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Addressing the Estate Planning Needs of Modern-Day Clients

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Presents

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By:

Charles A. Redd

CHARLES A. REDD, PARTNER
STINSON LLP
7700 FORSYTH BOULEVARD
SUITE 1100
ST. LOUIS, MISSOURI 63105-1821
(314) 259-4534 - TELEPHONE
(314) 259-3952 - FACSIMILE
charles.redd@stinson.com

www.stinson.com

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Charles A. Redd

Charles A. Redd is a partner in the St. Louis, Missouri, office of the law firm of Stinson LLP. Mr. Redd concentrates his practice in estate planning, estate and trust administration and estate and trust-related litigation. Prior to joining Stinson, Mr. Redd was a partner in and Vice Chairman of the Trusts & Estates Practice Group at the law firm of SNR Denton US LLP (now Dentons US LLP). Mr. Redd was also previously a partner in the law firm of Armstrong, Teasdale, Schlafly & Davis (now Armstrong Teasdale LLP) and was Chairman of that firm's Trusts & Estates Department. He was previously employed as a Trust Administrator by First Wisconsin Trust Company (now U.S. Bank, N.A.), Milwaukee, Wisconsin, and as an Assistant Counsel by Centerre Trust Company of St. Louis (now Bank of America Private Bank).

Mr. Redd has extensive experience and expertise in: (a) the drafting of wills, trust instruments, durable powers of attorney, marital agreements and other estate planning documents; (b) pre- and post-death tax planning for individuals, trusts and estates; (c) preparation and filing of estate tax returns, gift tax returns and fiduciary income tax returns; (d) representation and filing of estate tax returns, gift tax returns and fiduciary income tax returns; (e) representation of individual and corporate fiduciaries and (f) litigation in the Probate Division and other equity divisions of the Circuit Court. Mr. Redd has worked on estates and estate planning projects, some involving assets valued at over a billion dollars, and has successfully handled numerous estate tax, gift tax and generation-skipping transfer tax matters, will and trust construction cases, will contests, contests of trust agreements, alleged breach of fiduciary duty cases and other types of cases involving estates and trusts.

Mr. Redd is a member of the State Bar of Wisconsin, The Missouri Bar, the Illinois State Bar Association, The Bar Association of Metropolitan St. Louis and the Estate Planning Council of St. Louis.

Mr. Redd was Chairman of the Missouri Bar's Health Care Durable Power of Attorney Subcommittee, and he played a significant role in the drafting and enactment of the Missouri Durable Power of Attorney for Health Care Act. In 1991, Mr. Redd received The Missouri Bar President's Award. Mr. Redd was the principal draftsman of the Missouri Family Trust Company Act.

Mr. Redd is an elected member of The American Law Institute and a Fellow of The American College of Trust and Estate Counsel (Past Missouri State Chair; Past Regent; Past Chair of Communications Committee; Estate and Gift Tax Committee; and Fiduciary Litigation Committee). He was an adjunct professor of law (Estate Planning) at Northwestern University School of Law for fifteen years. He serves as a member of the Advisory Committee for the Heckerling Institute on Estate Planning and is Co-Chair of the Editorial Advisory Board of, and writes a regular column in, Trusts & Estates magazine. In 2018, he was inducted into the Estate Planning Hall of Fame® by the National Association of Estate Planners and Councils. In 2023, he was recognized by the Estate Planning Council of St. Louis as Distinguished Estate Planner of the Year. Mr. Redd is listed in The Best Lawyers in America and is "Band 1" ranked by Chambers and Partners in their High Net Worth guide. He frequently writes and lectures nationally on topics in the trusts and estates field.

Turney P. Berry

Turney P. Berry concentrates his practice in the areas of estate planning, fiduciary matters, and charitable planning. Mr. Berry is the leader of Wyatt, Tarrant & Combs' Trusts, Estates & Personal Planning Service Team and a past member of the firm's Executive Committee. Mr. Berry is active in the American College of Trust and Estate Counsel (ACTEC), and served as President of the ACTEC Foundation, Regent of the College, State Chair for Kentucky, Chair of the Estate & Gift Committee, and Chair of the Charitable and Tax-Exempt Committee. Currently he serves as Chair of the State Laws Committee, and a member of the Long Range Planning Committee.

