tells us it is creating an exemption for cash surrender values. Second, 222.14 was initially enacted in 1925 and only protected life insurance cash values; however, in 1978 it was amended to protect "proceeds of annuity contracts" as well. The new words "proceeds of annuity contracts" were added to the statute in 1978 with the intention of protecting both cash values of annuities as well as the proceeds; however, as a result of poor drafting, it was not clear whether the term "proceeds" was intended to exclude the cash value of an annuity from protection. This change created confusion in the Florida courts, which was ultimately resolved in 2001 in the case of Goldenberg v. Sawczak, 791 So. 2d 1078. Here, the Florida Supreme Court ruled that the reference to "proceeds of annuity contracts...upon whatever form..." included the protection of the cash surrender values. The decision was based in part on Florida's long standing policy favoring liberally construed exemptions.

So what result should we expect in Georgia?

First, Georgia does not have a longstanding policy favoring liberally construed exemptions. Second, unlike the Florida statute, there is no mention of the term "cash surrender value" in the Georgia annuity statute. Even if we ignore the Florida statute and focus solely on the new Georgia legislation, the new life insurance statute contains separate paragraphs dealing individually and expressly with proceeds and cash values; whereas, the new annuity statute is but a single sentence referring only to the protection of "proceeds." If cash values of annuities were meant to be protected in Georgia, why doesn't the statute just come right out and say that?

The Florida Supreme Court had no problem concluding that the words "upon whatever form…" modify the term "proceeds" and deciding that the cash value of an annuity was simply the form of proceeds resulting upon surrender of the annuity. A Georgia court might just as likely reach a contrary conclusion; that "upon whatever form" in the Georgia statute does not describe the "proceeds," but refers instead to the variety of annuity arrangements the proceeds of which would be granted protection. Consequently, absent an amendment to the statute or a ruling by the Georgia courts, we cannot be certain that the cash values of annuities are protected from creditor claims.

Who is protected and from whom is he/she protected? The new annuity statute protects the proceeds of an annuity from any creditor of "the person who is the beneficiary of such annuity contract." This seems simple enough; however the statute does not address two (2) critical issues.

First, the new annuity statute is silent about claims filed by creditors of the annuity owner; it only speaks of creditors of the beneficiary. If the annuity owner has creditors, those creditors should be able to garnish the annuity proceeds payable to the owner (unless the owner is considered the beneficiary); and after the owner's death, the owner's creditors should be able

to attach the remaining proceeds before they can be paid to a third party beneficiary. Why? Because the new statute does not protect beneficiaries from creditors of the owner. The new statute only protects the beneficiaries from claims by their own creditors.

The new annuity statute is also ambiguous as to whether the annuity owner is or may be considered the annuity beneficiary for purposes of deriving protection from his/her own creditors. In a vacuum, it is obvious that an annuity owner is always the beneficiary of an annuity as long as he/she is living; and therefore ought to receive protection from his or her own creditors. However, juxtaposed against the former annuity statute, it is not clear whether the new annuity statute was intended to protect the owner of the annuity from his or her own creditors. The old annuity statute expressly protected proceeds of an annuity from creditors of the annuity owner, only when the proceeds were payable to a person "other than the person effecting the contract or his executors or administrators." Under the old annuity statute, the annuity owner was not protected from his/her own creditors. Similarly, the old and new life insurance statute make a distinction between the result when life insurance proceeds are payable to a third party beneficiary or the insured's estate, and only protect life insurance proceeds payable to third party beneficiaries.

If this is a matter of terminology, and the annuity owner is never considered the "beneficiary" of the annuity contract, then proceeds paid to the annuity owner are not protected by this statute. On the other hand, if the annuity owner is by definition considered the "beneficiary" during his or her lifetime, then the new statute provides blanket protection of annuity "proceeds" payable to annuity owners. This interpretation has an anomalous consequence, however, in that proceeds payable to a third party beneficiary are exposed to claims by creditors of the original annuity owner. Remember, the annuity statute protects the proceeds of an annuity from any creditor of the "beneficiary," and does not protect the proceeds from creditors of the owner.

It remains for the Georgia legislature and/or courts to revisit the new statute to provide clarity on the extent of creditor protection afforded annuities.

<u>Annuities – Additional Considerations</u>: Paralleling the new life insurance statute, the annuity statute provides that annuity proceeds will not be protected if the annuity was purchased, sold or transferred with the intent to defraud creditors. Additions to cash value beyond the initial purchase of the annuity with intent to defraud creditors (essentially converting non-exempt assets into potentially exempt assets) is not addressed within the statute but likely will not pass the gauntlet of Georgia's fraudulent transfer laws.

Also, Georgia's bankruptcy exemption statute, O.C.G.A. Section 44-13-100 (a)(1)(E), provides that annuity payments receive protection only if "on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor…." The bankruptcy statute provides limited protection for annuity "payments" but provides no protection whatsoever for the cash value of annuities. Thus, if Georgia intends to bestow Florida style asset protection on annuities, it may be necessary to amend the Georgia bankruptcy statute to accomplish this.

