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Subject: Martin Shenkman, Sandra Glazier & Howard Zaritsky on *Raia v. Lowenstein Sandler LLP* - Thoughts on a Recent Malpractice Case

"A recent New Jersey malpractice case, Raia v. Lowenstein Sandler LLP ('Raia'),[i] has served as the catalyst for discussions among many advisers. Regardless of how Raia is resolved, and at this preliminary juncture only a complaint has been filed, some of the issues it raises directly and indirectly, are important for practitioners to consider. Among the issues that practitioners might wish to ponder are:

- *Being sued, even if the case resolves favorably, is traumatic, costly, inhibits the ability to practice because of the time demands of the suit, and worse.*
- *How practitioners might conduct their practices with an eye toward what you can do to reduce the likelihood that a client will become unhappy and sue?*
- *What different or additional language might be added to retainer agreements?*
- *What approaches might be used to apprise clients of the risks inherent in many estate planning transactions? What approaches might be counter-productive?*
- *Should the rules of professional conduct governing attorneys be reconsidered as to restrictions on liability limitations given the current planning environment?*
- *How do other allied professionals address liability limitations and what might that mean to estate planning attorneys?*
- *Might mandatory arbitration provisions be beneficial and, if beneficial, are they permissible for attorneys under ethics rules?*

While Raia served as the catalyst for this newsletter, the implications of the allegations contained in the Raia complaint are much broader."

We close the week with commentary on *Raia v. Lowenstein Sandler LLP* by **Martin M. Shenkman**, **Sandra Glazier** and **Howard Zartisky**.[ii]

Here is their commentary:

EXECUTIVE SUMMARY:

Issues Practitioners Might Ponder in Light of Recent Malpractice Case

A recent New Jersey malpractice case, *Raia v. Lowenstein Sandler LLP* ("Raia"),[iii] has served as the catalyst for discussions among many advisers. Regardless of how Raia is resolved, and at this preliminary juncture only a complaint has been filed, some of the issues it raises directly and indirectly, are important for practitioners to consider. Among the issues that practitioners might wish to ponder are:

- Being sued, even if the case resolves favorably, is traumatic, costly, inhibits the ability to practice because of the time demands of the suit, and worse.
- How practitioners might conduct their practices with an eye toward what you can do to reduce the likelihood that a client will become unhappy and sue?
- What different or additional language might be added to retainer agreements?
- What approaches might be used to apprise clients of the risks inherent in many estate planning transactions? What approaches might be counter-productive?
- Should the rules of professional conduct governing attorneys be reconsidered as to restrictions on liability limitations given the current planning environment?
- How do other allied professionals address liability limitations and what might that mean to estate planning attorneys?
- Might mandatory arbitration provisions be beneficial and, if beneficial, are they permissible for attorneys under ethics rules?

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COMMENT:

Background on the Case

Raia involves a malpractice claim against a well-respected law firm for planning and implementing (what appears from the complaint to be) a series of commonly used estate planning techniques including GRATs, gifts, and installment sales to grantor dynasty trusts, in an effort to reduce the client's potential estate tax obligations.

At its core, the *Raia* complaint focuses on the following points:

- The grantor's use of an installment sale to an intentionally defective grantor trust ("IDGT") may result in the loss of basis adjustments when the grantor dies. The plaintiffs argue that the loss of basis adjustment on the grantor's death and income tax consequences *potentially* triggered on the change from grantor trust status to a complex trust either were not explained to them or were not understood by them.
- The fact that planning techniques are commonly used does not necessarily assure those techniques are appropriate for the particular client, or the circumstances in *Raia*. This issue is a particularly important warning to practitioners to exercise caution in applying even common planning techniques without first understanding each client's unique situation, circumstances and goals.
- The complaint appears to focus on the income tax consequences that will be experienced when grantor trust status is lost or toggled off.
- The potential for increased income tax consequences to the beneficiaries of the plan due to the loss of a potential step-up in basis on assets transferred out of the estate.
- The income tax cost on negative basis real estate assets sold to the IDGT may be significant if the trust ceases to be a grantor trust during the grantor's lifetime.