As a Uniform Law Commissioner, Mr. Berry currently serves as Chair of the Study Committee on Transfers to Minors Act, Vice-Chair of the Drafting Committee on Conflicts of Laws in Trusts and Estates, Member of the Electronic Estate Planning Documents Committee, Member of the Joint Editorial Board for Uniform Trust and Estate Acts, and Member of the Drafting Committee on Uniform Determination of Death Act. He has served as chair of the Uniform Fiduciary Income and Principal Act (UFIPA), chair of the Uniform Power of Appointment Act, Vice Chair of the Drafting Committee on Electronic Wills Act, Co-Chair of the Drafting Committee on Uniform Cohabitants' Economic Remedies Act, and as a member of the drafting committees for the Directed Trust Act, the Revised Fiduciary Access to Digital Assets Act, the Trust Decanting Act, the Insurable Interests in Trusts Act, the Premarital and Marital Agreements Act, the Transfer on Death Deeds Act, the Revised Disposition of Community Property Rights at Death Act, and the Uniform Probate Code Artificial Reproductive Technology provisions, and an adjunct member of the Fundraising Through Public Appeals Act.

Mr. Berry is a Fellow of the American College of Tax Counsel, a member of the American Law Institute, a member of The International Academy of Estate and Trust Law, a member of the Advisory Council of the Heckerling Institute on Estate Planning, a Member of the Advisory Board of Trusts and Estates Monthly, and a member of the Bloomberg BNA Tax Advisory Board (Estates, Gifts, and Trusts). He serves as Adjunct Professor at the University of Miami Estate Planning LLM Program (teaching Business Succession Planning), and has served as Adjunct Professor at Vanderbilt University, the University of Missouri, and the University of Louisville, and regularly speaks at the nation's leading estate planning conferences. Since 1996, Mr. Berry has served as Co-Chair of the Midwest/Midsouth Estate Planning Institute at the University of Kentucky (the longest continuously run CLE event in Kentucky).

Mr. Berry has been certified as an Accredited Estate Planner® (AEP®) by the National Association of Estate Planners & Councils and is a member of its Estate Planning Hall of Fame [Kentucky does not recognize legal specialties]. He is listed in Woodward/White's The Best Lawyers in America® and in the Kentucky Super Lawyer Magazine in the area of Trusts and Estates.

A native of Tennessee, Mr. Berry received his B.A. and B.L.S. in 1983 from the University of Memphis and his J.D. in 1986 from Vanderbilt University.

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Addressing the Estate Planning Needs of Modern-Day Clients

By: Charles A. Redd
STINSON LLP
St. Louis, Missouri

I. INTRODUCTION

Estate planning professionals must be able to handle the estate planning needs of twenty-first century clients, whether they are children or grandchildren of our established clients or new clients who have already accumulated wealth or are on a trajectory to do so. Some of today's clients adhere to values and live in ways not commonly recognized or understood in society just a few decades ago. Estate planning for these clients may involve considerations and require approaches that are unique relative to our experience with "traditional" or older clients.

II. SAME-SEX MARRIAGES, CIVIL UNIONS AND COHABITING UNMARRIED INDIVIDUALS

A. Same-Sex Marriages

Not so long ago, American law universally recognized marriage as a status available exclusively to one man and one woman. State-by-state, that began to change. The laws of some, but not all, states were amended to allow individuals of the same sex to marry.[1] In that legal environment, perplexing questions arose regarding whether a couple legally married under the law of State X was entitled to have their marriage recognized in State Y, whose laws didn't recognize same-sex marriage.

In 2013, the dam began to break when the Supreme Court of the United States handed down its decision in *United States v. Windsor*.[2] In *Windsor*, the estate of a predeceased same-sex spouse sought a federal estate tax marital deduction. The Supreme Court ruled that Section 3 of the Defense of Marriage Act,[3] which defined "marriage" as a status to be enjoyed exclusively by one man and one woman, was unconstitutional, and so the marital deduction was to be allowed. Then, just two years, to the day, later, the Supreme Court decided the case of *Obergefell v. Hodges*,[4] which held that a marriage of two individuals of the same sex must be recognized as legally valid in all states because failure of such recognition violated the Fourteenth Amendment.

From and after *Obergefell*, same-sex marriage has been and is no different, under civil law, from marriage of persons of the opposite sex. Accordingly, all estate planning opportunities,

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[1] Among the first states whose laws came to recognize same-sex marriage were California, Connecticut, Delaware, Iowa, Maine, Maryland, Massachusetts, Minnesota, New Hampshire, New York, Rhode Island, Vermont and Washington.
[2] *United States v. Windsor*, 570 U.S. 744, 133 S.Ct. 2675, 186 L.Ed.2d 808 (June 26, 2013).
[3] 1 U.S.C. § 7.
[4] *Obergefell v. Hodges*, 576 U.S. 644, 135 S.Ct. 2584; 192 L.Ed.2d 609 (June 26, 2015).

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obstacles, advantages and disadvantages that flow from the marital status apply equally to same-sex and opposite sex marriages. No extra steps, effort or workarounds are required.