Conclusion**:** While the amendments passed in House Bill 1304 appear to be a step in the direction of providing creditor protection for life insurance and annuities products, many questions remain. Our recommendation as we await further guidance is for clients to carefully review how life insurance and annuities are held, that is how they are titled, and carefully reconsider their beneficiary designations.

Probate Court Determination of Caveat to Petition to Terminate Temporary Guardianship

The following order was entered in the Bibb County Probate Court pursuant to O.C.G.A. §29-2-8(b) which permits the Probate Court to hear a temporary guardian's objections to the termination of a temporary guardianship. *Georgia Probate Notes* is grateful to Judge Bill Self for permission to print his order.

IN THE PROBATE COURT OF BIBB COUNTY
STATE OF GEORGIA

IN RE:	:	DOCKET NO. 04PV33286
HAYDEN ALEXANDER SHARP,	:	
Minor	:	PETITION TO TERMINATE
CHRISTOPHER WAYNE SHARP,	:	TEMPORARY
Temporary Guardian	:	GUARDIANSHIP

FINAL ORDER

On July 26, 2004, this Court appointed Christopher Wayne Sharp, the biological father of the minor, as Temporary Guardian of Hayden Alexander Sharp.

On December 12, 2005, Jennifer Shelly, now known as Jennifer Garner, the natural mother of the minor, filed her Petition to Terminate Temporary Guardianship. Service of such Petition was made upon the Temporary Guardian, and, on January 6, 2006, the Temporary Guardian filed his Caveat to the Petition to Terminate.

The matter was scheduled for hearing before this Court on February 20, 2006. Following an Order of Continuance, the matter was rescheduled for hearing on this date. The Petitioner was present and was represented by David J. Studdard. The Temporary Guardian was present and was represented by Ann E. Parman.

After consideration of the evidence presented and the argument of counsel, the Court makes the following:

Findings of Fact

1. Hayden Alexander Sharp was born on October 31, 2003. His mother is Jennifer Shelley, and his father is Christopher Wayne Sharp. The father was present at the time of the birth, his name appears on the birth certificate as the father of the child, and he testified that he signed the original birth record. The mother of the child acknowledges fully that Christopher Wayne Sharp is the father of the child.

2. At some point in time, the mother voluntarily surrendered physical custody of the child to the father, Christopher Wayne Sharp, acknowledging her own then inability to properly care for the child. The child has resided with the father continuously since May, 2004, when he was six to seven months of age. His visitation with and personal interactions with the mother during the time since May, 2004 has been minimal and sporadic.

3. The mother, Jennifer Shelley Garner, was incarcerated at some point in time on a charge of credit card theft and subsequently entered a drug treatment program and the Job Corps. She has subsequently remarried and has had another child, now 3 months of age. She testified that she has been drug-free for approximately 18 months.

4. The father has filed a petition to legitimate the child and for custody in the Superior Court of Fayette County [2006V0248H]. The father testified that he had been under the impression that he was not required to file for legitimation, since he had signed the child's birth records with the knowledge and consent of the mother.

5. The father, too, has remarried and now has another child approximately one year old.

6. Prior to a dispute between the parents, the father had permitted the father and step-mother of the child's mother to visit regularly with the child. After the dispute, he ceased allowing the grandparents to visit because he did not want them to allow the mother to visit the child without his permission.

Upon such facts, the Court makes the following:

Conclusions of Law

A. As the acknowledged biological father of the minor and the person with whom the child has lived most of his 28 months of life, the father has certain rights which should be recognized even though the minor was born out of wedlock.

B. The parental rights of the mother of the minor have not been terminated by any court, and she, too, has rights which should be recognized.

C. The matter of the permanent custody of the minor, the rights of the non-custodial parent, and the respective obligations of the parents to the support of the minor must be heard in a court of competent jurisdiction.

D. It would not, however, be in the best interest of the minor involved in these proceedings to terminate the temporary guardianship and send the child to live with his mother, with whom he has had so little involvement during his 28 months of life, and a step-father essentially unknown to the child. It would be in the best interest of the minor for this temporary guardianship to remain of full force and effect until the matter of custody and visitation rights can be determined by the Superior Court of Fayette County.

E. It would further be in the best interest of the minor involved in these proceedings for this Court to establish and provide for certain visitation rights for the mother of the child, pending an order of the Superior Court of Fayette County addressing the issue.

WHEREUPON, IT IS CONSIDERED, ORDERED AND ADJUDGED as follows:

I. The temporary guardianship of Hayden Alexander Sharp granted by this Court on July 26, 2004 to Christopher Wayne Sharp shall continue of full force and effect until terminated by an award of custody of the minor by the Superior Court of Fayette County or until further order of this Court.