- The plaintiffs assert that they were not informed of these risks. The actual facts of this aspect of *Raia* cannot be known, the mere issue itself has significance to practitioners and perhaps impacts changes in the standards of practice.

- An underlying premise appears to be that even though the Plaintiffs were not the grantor (or the client under the engagement related to the formation of the plan), they nonetheless have standing to bring the action and as beneficiaries are entitled to damages.

Paragraph 6 of the complaint provides:

> *The applicable standard of care requires that defendants know and apprise the plaintiffs of the consequences of the advice defendants provide and the implementation of that advice. Nonetheless, Mr. Weinstock and the Lowenstein firm failed, over a period of years, during the course of meetings, correspondence and telephone conferences with the plaintiffs, to appreciate these consequences or to advise the plaintiffs of them. This was a breach of the applicable standard of care, which was the proximate cause of damages to the plaintiffs*.

This is the second action filed relating to this estate plan. The first action, filed in March 2018 against a national CPA firm, has been stayed in order to add the law firm as a defendant.[iv] The plaintiffs appear not yet to have brought the wealth management firm that advised them into *Raia* as additional responsible defendants. Still, wealth managers everywhere, along with estate planners, and CPAs, may wish to take heed and consider protective actions that might be implemented to their practice procedures regardless of *Raia*'s ultimate disposition.

Any estate planning professional who reads this case must get a feeling that "there but for the grace of God, go I."

New Jersey State Law Prerequisites to a Malpractice Action

New Jersey, where *Raia* was brought, requires that the plaintiff in a professional malpractice case submit an affidavit of merit by a similarly licensed professional stating that in the affiant's professional opinion, "there exists a reasonable probability that the care, skill or knowledge exercised

or exhibited in the … practice or work that is the subject of the complaint fell outside acceptable professional …standards." The affidavit of merit must be submitted within 60 days of the filing of the defendant's answer (extendable to 120 days upon a showing of good cause). The penalty for failure to do so is dismissal of the case with prejudice. It is not clear whether the plaintiffs filed the affidavit of merit with the complaint, as is common practice.

A New Jersey legal malpractice claim involves a plaintiff's interest in damages arising from the defendant attorney's breach of professional standard of care.[v] By contrast:

> *[t]he conduct required to constitute a breach of fiduciary duty requires a more culpable state of mind than the negligence required for malpractice. Damages may be obtained for breach of fiduciary duty when a "position of influence has been acquired and abused, or when confidence has been reposed and betrayed.*[vi]

<u>Possible Issues with the Allegations of Damage</u>

It appears that the grantors of the trusts in the complaint are still living and that the trusts are still grantor trusts.[vii] If that is correct, remedial action, such as swapping assets if the trusts permit, or unwinding installment sales, may still be possible. It is not, therefore, clear whether or not damages have actually been incurred. Also, the plaintiffs have a duty to mitigate their own damages and it is not clear at this stage whether remedial action was feasible, and if so whether it was taken.

Thus, some of the complaints might be speculative and dependent on what the law will be when the grantor dies or the trust ceases to be a grantor trust. Again, until more is known it is unclear what many of the critical facts are in *Raia*.