B. Civil Unions

Until same-sex marriage was recognized in all states in the same way as heterosexual marriage, civil unions, sometime referred to as domestic partnerships, were a substitute, or a "placeholder," for marriage for same-sex couples. Before *Obergefell*, the laws of several states didn't recognize same-sex marriage but provided for civil unions.[5] Statutes setting out the requirements and characteristics of civil unions generally sought to mimic as much as possible traditional marriage.[6] From and after *Obergefell*, civil unions have no longer served the purpose for which they were designed. Today, a same-sex couple, just like an opposite sex couple, may choose to be married or may choose to cohabitate.

C. Cohabiting Unmarried Individuals

1. *In General*

A couple may choose not to marry for a variety of legal (including tax) and non-legal reasons. Simply put, in the 21st century, the institution of marriage doesn't invoke nearly the same value and respect it once did. Today, a significant fraction of couples choose to live together without being married.

2. *Differences in Treatment for Estate Planning Purposes*

Estate planners working for unmarried couples must understand that the emotional bonds between the couple are likely every bit as close as with a married couple, but at the same time the lack of a marital relationship presents challenges that need to be recognized and addressed. Among the salient issues are these:

- **Gift and Estate Tax Marital Deduction.** Not available to unmarried couples.

- **Transmission of Deceased Spouse's Unused Exclusion Amount ("Portability").** Not available to unmarried couples.

- **Gift-Splitting.** Not available to unmarried couples.

- **Disclaimers.** A surviving spouse who disclaims an interest that passed from the predeceased spouse may still meet the requirements for a tax-free qualified disclaimer under even though the disclaimer results in the property passing for the surviving spouse's benefit.[7] A disclaimer by one who is

[5] These states included Colorado, Hawaii, Illinois, New Jersey, Oregon and Wisconsin.
[6] However, in some states whose laws recognized civil unions, a same-sex couple in a civil union remained at a disadvantage, as compared to a heterosexual couple, with regard to state estate or inheritance tax.
[7] Internal Revenue Code ("IRC") § 2518(b)(4); Treas. Reg. § 25.2518-2(e).

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not the surviving spouse of the decedent will not meet the requirements of Internal Revenue Code ("IRC") § 2518 if the disclaimant has a beneficial interest in disclaimed property.

- **Retirement Benefits.** A surviving spouse who is named as beneficiary under a qualified plan or IRA is an "eligible designated beneficiary."[8] An unmarried surviving partner ordinarily wouldn't be. A surviving spouse has preferential rights as compared to a non-spousal beneficiary when it comes to rollovers, determination of the required beginning date and calculating minimum required distributions. Additionally, a spouse who owns a retirement asset subject to ERISA must obtain the other spouse's written consent to change the beneficiary with respect to such asset.[9] Unmarried partners don't have this burden (or, from the point of view of the non-owning partner, this protection).

- **Tax Return Filing Status.** Members of an unmarried couple may file their federal income tax returns only as single taxpayers or as a head of household. Members of a married couple may only file as "Married Filing Jointly" or "Married Filing Separately." In some cases, such as where the members of a couple have taxable incomes in similar amounts, they may actually be better off by not being married and filing jointly.

- **Loss Recognition.** Married couples generally lack the ability to deduct losses arising from direct or indirect transfers between themselves.[10] Unmarried couples have the advantage here.

- **S Corporations.** Members of a family (including spouses) who hold shares of an S corporation are treated as only one shareholder for purposes of determining whether the 100 shareholder limit has been met.[11]

- **Internal Revenue Code Chapter 14.** The restrictions imposed by IRC §§ 2701, 2702 and 2704 don't apply in the case of transactions between family members.[12] Thus, unmarried couples have a decided advantage in this context. For example, a grantor retained income trust ("GRIT") could be used.

- **State Probate Laws.** Certain rights that conclusively or presumptively accrue to spouses generally don't apply in the case of unmarried individuals,

[8] IRC § 401(a)(9)(E)(ii).
[9] *See* IRC § 417(a)(2), which prohibits depriving a spouse of a "qualified joint and survivor annuity" or a "qualified preretirement annuity in the absence of the spouse's consent.
[10] IRC § 267.
[11] IRC §1361(c)(1).
[12] *See* IRC §§ 2701(a) & (e)(1); 2702(a)(1) & (e); 2704(a) & (c)(2).

such as elective share, fiduciary appointment presumptions and other spousal rights arising under state probate laws.[13]

- **Tenancy by the Entirety.** Not available to unmarried couples.

- **Community Property.** Not available to unmarried couples.

3. *Cohabitation Agreements*

For unmarried couples, cohabitation or domestic partner agreements provide protections (and may have some enforceability requirements) analogous to those in a marital agreement context in the event of separation or death. Cohabitation or domestic partner agreements are particularly important because, unless cohabitants define their relationship in a written contract, the law will not ordinarily recognize the relationship in the event of a separation or the death of one of the parties. Accordingly, a cohabitation agreement can help secure the legal rights of parties who are in a relationship ostensibly similar to marriage, define the extent of such rights in accordance with the parties' intent and help minimize any disputes upon a break-up or the death of a party. That said, depending on the applicable jurisdiction and the existence (or lack thereof) of so-called palimony rights,[14] there may or may not be rights potentially to be waived.