II. Until the matter has been addressed by the Superior Court of Fayette County, the mother, Jennifer Shelley Garner, shall be entitled to have the minor child visit with her at the following times and under the following circumstances:

a. At any and all times which may be mutually agreed upon by the parents;

b. During every other weekend, from 6:00 PM on Friday until 4:00 PM on Sunday, beginning on March 24, 2006;

c. From 9:00 AM until 6:00 PM on Sunday, March 14, 2006 (Mother's Day);

d. It shall be the obligation of the mother to pick up the child at and return the child to the residence of the father, or such other place as may be mutually agreed upon, at the beginning and end of each visitation;

e. It shall be the obligation of the father to have the child ready and prepared to accompany the mother for each such visitation, with adequate and proper clothing for the visitation period; and it shall be the obligation of the mother to return all clothing and any other items brought by the child to the father at the end of each visitation; and

f. Each parent shall refrain from making any derogatory remarks about the other parent in the presence of the minor child.

SO ORDERED on March 13, 2006.

_____

WILLIAM J. SELF, II, JUDGE
PROBATE COURT OF BIBB COUNTY

STATE BAR OF GEORGIA
FIDUCIARY LAW SECTION

A Message from the Chair of the Fiduciary Law Section

The Fiduciary Law Section is pleased to again co-sponsor this issue of *Georgia Probate Notes*. We hope you find the articles related to Georgia's Probate Courts and those authored by our Section volunteers to be of interest and helpful in your practice.

Mark Williamson, Secretary/Treasurer of the Fiduciary Law Section, is hard at work on the 2007 Estate Planning Institute in Athens on February 9-10, 2007. Planning for the 2007 Fiduciary Law Institute at the King and Prince on St. Simons Island (July 12-14, 2007) has also begun under the leadership of Chair-Elect Adam Gaslowitz. I hope you will put both of these seminars on your calendar.

Finally, I join Judge Guess in thanking Richard Barnes and Ed Manigault for their efforts in publishing this joint newsletter and for their work on our Section's website. I encourage you to visit this website regularly for updated information through the State Bar of Georgia's homepage (www.gabar.org.).

Alan F. Rothschild, Jr.

Georgia Advance Directive for Health Care Roundtable

By Nikola R. Djuric
Sutherland Asbill & Brennan LLP
Chairman, Legislation Committee
Fiduciary Law Section

During the 2006 session of the Georgia General Assembly, there were a few legislative efforts to revise the statutory form living will, primarily to fix the confusing language relating to nutrition and hydration. One bill passed, but it had a technical flaw and was vetoed by Governor Perdue at the request of its sponsor. After the session, the Fiduciary Law Section's Legislation Committee agreed to work with Georgia State Representative R. Steve "Thunder"

Tumlin, Jr. to review the statutory form Living Will and Durable Power of Attorney for Health Care and draft revised forms for introduction in the 2007 session of the General Assembly.

On June 5, 2006, Rep. Tumlin convened a roundtable of persons interested in Georgia's law on advance directives for health care. The meeting was arranged by Professors Charity Scott and Mary Radford at Georgia State University. The roundtable was co-chaired by Kathy Kinlaw, M.Div., Acting Director, Center of Ethics, Emory University, and me (in my capacity as chairman of the Legislation Committee).

The membership of the roundtable was expanded throughout the summer and met nearly every week from June 5 to September 12. The following persons participated in one or more meetings of the roundtable:

William H. Boling, Jr.
Powell Goldstein LLP
Health Law Section, State Bar of Georgia

Sylvia B. Caley
Director, Health Law Partnership
Georgia State University College of Law

Richard W. Cohen, M.D.
Resurgens Orthopaedics

Victoria L. Collier
The Elder & Disability Law Firm of
Victoria L. Collier PC

Elizabeth B. Connell, M.D.
Professor Emeritus, Dept. of Gyn/Ob
Emory School of Medicine

Becky Kurtz
State Long Term Care Ombudsman

Lisa A. D'Agostino,
Associate General Counsel
Office of the General Counsel
Emory University

Kevin Harris
Georgia Right to Life

Robert M. Keenan, III
King & Spalding LLP
Georgia Academy of Healthcare Attorneys

N. Wallace Kelleman
Kelleman Law Firm P.C.

Knob Knobel
Pres., Memorial Society of Georgia
Legislative Director, Compassion & Choices

Ruthann P. Lacey
Ruthann P. Lacey, P.C.

Brian W. Looby
Associate General Counsel
Medical Association of Georgia

Melanie S. McNeil
Executive Director
Georgia Council on Aging

Francis J. (Frank) Mulcahy, Jr.
Tinsley Bacon Tinsley, L.L.C.
Executive Director
Georgia Catholic Conference

Joshua H. Norris
Director of Legal Advocacy
Georgia Advocacy Office

Mary Margaret Oliver
Georgia State Representative

Donald J. Palmisano
General Counsel
Medical Association of Georgia

Mary F. Radford
Professor of Law
Georgia State University College of Law

Jerri Nims Rooker, Assistant Director
Center for Law, Health & Society
Georgia State University College of Law

Deanna O. Richardson
Director, Palliative Care Service, Piedmont Hospital

Charity Scott
Professor of Law
Director, Center for Law, Health & Society
Georgia State University College of Law