<u>Selected Allegations in the Complaint</u>

Regardless of the resolution of *Raia*, the allegations should concern practitioners and may cause them to re-evaluate their policies and procedures. The allegations in the complaint include the following:

- A client[viii] may sue counsel without having yet been harmed by the estate planner's actions, as long as there is an imminent risk of harm.[ix]

- The advisors were accused of not analyzing fully the risks and benefits of the plan.[x]

- The advisors were accused of not fully informing the clients of the risks of transferring real estate to a dynasty trust.[xi]

- Communication to the client of the potential consequences of a transaction is essential. The complaint alleges that this was not done.[xii]

- The advisors were claimed not to have considered or informed the clients fully of the problems caused by the loss of a basis adjustment at death with respect to real property that was transferred to a grantor trust.[xiii]

- Practitioners need to be careful about over-selling or marketing particular planning techniques. While no conclusion can be made on what occurred in *Raia*, that was an allegation in the complaint.[xiv] Suggesting that counsel "marketed" its plan and advice is certainly possible, although the facts have not yet been determined. We do not know what conversations occurred. Some attorneys (not suggesting that this occurred in *Raia*) do stress the advantages of a plan and downplay the disadvantages. Clients' memories can be selective and creative. If a practitioner stresses the estate tax savings, the client may not remember at all your discussion of income tax or other issues. Apart from *Raia*, this allegation should be considered by practitioners who feel pressured by the need to produce revenue to be cautious of "marketing" a plan to any client. Perhaps the discussion of options with the client might deflect such an objection. If options are provided then it would seem more difficult for a client to argue the plan was pushed or marketed to them. Even when an option is presented to a client, the client always retains the right not to engage in the plan and to explore other alternatives. Moreover, if the client doesn't understand the plan, doesn't the client have some duty to inform the practitioner that they need or desire further explanation before engaging in the transaction? Even when best practices are implemented, no one has the ability to truly see into a client's mind to discern what they did or didn't understand in terms of the advice and information provided.

Estate Planning is By Nature Uncertain

The tax laws are always in flux. Almost every new administration in Washington proposes and often enacts changes in the tax laws. No one can forget 2010, the year with no estate tax. President Obama's Greenbook proposals recommended a $3.5 million exemption, severe restrictions on GRATs and a myriad of other planning techniques, which could have dramatically changed the outcome of many estate tax plans. In 2012, Congress (a) contemplated reducing the federal estate tax exemption and (b) the estate tax was generally higher than income taxes, especially if the compounding implications of a generation skipping transfer tax were added to the equation. President Trump almost repealed the estate tax, but was forced to settle for doubling the already historically high exemption amount.

Few, if any, planners contemplated that within a relatively short time, the federal estate tax exemption would rise from approximately $5 Million in 2012 to $11.4 million per person in 2019, thereby changing the focus for many from estate tax savings to achieving basis increases on the death of the grantor. The next administration might reverse the path and increase estate tax rates, reduce estate tax exemptions, and curtail the use of many estate tax planning techniques. Some Democratic Presidential candidates have suggested such sweeping and harsh reforms of the estate tax system. For example, Senator Bernie Sanders has proposed a reduction in the gift tax exemption to $1 million, a reduction of the estate tax exemption to $3.5 million, and an increase in the top estate tax rate to 77%.

The Proposed Regulations under Section 2704, reducing or eliminating valuation discounts were withdrawn, but they might resurface in another administration after the 2020 election. Prior to their withdrawal many estate planners, CPAs, and wealth advisers around the country recommended that clients consider taking immediate action to lock in discounts before they might be lost. Having done this might look unfortunate in light of the withdrawal of these proposed regulations, but prescient if they are reintroduced.

This uncertainty should not provide clients a cause of action against their advisers for acting in anticipation of a change that did not occur or acting in

anticipation that no changes of significant impact would occur. That would hardly be reasonable. The 2017 tax act, for many, changed the dynamic between income and estate tax planning for those under the estate tax exemption. Those with estates under the newly-increased estate tax exemption now focus more on using estate planning devices that retain the ability to adjust basis at death. However, some advisers viewed the 2017 Tax Act as confirmation that the estate tax will never be repealed; if President Trump, with a Republican Congress, could not repeal the estate tax, can it ever happen?

No adviser has a crystal ball - so what does all this mean for planners and their clients?