While the scope and enforceability of marital agreements are generally governed by specific statutes,[15] cohabitation agreements are almost exclusively governed by general contract principles. Thus, cohabitation agreements can be more flexible in their design. However, the consideration provided by each party should be explicitly stated. An agreement to pool earnings or for each party to provide business services is generally adequate.[16]

III. ASSISTED CONCEPTION CHILDREN, ADOPTED AND NON-ADOPTED CHILDREN AND OTHER "OUT-OF-THE-ORDINARY" BENEFICIARIES

A. Assisted Conception Children

When engaged in estate planning for a client who may anticipate the birth of children in a manner other than through an "ordinary" conception process, it's critical to draft documents that

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[13] Many states that recognize civil unions also grant the members of such unions the rights and benefits identical or similar to those of married persons. For example, Vt. Stat. Ann. tit. 15, § 1204(a) provides that parties to a civil union have "all the same benefits, protections, and responsibilities under law…as are granted to spouses in a civil marriage," and Vt. Stat. Ann. tit. 15, § 1204(e)(1) further provides, by way of example and not limitation, that such benefits and protections include "laws relating to title, tenure, descent and distribution, intestate succession, waiver of will, survivorship, or other incidents of the acquisition, ownership, or transfer, *inter vivos* or at death, of real or personal property, including eligibility to hold real and personal property as tenants by the entirety…" Similarly, N.J. Rev. Stat. § 37:1-33 provides that "whenever in any law…reference is made to 'marriage,' 'husband,' 'wife,' 'spouse,' 'family,' 'immediate family,' 'dependent,' 'next of kin,' widow,' widower,' 'widowed' or another word which in a specific context denotes a marital or spousal relationship, the same shall include a civil union…"

[14] *See*, *e.g.*, *Marvin v. Marvin*, 557 P.2d 106, 18 Cal.3d 660, 134 Cal. Rptr. 815 (1976).

[15] *See*, *e.g.*, Section 452.325, RSMo.

[16] *See* Wolven, "The New Normal: Planning for the 'Modern Family'," 49TH ANNUAL HECKERLING INSTITUTE ON ESTATE PLANNING (2015).

explicitly take this possibility into consideration so that no such child is inadvertently excluded or, depending on the client's desires, included.

In this context, consider whether a client's Will and/or trust instrument should specify whether an assisted conception child is to be treated as a natural-born child (or more remote descendant) of the client:

- If such child was conceived using the client's ovum or sperm and the ovum or sperm of the client's spouse (or non-marital partner);
- If such child was conceived using the client's ovum or sperm and the ovum or sperm of a donor;
- If such child was conceived using the ovum or sperm of a donor and the ovum or sperm of the client's spouse (or non-marital partner);
- If such child was conceived during the client's life;
- Regardless of whether the ovum (the client's or that of the client's spouse (or non-marital partner) or of a donor) was fertilized in utero;
- Regardless of whether the fetus was carried to term by the client or the client's spouse (or non-marital partner); and/or
- Regardless of whether the child has been legally adopted by the client if such adoption is required under applicable law at the time of such child's birth to establish that the client is such child's parent.

Also, be careful to note in the client's estate planning documents that no individual who may be considered a natural parent of a child solely because of having donated ovum or sperm or having acted as a surrogate mother and who would not otherwise be a beneficiary under the client's estate plan, nor any other individual who is related to such individual by consanguinity or affinity, is ever to be a beneficiary under the client's estate plan.

As an example of the difficulties to be encountered in this area of law, consider the case of *Astrue v. Capato*,[17] wherein the Supreme Court of the United States held that twins posthumously conceived through *in vitro* fertilization were not "children" for purposes of "child's insurance benefits" under the Social Security Act. The Court deferred to a Social Security Administration rule that in turn deferred to state intestacy law, and the law of Florida, which applied in this case, treated posthumous children as children only if they were conceived before death.

B. Adopted and Non-Adopted Children

Depending on family composition and dynamics, innumerable estate planning choices may present themselves in connection with whether adopted children or even non-adopted children are to be included in (or excluded from) the client's estate plan (as the client's children or more remote descendants). Included among the questions that may be relevant and need to be handled explicitly are the following:

[17] *Astrue v. Caputo*, 566 U.S. 541, 132 S.Ct. 2021, 182 L.Ed.2d 887 (May 21, 2012).