Temple Sellers
Vice President, Legal Services
Georgia Hospital Association

Jill A. Travis
Deputy Legislative Counsel
Georgia General Assembly

R. Steve "Thunder" Tumlin, Jr.
Smith, Eubanks, Smith & Tumlin, PC
Georgia State Representative

Beverly A. Tyler
Executive Director
Georgia Health Decisions
Research Associate
Georgia Health Policy Center

Teresa Warren
Hospice of Northeast Georgia Medical Center

Thomas H. Vann, Jr., Esq.
Alexander & Vann, LLP

The members of the roundtable discussed how Georgia's current statutes and statutory forms are viewed by patients, physicians, nurses, patient advocates, hospital lawyers, estate planning lawyers, and the general public, and discussed a whole range of medical, legal, religious, ethical, and practical issues relating to the forms and end-of-life decisions. It is impossible to exaggerate how important it has been for us to hear the views of so many individuals whose perspectives on the current statutory forms are so different. There are significant problems being confronted every day by patient advocates and hospital lawyers, for example, that would never occur to a lawyer who drafts and supervises the execution of these forms as part of the estate planning process.

We also examined forms produced by private groups (especially the The Critical Conditions Planning Guide from Georgia Health Decisions), the Uniform Health-Care Decisions Act, recent legislation in New Jersey and Maryland, and many other sources.

One of the roundtable's earliest decisions was to combine the living will and the power of attorney for health care into a single form that we have called the Georgia Advance Directive for Health Care. We quickly realized how difficult it would be to create a statutory form that was suitable in every situation. Nevertheless, that is what many expect a statutory form to be. Throughout the process, the roundtable participants tried to balance the often competing requirements of clarity, technical correctness, simplicity, comprehensiveness, and brevity.

The roundtable was also very sensitive to the potential political consequences of making changes to the substantive provisions of current law that reflect a decision by the Georgia General Assembly on difficult questions of public policy.

Work on a draft form was completed in mid-September. Work on the necessary amendments to the statutes is ongoing. In October, the draft form (and, when ready, the draft bill) will be studied by the Legislation Committee and introduced to other interested individuals and groups. The roundtable's goal remains to present sponsoring lawmakers with a bill that can be introduced in the 2007 session of the Georgia General Assembly.

Proposals for Revising Georgia's Trust Code

Mary F. Radford
Professor of Law
Georgia State University College of Law

The Trust Code Revision Committee of the Fiduciary Law Section of the State Bar of Georgia is in the process of reviewing and revising Chapter 12 of Title 53 of the Georgia Code, the "Georgia Trust Code". It is expected that the revisions will be presented to the Fiduciary Section and the State Bar Board of Governors in late summer, 2007, for introduction to the Georgia General Assembly in January, 2008. The Trust Code Revision Committee has been examining the current Georgia trust law in monthly meetings since July, 2003. The Committee is chaired by William Linkous (Atlanta) and Professor Mary Radford (Georgia State University College of Law) serves as the Reporter. Committee members are: Julian Friedman (Savannah), Greg Fullerton (Albany), Tom Jones (Atlanta), David Laney (Columbus), Faryl Moss (Atlanta), Albert Reichert (Macon), Ann Salo (Atlanta), John Spears (Decatur), and Rees Sumerford (Brunswick).

Some may ask why Georgia's fairly modern Trust Code is in need of updating. Georgia's current trust code, the "Georgia Trust Act" (Chapter 12 of Title 53) was enacted in 1990 after extensive study of Georgia trust law by the first Georgia Trust Code Revision Committee of the Fiduciary Law Section of the State Bar of Georgia. Since that time, however, two important developments have occurred. First, the American Law Institute promulgated the Restatement (Third) Trusts in 1996. Second, the Uniform Trust Code of 2000 (the "UTC") has been approved by the National Conference of Commissioners on Uniform State Laws. Georgia was one of the few states that had codified its trust law prior to the drafting of the UTC. In fact, the Georgia Trust Act of 1990 was one of the models used by the drafters of the UTC, as were the trust codes of California, Indiana, Texas, and Washington. As of July, 2006, the Uniform Trust Code has been adopted by Alabama, Arkansas, District of Columbia, Florida, Kansas, Maine, Missouri, Nebraska, New Hampshire, New Mexico, North Carolina, Ohio, Oregon, Pennsylvania, South Carolina, Tennessee, Utah, Virginia, and Wyoming. The Georgia Trust Code Revision Committee thus is examining the UTC and the new Restatement to determine what portions of these promulgations would be beneficial to the state of Georgia.

The following description of revisions that are currently under consideration by the Trust Code Revision Committee reflects preliminary decisions, all of which are subject to change. The Committee welcomes comments and suggestions from members of the State Bar of Georgia.

A. Governing Law

The current Georgia Trust Code contains no provisions that dictate which state's laws apply when trust matters are at issue. Under consideration is the adoption of two new provisions that are modeled after Sections 270 and 278 of the Restatement of the Conflict of Laws and UTC Sec. 107. Basically, these provisions state that the law governing the validity of the trust and the meaning and effect of trust terms will be that law that is designated by the

terms of the trust unless the effect of that designation would be contrary to public policy. In the absence of a controlling designation in the terms of the trust, the law of the jurisdiction having the most significant relationship to the matter at issue will be the controlling law.