Uncertainty is part of the fabric of the estate planning process. Clients must understand and accept this. Regardless of the outcome of *Raia*, it may be advisable for practitioners to consider adopting new standards of practice that enhance the likelihood that clients understand these risks; and, corroborate that explanation of the risks were provided and the client understood.

Any form of tax planning is always subject to a risk of changes in the law, the economic assumptions underlying the planning, that client goals or family dynamics might evolve, and a myriad of other assumptions involved in any plan. A change in something as simple as interest rates can have a dramatic impact on the ultimate tax consequences of a GRAT or a charitable remainder or lead trust. If the donor/settlor of a GRAT dies during the annuity term, one often assumes that the transaction has failed, but in reality, if both the value of the trust assets and prevailing interest rates have risen sufficiently, only part of the trust assets may be included in the decedent’s gross estate. No practitioner has any control over the value of the assets or interest rates. At high levels of wealth transfer planning, such as that in *Raia*, it is unlikely that any dozen nationally-known practitioners would agree on the best approach or technique to use.

In fact, on many seemingly commonly used planning points practitioners will disagree vehemently. For example, many large transactions incorporate defined value mechanisms. These have been so commonly used that some might presume that there is a single commonly-used and agreed-upon approach. In reality, there are a myriad of approaches, each

with a range of options, and many still result in disagreement at the higher echelons of the profession as to which is best. Consider:

- Some view a Wandry clause as a safe technique based on the Tax Court decision,[xv] but note that the IRS has non-acquiesced, and has challenged Wandry clauses on audit. Some practitioners are happy that many taxpayers have had success on these audits. This traditional application of the Wandry mechanism would entail the client's transfer of a specified dollar value of entity interests, not a specified percentage of interests.

- A possible risk of using the traditional Wandry approach described above, is that if less than all interests are transferred to the recipient (e.g., a buying grantor trust or IDGT), the remaining entity interests might give rise to a Powell-type argument. Because of a Wandry clause some equity interests might remain with the transferor/client. Those remaining interests "in conjunction with" others might be argued as creating a Section 2036(a)(2) issue for the transferor. Therefore, it might be safer to apply the Wandry mechanism in a manner to assure the transfer of all equity interests using a variant of the Wandry approach. This might be a traditional Wandry mechanism coupled with a sale as of the same date of any interests not transferred as a result of the Wandry clause. The remaining interests would be sold for the gift tax value finally determined. Absent some type of a secondary transfer might a successful Wandry provision create Powell implications undermining the entire plan?[xvi]

- The *King*[xvii] case addressed whether a clause in an agreement for the sale of a debtor's corporate stock to his children's trust requiring a price adjustment in the event the IRS determined the stock was sold for less than its fair market value could be enforced to defeat a gift tax assessed under Section 2512(b). Some practitioners believe that because this strategy withstood attack in *King* and has been positively cited in other (but not all) cases, it represents a viable and safe approach, while others are less sanguine, outside of the Tenth Circuit which decided it. Other practitioners have their own spin on how a note adjustment might be crafted in an attempt to avoid the implications of a Proctor issue.[xviii]

- Some practitioners use, in lieu of a Wandry approach, a spill-over of any excess consideration into a GRAT. They believe there is

merit to this position as the GRAT is sanctioned in regulations. Other practitioners have expressed concern about this technique.

- A marital trust is used in some instances as the receptacle for a spill-over of any excess, but that too raises issues as to which type of martial trust might be advisable.
- An incomplete gift trust is suggested by some as the optimal spill-over receptacle. Some practitioners, however, are uncomfortable with this approach.
- There are many other variations and views.

The point is that for almost all estate planning, especially at high levels of wealth, there are many different views and perhaps a myriad of options. There is no consistency of approach because the laws are unclear and even “clear” laws are subject change, and even different interpretations.