- Are children adopted by the client and/or the client's spouse (or non-marital partner) to be included? If "yes," must they have been adopted before having reached a designated age?
- Are natural-born and/or adopted descendants of any such adopted child to be included?
- Are children adopted by any natural-born descendant of the client and/or the client's spouse (or non-marital partner) to be included? If "yes," must they have been adopted before having reached a designated age?[18]
- Are children and/or or more remote descendants of the client's spouse (or non-marital partner) to be included?
- Are children and/or or more remote descendants of the client and/or the client's spouse (or non-marital partner) to be included if such children or more remote descendants are later legally adopted by an individual who is not a descendant of the client and/or the client's spouse (or non-marital partner)?
- Are certain children and/or or more remote descendants of the client to be excluded (perhaps because they are the product of a disfavored relationship or they have a poor relationship with the client and/or the client's spouse (or non-marital partner))?
- Is any child born to a mother who isn't married at the time of such child's birth, as well as the descendants of such a child, to be considered not descendants of the child's putative father, or of such father's ancestors, unless the mother and putative father subsequently marry or such father acknowledges in writing that such child is his child?

Moreover, in cases in which the context suggests it should be done, don't overlook the necessity to state in the client's estate planning documents that no individual who may be a legal parent of a child or more remote descendant of the client and/or the client's spouse (or non-marital partner) solely because of having adopted such child or more remote descendant and who would not otherwise be a beneficiary under the client's estate plan, nor any other individual who is related to such individual by consanguinity or affinity, is ever to be a beneficiary under the client's estate plan.

C. Surviving Spouses of Children

Might a client wish to include in his or her estate plan, following the death of a child of the client, the surviving spouse, if any, of such deceased child? In a case in which the answer is in the affirmative, it would seem, nevertheless, that most clients would want to impose conditions on such an arrangement. These conditions would likely include that the surviving spouse:

- Hasn't remarried; and, at the child's death, wasn't:

[18] *See Andresakis v. Modisett*, No. 07-16-00003-CV (Tex. App.—Amarillo January 4, 2017), for an example of a case in which a child, by reason of having been adopted as an adult, obtained a beneficial interest in a trust.

- o Living separate and apart from such child for any reason other than such spouse's or such child's physical or mental infirmity related to illness, injury, genetic or congenital condition, advanced age or other cause;
- o Legally separated from such child; or
- o A party with such child to a pending action or proceeding for legal separation, separate maintenance, divorce, dissolution of marriage, declaration of invalidity of marriage or annulment.

IV. Dealing With Irrevocable Trusts Whose Terms Restrict Who May be a Beneficiary

A. Freedom of Disposition

A cornerstone of American jurisprudence in the design and administration of estate plans is that, with relatively rare exceptions, and after obligations to creditors and taxing authorities have been satisfied, individuals are free, by means of properly designed and legally valid documents, to direct disposition of their property, during life and at death, in any manner, and to whomever, they choose. One exception relates to spouses. An almost inviolable rule is that an individual may not put in place an estate plan that impoverishes his or her spouse. Generally, elective share and related provisions of law in common law jurisdictions, and community property regimes in community property states, ensure this result. An additional exception rises in the State of Louisiana, where the rules of "forced heirship" prevent an individual's complete disinheritance of certain of his or her children.

Still another exception arises under the masthead of "violation of public policy."[19] Public policy is an amorphous concept. It's susceptible to change over time as societal mores evolve. It also varies from state to state. In some states, a particular manner of disposition may be regarded by the courts as repugnant and unworthy of enforcement, whereas, in other states, it wouldn't be a problem. One of the most notable and interesting examples of this in recent years is the *Feinberg* case.

B. *In Re Estate of Feinberg*

Feinberg[20] is a relatively recent and fascinating exposition of public policy considerations arising in connection with property passing at a decedent's death under his or her estate planning documents.

1. *Facts*

Max Feinberg died in 1986. In his revocable trust instrument, he conferred on his wife, Erla, lifetime and testamentary limited powers of appointment over certain trust assets. In

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[19] See RESTATEMENT (THIRD) OF THE LAW OF TRUSTS § 29 (3d ed. 2003), which provides that trust provisions that are contrary to public policy are void.

[20] *In re Estate of Feinberg*, 919 N.E.2d 888, 235 Ill.2d 256 (September 24, 2009); *see*, *also*, Cundiff & Copans, "*In re Estate of Feinberg*: When Legal Fees Consume an Estate – Restrictive Clauses Are Moot," 35 ACTEC J. 255 (Winter 2009); Horton, "Testation and Speech," 101 GEORGETOWN L. REV. 61 (2012).

default of exercise of these powers, Max directed distribution to his descendants but subject to what the court called a "beneficiary restriction clause." The beneficiary restriction clause directed that 50% of the trust assets be held in separate trusts for his grandchildren but provided that any descendant who married outside the Jewish faith or whose non-Jewish spouse did not convert to Judaism within one year of marriage would be deemed deceased and his or her beneficial interest in the trust established or to be established for him or her.