B. Certification of Trusts

UTC Sec. 1013 and statutes in a number of other states (e.g., California, Idaho, Indiana, Nebraska, Nevada, Michigan) allow the trustee to furnish to a third party a "certification" of the trust rather than furnishing the entire trust document. The Trust Code Revision Committee will recommend a certification option for Georgia. The certification would contain relevant information such as: (1) the fact that the trust exists and the date of the trust and any amendments; (2) the identity of each settlor; (3) the identity and address of each current trustee and, if more than one, the number and identity of those required to exercise the powers of the trustee; (4) the relevant powers of the trustee and any restrictions or limitations on those powers; (5) the revocability or irrevocability of the trust; (6) how trust property should be titled; (7) except as specifically disclosed in the certification, that the transaction at issue requires no consent or action by any person other than the certifying trustee; and (8) such other information as the trustee deems appropriate. A person who acts in reliance upon the certification without knowledge that any information therein is incorrect will not be liable for so acting and may assume without inquiry that the information is correct. A person who in good faith enters into a transaction in reliance upon the certification may enforce the transaction as if the information in the certification were correct. A person who demands to see the trust instrument in addition to a certification of the trust or relevant excerpts may be liable for damages, including court costs and attorney's fees, if the court determines that the demand was not made in good faith.

C. Creation and Validity of Express Trusts

1) *Writing requirement*: The new Code will retain the requirement that an express trust be in writing and will add the requirement that the writing be signed by the settlor. Also, the Revision Committee may recommend that the current Georgia statute that allows the creation of life insurance trusts by oral agreement (OCGA Sec. 53-12-22.1) be repealed.

2) *Trust property*: The requirement that a trust have trust property will be retained. In addition, provisions will be added that require that a transfer of legal title to the property be made to the trustee and, in the case of real property, that the instrument of transfer be recorded.

3) *Beneficiary*: The Code will refine the requirement that the trust have a beneficiary by requiring that, except in the case of a charitable trust, the trust have a beneficiary who is "reasonably ascertainable" within the Rule against Perpetuities period. The Code will also provide that the requirement for a reasonably ascertainable beneficiary is "satisfied if under the trust instrument the trustee or some other person has the power to select the beneficiaries based on a standard or in the discretion of the trustee or other person." This latter section is modeled after California law.

4) *Capacity of Settlor to Create the Trust*: The UTC commentary indicates that many of the UTC provisions relating to revocable trusts revolve around the concept that people in most states use revocable trusts as will substitutes. Consequently, the UTC lowers the capacity requirement for establishing a revocable trust from the capacity to contract to the lower level of testamentary capacity. The Trust Code Revision Committee decided to retain the higher level capacity in the Georgia Code for two reasons: 1) the use of revocable living trusts as will substitutes is not as pervasive in Georgia as it is in some states; and 2) the execution of a trust does not require the protective formalities (e.g., witnesses) that are required for the execution of a will.

5) *Trustees*: The new Code will contain a provision that states that no merger of title to trust assets occurs simply because the trustee or trustees are the same person or persons as the beneficiary or beneficiaries of the trust. Also the statute will clarify that by accepting the trusteeship of a trust or otherwise acting in a fiduciary capacity in this state, a trustee submits personally to the jurisdiction of the courts of this state regarding any matter involving the trust.

6) *Trusts for Animals*: Following a trend in the UTC and many states, the new Code will allow a trust to be set up with only non-humans (pets or other animals, such as show horses) as beneficiaries. At the termination of the trust, any unused assets will be transferred as provided by the terms of the trust or the will or, if there are no such terms, to the heirs of the settlor. The trust will last through the lifetime of the animal. The trust may be enforced by a person who is identified in the trust or by someone appointed by the court.

7) *Spendthrift & Discretionary Trusts*: Georgia currently has one of the most detailed and extensive spendthrift trust statutes (OCGA Sec. 53-12-28) of any state. The substance of that statute will be retained, with some refinements, including an exception of application of the statute to special needs trusts and community trusts, which are subject to their own federal and state laws. For discretionary trusts, a provision will be added that provides that a creditor of a beneficiary may not compel the trustee to pay any amount that is payable only in the trustee's discretion regardless of whether the trustee is also a beneficiary. Just as with spendthrift trusts, this protection will not apply to the extent of the proportion of trust property attributable to the beneficiary's contribution.

8) *Uniform Testamentary Additions to Trusts Act*: The Georgia statute will be updated to reflect changes made in the 1991 revision of UTATA.

D. Implied Trusts

Georgia has detailed and extensive provisions relating to implied (resulting and constructive) trusts. As has been evidenced by recent appellate cases, these statutes seem to work well and will be retained.

E. Charitable Trusts

The current statutes relating to charitable trusts will be retained. The new Code will not adopt the provision of the UTC that allows the settlor to enforce the provisions of a charitable

trust. The provisions related to private foundations will be retained but reorganized to make them more readable.