Practice Implications

The issues raised in *Raia* might affect traditional estate tax planning and the delivery of estate planning services. Depending upon the outcome of the case, clients may try to hold a practitioner to the high standard of foretelling the future. From the allegations in this complaint, one might conclude that the plaintiffs believe a planner should be omniscient and accurately predict changes in the law, the economy, and the client’s situation and desires. The plaintiffs do not appear to look simply at whether the professional exercised judgment consistent with the standard of practice in the industry at the time the plan was created. Tax planning is not an exact science; its proposed solutions can’t be confirmed or disproven in a laboratory or simply with a calculator.

Estate planning is at best an art, rather than a science, and practitioners should not be held to an impossible standard. All any estate planner can do is a reasonable job based on the facts, circumstances and goals presented by the client, coupled with consideration of: the known family dynamics; reasonable guesses as to when particular assets might be sold; what those assets might be worth when sold; when someone might die; what interest rates might do; how Congress might change the tax law; how the Treasury might interpret the tax law; and, what stance a particular IRS auditor might take.

Ask any insurance consultant the likelihood that a policy illustration will reflect the exact result that will be realized, and the answer is likely to be zero. That does not make it inadvisable to buy life insurance; rather, the purchaser must adhere to the principle of caveat emptor and minimize risks by working with competent professionals. The policy may not perform as illustrated, but it needs to be monitored periodically and may nonetheless provide a valuable financial result. Are the other aspects of estate planning different?

Many clients have credit shelter trusts (or still have an estate plan that contemplates application of a “reduce to zero” formula) that were drafted when the estate tax exemption was significantly lower (and perhaps no more than $1 million). Those plans may provide no estate tax benefit because the client’s estate is under the current exemption levels. Still, these trusts provide an income tax disadvantage because of the possible loss of basis adjustment for the credit shelter trust assets (or assets in a marital trust for which no QTIP election is made) at the surviving spouse’s death. This should not mean that every heir of such a trust has a valid claim against the advisers who recommended the use of a “reduce to zero” formula, though the theory espoused by the plaintiffs in *Raia* might suggest a contrary view. Practitioners who recommended the use of “reduce to zero” formulas did the best they could to address the laws then known and reasonably anticipated at the time the plan was created. If clients heed the advice mentioned above with respect to life insurance policies and periodically monitored the trust, many or all of any adverse results because the plan was premised upon a lower estate tax exemption being applicable might be mitigated. For example, asset location decisions might suppress the appreciation inside the credit shelter trust, and highly appreciated assets might be distributed to the beneficiary before his or her death. Decanting, if feasible, in order to provide a beneficiary with a power of appointment might result in a step up in basis becoming available on the beneficiary’s death. One of the authors regularly suggests to clients that they review their estate plans every year for changes in family dynamics, changes in the law and other circumstances that might affect their estate planning desires and the operation of their current plan. Shouldn’t the damage caused by a client’s failure to heed such advice fall on the client, rather than the planner?

Clients Must Take Responsibility in their Planning

Another disturbing issue underlying *Raia* is that clients bear some responsibility for making sure they understand what they are doing when they implement their estate plan. Shouldn't clients be responsible for understanding that there are risks inherent in any planning and that it is their decision whether to accept those risks? Estate planning professionals should endeavor to make sure that the client understands the estate plan being proposed, and no competent client, who is found to be free of undue influence, fraud or duress, should be permitted later to feign ignorance of fundamental aspects of the plan.

Creating an irrevocable life insurance trust has been a very common estate planning transaction for decades, but if the trust holds a second-to-die or survivorship policy that is no longer needed because of the increase in the estate tax exemption, the client ought not be able to hold the attorney and insurance agent responsible for not having anticipated this growth in the exemptions. That would hardly be reasonable, because it is not the adviser's fault that the estate tax laws changed, or that the client/insured inadvisably lived long enough for that to occur.[xix] The client in that common plan must be charged with and accountable for understanding the basic tax rules that underlie the plan, and the facts that tax laws change, that one's lifespan is unpredictable, and that there are simply no guarantees in estate planning. It would seem that attributing some knowledge to even an average estate-planning client is logical, fair and is commonly done.