Erla exercised her lifetime power to direct the distribution at her death of $250,000 to each child and grandchild who would not be deemed deceased under Max's beneficiary restriction clause. When Erla died in 2003, all five grandchildren had been married for more than one year, but only one met the conditions of the beneficiary restriction clause. One of the disinherited grandchildren sued Max's children (including her father) challenging the validity of the beneficiary restriction clause.

2. *Trial Court and Appellate Court Holdings*

The trial court ruled the beneficiary restriction clause invalid on public policy grounds for interfering with the right to marry a person of one's own choosing. The Appellate Court of Illinois affirmed – largely in reliance on prior decisions of the Supreme Court of Illinois and, even more, on Section 29 of the RESTATEMENT (THIRD) OF THE LAW OF TRUSTS.[21]

3. *Decision of the Supreme Court of Illinois*

The Illinois Supreme Court didn't take up whether the plan of disposition set out in Max's estate plan violated public policy but, rather, focused on whether the manner in which Erla exercised her lifetime power of appointment violated public policy.

In so doing, the court reviewed Illinois public policy in support of broad testamentary freedom, observing that state law imposed only two limits on a testator's freedom to dispose of property as he or she desired – a surviving spouse's right to renounce a Will in favor of statutory benefits and protections for pretermitted heirs. The court noted that there is no forced heirship for descendants under Illinois law.

In support of this policy, the court noted the broad purposes for trusts under state trust statutes, the repeal of the common law rule against perpetuities and the Rule in Shelley's Case, and the focus in case law on determining the intent of the testator. The factual record indicated Mr. Feinberg's intent to benefit those of his descendants who furthered his commitment to Judaism by marrying with the faith and his concern with the dilution of the Jewish people by intermarriage. The court observed that Mr. Feinberg would be free during his lifetime to attempt to influence his grandchildren to marry within the faith, even by financial incentives.

The court acknowledged the long-standing rule that dispositive provisions that encourage divorce violate public policy. However, the court distinguished its prior decisions on the grounds that: (a) because of Erla's power of appointment, the grandchildren never received a

[21] *See* footnote 19, *supra*.

vested interest in any trust upon Max's death; (b) because they had no vested interest that could be divested by noncompliance with the condition precedent, the grandchildren weren't entitled to notice of the existence of the beneficiary restriction clause; and (c) the grandchildren, since they weren't heirs-at-law, had at most a mere expectancy that failed to materialize.

The court refused to consider whether to adopt the rule of Section 29 of the RESTATEMENT (THIRD) OF THE LAW OF TRUSTS because Erla's exercise of her power of appointment was not in trust but, rather, was in the nature of a testamentary disposition. The court held that Erla's exercise didn't operate prospectively to encourage the grandchildren to make choices about marriage, since the condition precedent (marriage within the faith) was either satisfied or not at the moment of Erla's death and observed the distinction between conditions precedent (which might be effective even if a complete restraint on marriage) and conditions subsequent (which may not). The court observed that, because Erla's exercise of her power of appointment didn't result in any continuing trusts, this wasn't a case of "dead hand control" or an attempt to control the future conduct of the beneficiaries.

For all these reasons, the court concluded there was no violation of public policy and therefore reversed the rulings of the courts below.

The court rejected the disinherited grandchild's other arguments, including her claim that the beneficiary restriction clause violated the constitutional right to marry, because the absence of a governmental actor. The court summarized its holding as follows: "Although those plans might be offensive to individual family members or to outside observers, Max and Erla were free to distribute their bounty as they saw fit, and to favor grandchildren of whose life choices they approved over other grandchildren who made choices of which they disapproved, so long as they did not convey a vested interest that was subject to divestment by a condition subsequent that tended to unreasonably restrict marriage or encourage divorce.

C. Public Policy Considerations

When evaluating provisions in a Will or trust instrument from the perspective of whether it will (or should) withstand public policy scrutiny, a couple of levels of analysis may be appropriate. First, is the restrictive or punitive language under consideration viscerally offensive? Again, as stated above, the answer to this question may depend on the era and the locale in which it's presented. Second, does that language have a realistic potential to cause its target to take, or refrain from taking, particular action?[22]

Feinberg illustrates how the answers to these questions may lead a court to a conclusion. The majority opinion that emanated from the Illinois Appellate Court stated that what came to be referred to by the Illinois Supreme Court as the "beneficiary restriction clause" "seriously interferes with and limits the right of individuals to marry a person of their own choosing." Quite to the contrary, the dissent saw the beneficiary restriction clause as a legitimate method by which to preserve a 4,000-year-old heritage. Moreover, the dissent observed, and the Illinois Supreme

[22] Such language could lack such potential at the death of a testator or settlor but have such potential at the subsequent death of a trust beneficiary.