F. Revocation, Modification, Termination of Trusts

1. *Revocation*.

a) The UTC reverses the common presumption so that a trust that is silent on the issue of revocability is presumed to be revocable by the settlor. Unlike the UTC, the Georgia statute will retain the requirement that currently exists in Georgia law that a settlor must expressly retain the power to revoke the trust in order for the trust to be revocable.

b) The new Code will clarify that a trust will not be considered to be revocable merely because the life beneficiary has a reversion in or a power of appointment over assets of the trust or because the life beneficiary's heirs or estate have a remainder interest therein.

c) The Code will add a provision that allows a settlor's agent under a power of attorney to revoke or modify the trust but only to the extent expressly authorized by the terms of the trust or the power. Also the Code will state that a settlor's powers with respect to revocation, amendment, or distribution of trust property may be exercised by the settlor's conservator only as provided in OCGA Sec. 29-5-23. This section of the Guardianship Code allows the conservator to exercise such powers only if the governing instrument allows the conservator to do so.

d) The new Code will provide that any judicial proceeding to contest the validity of a trust that was revocable at the settlor's death must be commenced within two years of the settlor's death. The Committee chose two years because that period coincides with the period beyond which a petition for Year's Support cannot be filed.

2. *Modification*.

Some controversy has arisen in connection with the UTC provision that would allow the settlor and beneficiaries of an irrevocable trust to agree among themselves to revoke or modify the trust. Some believe that this power in a settlor would constitute a sufficient amount of control to bring the value of the assets of the trust back into the settlor's gross estate for estate tax purposes under Secs. 2036 and 2038 of the Internal Revenue Code. Consequently, the UTC drafters made that provision an "optional" one and those states that did not already allow such modification procedure have not adopted that provision. Current Georgia law does not allow this modification procedure and thus the new Code will not add it. A modification of a trust that cannot be modified by its terms must be accomplished by the court. The proposed new statute would allow the court to:

1) modify the administrative terms of a trust if continuation of the trust on its existing terms would impair the trust's administration; or

2) modify the administrative or dispositive terms of a trust if, owing to circumstances not known to or anticipated by the settlor or testator, compliance with the terms of the trust would defeat or substantially impair the accomplishment of the purposes of the trust.

3) modify the trust by the appointment of an additional trustee or special fiduciary if the court considers the appointment necessary for the administration of the trust. (This last section is has no counterpart in the current Trust Act.)

The new Code would also allow the court to reform a trust if it is proved by clear and convincing evidence that the terms of the trust were affected by a mistake of fact or law. The new Code will retain the current provisions relating to division or consolidation of trusts.

3. *Termination*.

The proposals in the new Code would allow the court to approve the termination of a trust if:

1) the costs of administration are such that the continuance of the trust, the establishment of the trust if it is to be established, or the distribution from a probate estate would defeat or substantially impair the purposes of the trust;

2) the purpose of the trust has been fulfilled or become illegal or impossible of fulfillment; or

3) owing to circumstances not known to or anticipated by the settlor or testator, the continuance of the trust would defeat or substantially impair the accomplishment of the purposes of the trust.

G. Trustees' Compensation

A new compensation schedule for trustees will be added. This schedule will be used only if the trust does not contain a compensation schedule or there is no separate compensation agreement between the settlor and the trustee or the beneficiaries and the trustee. The compensation schedule is as follows:

> (1) one percent (1%) of the market value of any principal asset received upon the initial funding of the trust and at such time as additional principal assets are received; and (2) an annual fee equal to one percent (1%) of the market value of the trust assets valued as of the last day of the trust accounting year prorated based on the length of service by the trustee during that year.

This schedule applies to trustees only and has no effect on the current statutory fees for personal representatives or conservators.

H. <u>Trustees' Duties and Powers</u>

The UTC grants automatically to trustees most of the powers that are contained in current OCGA Sec. 53-12-232. Under current Georgia law, a trustee's "automatic" powers are quite limited but a settlor may incorporate the long list of powers into the trust agreement. After extensive discussion, the Committee decided to follow the UTC approach so that trustees, merely by virtue of being trustees, are automatically granted most of the powers that appear in current OCGA Sec. 53-12-232. In addition, the Code will allow these powers to be incorporated by reference. In that way, a settlor can ensure that the trustee has those powers even if the applicable law governing the trust is changed to that of another jurisdiction.

The Committee will retain the provisions contained in the 2005 "Flexible Income Bill" that allow a trustee to make adjustments between principal and income if such adjustments are necessary to ensure fair and impartial treatment of both income and remainder beneficiaries. The new Code will also retain the procedure by which a trustee may petition to convert a trust to a unitrust and will add a provision that will allow a trust to be set up as a unitrust from the outset.

The Committee examined in depth and will recommend the adoption of most of the provisions of the Uniform Principal and Income Act of 2000. The current Georgia law is based on an older version of that uniform act.

The Trust Code Revision Committee will continue its deliberations through June, 2007. Please submit any comments or recommendations you may have to Mary Radford at *mradford@gsu.edu*

The Mouse that Roared? - SunTrust v. Merritt

Ralph R. Morrison
Jones Day

Note: The case of SunTrust v. Merritt provoked criticism and incited controversy even before the Georgia Court of Appeals issued its decision. The author, head of the litigation team that successfully defended the corporate Trustee SunTrust, addresses these criticisms and argues that the case is rightly decided. The author also provides insights to the ruling in the case, as well as information not included in the Court's opinion.

SunTrust v. Merritt, 272 Ga. App. 485, 612 S.E.2d 818 (2005), *cert. denied*, in essence stands for the principle that where a Trustee administers a trust for about ten years, pays all expenses and distributes all net income as mandated by the trust instrument, and at the end of the day delivers out to the remainder beneficiaries more than the original funding amount, the Trustee has not breached its fiduciary duty and, therefore, has no liability under Georgia law for failing to make as much money as the remainder beneficiaries might have liked.

This rule of law seemed to me unremarkable, yet apart from the Namik decisions,[1] I can remember few recent Georgia fiduciary cases that generated such interest. Merritt also produced some very persistent criticism. Before there was an appellate court decision, the case was dissected at the 50th Annual Estate Planning Institute[2] in Athens in February 2005, then it was criticized in July 2005 at the Fiduciary Law Institute while the Georgia Supreme Court still had an opportunity to "do the right thing" [which in my view it did, when it ultimately denied *Certiorari* and denied reconsideration]. An earlier issue of this publication[3] featured an article criticizing the case while it was still "live" and on appeal. In addition, an *Amicus* Brief was filed with the Georgia Supreme Court in opposition to the Court of Appeals decision signed by two influential Georgia legislators (sponsors of the recently enacted "Total Return" legislation), arguing, in essence, that if Merritt stood, the legislature may have made a mistake in passing Georgia House Bill 406.

The case was also the subject of an hour-long presentation by my worthy opponent at the 51st Annual Estate Planning Institute (February 2006) in Athens, and was discussed again by two speakers at the 2006 Fiduciary Law Institute in July of this year.

Now, the case is decided and final. All appeals have been exhausted and I am free to write about it.[4] I see Merritt largely as a safe harbor for Trustees who invest within appropriate ranges under Georgia law and do not incur an actual overall dollar loss for the period from trust inception to the final payout. Had the Court held otherwise, it is hard for me to imagine limits on what manner of threats and expensive litigation our zealous plaintiffs lawyers could put Trustees through every time a trust terminates in this state.

Briefly, the Merritt facts were these: Mr. Merritt's mother (the Testatrix) left a Will dividing her estate into three equal shares for the life benefit of each of her three children: a son (William Merritt, Sr.) and two daughters. Each child was Co-Trustee of his or her respective trust and was to act jointly with the corporate Trustee on all matters, except encroachments over which the corporate Trustee had sole discretion. Each child was entitled to all net income for his or her trust; and each was eligible for encroachments only if "absolutely necessary," taking into account other income available to such child. There were no other permissible beneficiaries during each child's lifetime. The remainder beneficiaries were such child's descendants, per stirpes.

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[1] Wachovia Bank of Georgia v. Namik, 265 Ga. App. 80, 593 S.E.2d 35 (2003) (Georgia Court of Appeals reversing the trial court), Namik v. Wachovia Bank, 279 Ga. 250, 612 S.E.2d 270 (2005) (Georgia Supreme Court reversing the Court of Appeals)

[2] Barwick, Cox and McDonald, "Fiduciary Investment Issues How Does a Trustee Satisfy Its Fiduciary Duty When Deciding Investment Strategy For a Trust." Criticizing and attaching the unpublished trial court Order of March 9, 2004.

[3] Donna G. Barwick, "House Bill 406 - Georgia Flexible Income Trust Legislation," Georgia Probate Notes, Volume XXII, Number 8 (May-June 2005).

[4] Load up your buckshot and get your heckling barbs ready. My law partner, Greg Hanthorn, and I will speak on this subject in Athens at the 52nd Annual Estate Planning Institute in February 2007.

The corporate fiduciary did not act as the Executor. The Executor, a CPA family member, consulted with each of the children and, at the request of each, delivered original asset stocks "in kind" to the trusts for the Testatrix's two daughters. At the request of Mr. Merritt, however, all of the assets going to the trust for his life benefit, except for one individual issue $10,000 bond, were sold and cash was turned over to the corporate Trustee with the request and direction by both the Executor and Mr. Merritt (again, the Co-Trustee, son and sole life beneficiary) that all the cash be invested in the bank's tax-free government bond common trust fund.

Thus, with the request and approval of Mr. Merritt, virtually the entire trust was invested in a high quality tax-free bond fund. It should be noted that at the time of the trust funding Mr. Merritt was approximately 74 years old. He died about nine years later at age 83. He was a man of independent means, owned some speculative investments and held a Harvard M.B.A.. Years earlier, after the death of his first wife by whom he had three children, he remarried a very wealthy woman. He left his estate primarily to his surviving wife for her lifetime. As it happens, she died more than two years after he did, but while the case was still pending. Mr. Merritt's three children, the Plaintiffs, were the remainder beneficiaries of his estate.