Court ultimately agreed, that the beneficiary restriction clause couldn't operate to influence a beneficiary's behavior – whether in a positive or a negative direction. The beneficiary restriction clause operated to establish a condition precedent for receiving a distribution at Erla's death – a condition presumably not known to any beneficiary until Erla's death because it was contained in her Will which was ambulatory until her death. At that moment, a beneficiary either satisfied or didn't satisfy, the condition. Query, however, whether language in a Will or revocable trust instrument that restricts who may be a beneficiary may be considered so vile a court would hold it void regardless of whether it does nothing other than establish a condition precedent, *e.g.*, language that disinherits an individual who's married to someone of a particular ethnicity or to an individual of the same sex.

V. ESG INVESTING IN A TRUST

A. Introduction

ESG (environmental, social and governance) investing, otherwise known as socially responsible investing, or "SRI," has increased in popularity in recent decades. Generally, ESG investing promotes the consideration of social and/or ethical issues in making investments. Those who have concerns about and want to be good stewards of the environment may choose to make investments in firms that create or use "green energy" and not to invest in the fossil fuel industry. Individuals who are focused on social responsibility might direct their investments toward companies that have a demonstrated record of treating their employees fairly and, perhaps, away from producers of alcoholic beverages or firearms. Investors with a particular interest in governance could be attracted to companies having independent boards, capable management and executives who aren't compensated excessively.

Pursuing an ESG investment philosophy doesn't necessarily mean forfeiting financial returns. Depending on the particulars of a given ESG investing strategy, it may be possible to make ESG-oriented investments whose economic performance is competitive with non-ESG-oriented investments. It's also possible, though, to adopt an investment approach that sacrifices economic returns in exchange for supporting one or more ESG objectives. Clearly, individuals are entitled to make investments that aren't optimally productive of financial returns and even investments that lose value. Other than in exceptional cases, however, trustees don't have such latitude.

B. Trust Instrument Provisions

When a trust instrument contains explicit and clear instructions authorizing the trustee to engage in ESG investing, the trustee may select investments on the basis of ESG if such investments are otherwise appropriate for a trust, and conform to the ESG parameters set out in the trust instrument, even though such investments aren't as lucrative for the trust as available alternative investments.[23] Allowing ESG principles to govern in such a case would seem analogous to sanctioning a trustee's retaining and investing in closely-held business equity when

[23] *See* Uniform Prudent Investor Act (UPIA), Section 1(b).

the trust instrument explicitly allows or requires the trustee to do so regardless of whether such equity is otherwise a trust-quality investment.

On the other hand, "[i]f the trust instrument does not clearly authorize [ESG] principles, a trustee may consider a beneficiary request for responsible investing in the context of appropriate investment standards. That is permissible if the trustee can demonstrate that [ESG] will match or exceed the performance of other types of investments… If the trustee thinks that the [ESG] returns will be below-market, [ESG] investing is very risky for the trustee to undertake absent specific language in the trust agreement or a binding release from the beneficiaries (which is very hard to get)."[24]

C. Duty of Loyalty

ESG investing may violate the duty of loyalty espoused by Section 5 of the Uniform Prudent Investor Act (UPIA). Specifically, the Comments to Section 5 of the UPIA explicate the conflict between the duty of loyalty and ESG: "No form of so-called "social investing" is consistent with the duty of loyalty if the investment activity entails sacrificing the interests of trust beneficiaries – for example, by accepting below-market returns – in favor of the interests of the persons supposedly benefitted by pursuing the particular social cause." A trustee who invests to fulfill the trustee's own non-economic agenda, at the cost of lower returns on trust investments, breaches the trustee's duty of loyalty to the beneficiaries.

D. Duty of Impartiality

Trustees must act impartially as among the various beneficiaries of the trust.[25] It may not be possible (or appropriate) to engage in ESG investing when the personal philosophies and goals of the beneficiaries are in conflict, even when the investment produces the same result as non-ESG investing. Beneficiaries may have different beliefs and values such that investments that meet the ESG aspirations of one beneficiary may be in conflict with another's.

E. Duty of Prudent Investment

The Restatement (Third) of Trusts provides that "[t]he trustee has a duty to the beneficiaries to invest and manage the funds of the trust as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the trust."[26] Almost identically, the UPIA provides that "[a] trustee shall invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust."[27]

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[24] Steve R. Akers, "ACTEC 2014 Fall Meeting Musings," (November 18, 2014).
[25] UPIA, Section 6.
[26] RESTATEMENT (THIRD) OF TRUSTS, § 90 (2007).
[27] UPIA, Section 2(a).

F. State Laws

Lawmakers in some states have sought to enable, or at least make easier, ESG investing by a trustee. For example, an Illinois statute[28] says a trustee may consider environmental and social considerations. (Yes, that's what it says; "consider…considerations.") As another example, a Delaware law is a bit more explicit and says, essentially, that a fiduciary may take ESG factors into account if so doing comports with the beneficiaries' personal values and beliefs.[29] But what if the beneficiaries don't all share the same values and beliefs? And how much extra comfort and protection does a trustee really get from "may consider" or "may take into account"? Finally, New Hampshire's recently revised statute setting out the prudent investor rule[30] seems to do no more than state that a nonjudicial settlement agreement (NJSA) can be used to confer ESG investing power on a trustee. It seems obvious that a New Hampshire NJSA could have been so used before that statute was changed.[31] In any event, these statutes don't appear to move the needle much, if at all.

G. Conclusion

If a trustee can make an ESG investment that produces returns as good as or better than non-ESG investments, no one will have grounds to complain under traditional prudent investor rule principles with which we're all familiar, but the converse is also true. A trustee who sacrifices investment return to pursue some ESG-related agenda won't have a leg to stand on in a breach of trust case unless the will or trust instrument expressly allows such ESG investing or the Trustee gets informed, unanimous beneficiary consents, releases or ratification.[32]

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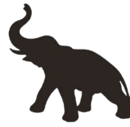
[28] 760 ILCS 3/902(c).

[29] *See* 12 Del. Code § 3302(a).

[30] N.H. Rev. Stat. § 564-B:9-902.

[31] *See* N.H. Rev. Stat. § 564-B:1-111(d).

[32] "Only to the extent permitted by the terms of the trust or by the consent of the beneficiaries may the trustees of private trusts properly take social considerations into account in making investment decisions." 4 AUSTIN W. SCOTT ET AL., SCOTT & ASCHER ON TRUSTS § 19.1.13 (5th ed. 2007).



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Fax (706) 353-3994, Email lsebestyen@CannonFinancial.com
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CERTIFICATE OF ATTENDANCE FOR CALIFORNIA MCLE

To be Completed by the Provider

Provider: Cannon Financial Institute (CA Provider #12179)

Subject Matter/Title: Addressing the Estate Planning Needs of Modern-Day Clients

Date and Time of Activity: August 20, 2024, 1:00-2:30 PM ET, 12:00-1:30 PM CT, 11:00AM-12: 30 PM MT,

10:00AM- 11:30 AM PT

Location: Teleconference

Length of Presentation: 1.5 Hours

ELIGIBLE CALIFORNIA MCLE CREDIT:

TOTAL HOURS: 1.5

Legal Ethics:

Elimination of Bias in the Legal Profession:

Competence:

To Be Completed by the Attorney after Participation in the Above-Name Activity

By signing below, I certify that I participated in the activity described above and am entitled to claim the following California MCLE credit hours:

TOTAL HOURS: ________________________

(You may not claim credit for the following sub-fields unless the provider is granting credit in these areas as listed above.)

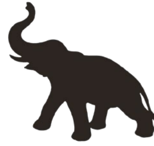
Legal Ethics:______________________________

Elimination of Bias in the Legal Profession:______________________________

Competence: ______________________________

Attorney Signature:

REMINDERS: Keep this record of attendance for four years. In the event that you are audited by the State Bar, you may be required to submit this record of attendance. Send this to the State Bar only if you are audited. You must sign in on the Official Record of Attendance for California MCLE maintained by this provider in order for these hours to qualify for California MCLE credit.



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August 20, 2024

Laurie Sebestyen
Professional Education Coordinator

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Virginia MCLE Board

Certification of Attendance (Form 2)

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Name: ________________________ **VSB ID#:** ________________________

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City **State** **Zip**

Course ID: NLL1556

Sponsor: Cannon Financial Institute

Title: Addressing the Estate Planning Needs of Modern-Day Clients

Type: Live

Format: Webcast

Credits: 1.50 **CLE** 0.00 **(Ethics)** 0.00 **Well-being**

Credit Certification

Date completed: ________________________ **Location:** ________________________

Do not leave blank or form will not be processed.

By my signature below I certify:

1. I attended a total of _____ (hrs/mins) of approved CLE of which (_____) (hrs/mins) were approved Ethics and _____(hrs/mins) were approved Well-being. (Claim credit for actual time in attendance. Round to the nearest half hour. E.g. 75 min=1.5 CLE hours.)
2. The sessions for which I am claiming credit had written instructional materials to cover the subject matter.
3. I participated in this program in a setting physically suitable for the course.
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5. I understand I may not claim credit for any course/segment for which credit has already been claimed in the current or preceding CLE periods.
6. I understand that a materially false statement shall be subject to appropriate disciplinary action.

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Date **Signature**

MCLE requirement: Paragraph 17, Section IV, Part Six of the Rules of the Supreme Court of Virginia and MCLE Board Regulations. Completion deadline: October 31. Reporting deadline: December 15. Fees are assessed for failure to comply with MCLE deadlines.

Virginia MCLE Board | Virginia State Bar | 1111 East Main Street, Suite 700 | Richmond, VA 23219-0026
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