In Merritt the complaint changed three times. First, Plaintiffs (Mr. Merritt's three children and thus, the grandchildren of Testatrix) claimed damages (as used in the Complaint, a term seemingly synonymous with breach) should be at least the trebling in unrealized value incurred in the two other trusts created by Testatrix for her two daughters, Mr. Merritt's sisters. This "on paper" appreciation was largely the result of a concentration of a beloved beverage company stock/original asset in the sister trusts.[5] Then, by testimony of Plaintiffs' stated expert from Alabama with a background in ERISA trust administration, the damages were said to be at least 100% of the historic S&P 500 appreciation between 1990 and 1998 (plus punitive damages, attorneys fees, disgorging Trustee fees, and so forth). The Plaintiffs' expert also offered testimony that in a case such as Merritt, it was a breach *per se* for a trust to be invested less than ninety percent (90%) in stocks.[6] Mr. Merritt's plain refusal to authorize such a mix only meant that, according to the Plaintiffs' expert, the corporate Trustee was obliged to sue its Co-Trustee, and obtain an order from the Court requiring the Trustees to make such investment changes which the Court, according to the Plaintiffs' expert, would willingly grant. Finally, in its third theory Plaintiffs argued the Trustee had a duty to the remainder beneficiaries for the principal value to "at least" keep up with inflation.

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[5] There is considerable irony in that position: In 2006, with the stock market down since 1999, other plaintiffs are now suing various corporate fiduciaries for holding stocks and stock concentrations, again even where there is no actual loss but a "paper loss" during a self-selected time period.

[6] Interestingly, it is my view that had the bank acquiesced to a Co-Trustee's request to invest 100% of the trust assets in equities, that, too, can be within the range of prudent investing, especially if the income beneficiary approved. I do not suggest that a court would likely substitute its judgment for Trustees who are in agreement -- facts might allow either an all stocks or even an all bonds trust investment to not be a breach, under particular facts and circumstances.

Much of the critics' concerns for this case dealt with how the holding in Merritt might impact the new Total Return statute. But the new statute was never law applicable to the Merritt Trustee. Defending SunTrust was based on an unremarkable approach – we sought to: (i) identify the duties of the Trustees; (ii) determine which duties ran to whom; and then (iii) determine whether there was a breach under the Merritt facts.

Notwithstanding what the Restatement 3d says about inflation, inflation is not an enumerated factor in Georgia's Prudent Person Rule. It is a stated factor in the Uniform Prudent Investor Act. Restatement 3d was not even published until four years after the Georgia Prudent Person Rule was enacted although drafts were available. Merritt found, under its facts, the failure to keep up with inflation was not a breach of fiduciary duty.

Merritt does not stand for the proposition that Trustees are insurers, but I believe it does provide a safe harbor for Trustees under similar facts who, where there is no actual dollar-in dollar-out loss and certainly where the investments are made at the request of the Co-Trustee, the corporate Trustee (against whom there was no evidence whatsoever of self-dealing, self-enrichment or feathering its own nest in some way) will not be liable for hoped for gains. Further, Merritt reaffirms a well established practice among Trustees -- unless the governing instrument evidences a contrary intent, a trust is presumed to exist first, primarily, for the generation closest to the grantor. Mr. Merritt was the primary beneficiary of his mother's trust. She made him a Co-Trustee, she gave him the exclusive right to all net income for his life and she allowed, in albeit a tight-fisted way, encroachments for him, and him alone, during his lifetime. Her intention seems clear. Yes, Trustees are to balance and consider the rights of the remainder beneficiaries, but at least in cases such as Merritt, the Trustee performed its duties to all beneficiaries.[7]

A final aside, one of the odder features of the case was if anyone had been unjustly enriched it was decedent's son, Mr. Merritt, based on the argument that he got "too much" income. We argued and prevailed on our Rule 19 Motion to compel the addition of a necessary party and the Plaintiffs were ordered to bring in their own father's estate as an involuntary party defendant. They did so. Mr. Merritt died a resident of Florida. Plaintiffs brought suit over a year after Mr. Merritt died. By that time his estate was in administration and the creditors period had run. As many of us know, the close of Florida's creditor period is normally an absolute bar to further claims. After winning its Rule 19 motion, SunTrust, therefore, had to bring a separate petition in the Florida Probate Court to reopen the claims period for Mr. Merritt's estate. That action was contested and, after a hearing, the Florida Court did re-open the claims period for SunTrust. I found it surprising that even after that, the case continued. We would have argued, had liability been found, that recovery should have been from Mr. Merritt's estate, of which the Plaintiffs were the sole remainder beneficiaries. In any event Merritt did conclude as a fully litigated case with happy and I believe proper results for both Georgia fiduciaries and trust beneficiaries.

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[7] Merritt, at p. 490 cites approvingly an Arizona case: "the Trustees' duty was to invest in such a manner as to produce an income for [the lifetime beneficiary] and, secondarily [to] preserve the principal", [Tovrea v. Nolan, 875 P.2d 144 (Ariz. App. 1993)].

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