Words of Practical Wisdom

Practitioners can practice however they wish, but there will always be the possibility of dissatisfied beneficiaries (and, to a lesser extent, dissatisfied clients), who will want to sue. The plaintiffs may not win, but if they sue, the practitioner loses. Even if the practitioner prevails, he will likely be distracted and upset and it will be hard to carry on a normal life, much less a normal practice. The claim may not only adversely affect the practitioner emotionally, but financially. Malpractice premiums for estate planners are on the rise and a claim (even if covered under a policy) may adversely influence the planner's premiums.

In light of the above, some of the best things a practitioner can do are:

- Don't oversell a technique -- be realistic about the probable success and possible problems.
- Don’t take on a matter unless you can get the client's expectations in line with what you can deliver. When appropriate and desired by the client, once a decision by the client has been made regarding implementation of a plan, especially components of which include an irrevocable instrument, consider whether a discussion with the probable beneficiaries regarding how the plan is presently intended to operate, and sets forth that no plan is fail safe or guaranteed to operate as contemplated, may prove helpful in both providing transparency and establishing reasonable beneficiary expectations. If such a meeting takes place, it may be important to have the client confirm in the beneficiaries’ presence that the plan reflects the client’s desires and for the planner to clarify his obligations run solely to the client and the purpose for the meeting is to assist the client in conveying information which the client wishes the beneficiaries to possess. A practical issue with beneficiary discussions is many clients will not authorize these, many do not wish to incur the fees, and some do not wish their heirs to be informed.[xx]

These recommendations come together under the heading of what some call the “Holiday Inn practice model” -- the “best surprise is no surprise.” Clients and beneficiaries will get used to disappointments that they are expecting; many do not take well to surprises.

Unfortunately, it is not always easy or possible to take the above steps. Clients often have selective memory of what they were told. This is why documented evidence can be important. One also might endeavor to create an environment in which changes might be addressed and surprises avoided (or at least timely addressed), given the constant changes in variables. This may be accomplished, in part, through annual or other timely client meetings. The other advisers on the estate planning “team”, and allied professions, may also need to play a role in assuring that the client takes advantage of these meetings or addresses changes that could adversely affect the plan. Unfortunately, this happens too infrequently.

Additional Estate Planning Practice Considerations

Raia should prompt practitioners to evaluate their practice procedures and consider practice management changes. Some of these are traditional practice management or risk prevention recommendations, while others are new approaches to traditional planning and practice techniques that practitioners may wish to consider:

- Put it in Writing. It is difficult for a practitioner to corroborate verbal discussions. In light of *Raia,*[xxi] practitioners should consider documenting risks that they and their clients might previously not have wished reduced to writing.
- Identify the Client. It might appear easy to identify who the client is in an engagement letter, but doing so with deliberation, forethought and clarity can, in many jurisdictions, limit who will have standing to bring an action and to whom the attorney's duties will run. Proper identification of the client has an array of other implications to protecting the practitioner. With the growing incidence of elder financial abuse and inheritance exploitation, identifying the appropriate client may clarify and even limit the practitioner's liability. For example, it may determine whether a potential heir who contacts the attorney to push the representation (procurement) is treated as a client to whom the attorney owes a duty.
- Address Conflicts. – If the practitioner represents the client engaged in the plan *and* beneficiaries who are or may be impacted by the plan, consider identifying the conflicts that may or do exist, address how such conflicts will addressed, and perhaps consider obtaining written waivers, so that the duties and responsibilities of the practitioner, and how they will be managed, are understood by those concerned.
- Written List of Risk Factors. In the heyday of the tax shelter syndication days (the 1980s), every private placement memo had a long risk factors section in the front of the document. While many of these points were boilerplate in most deals, better-crafted private placement memorandum also had customized risks associated with the particular transaction. Perhaps some practitioners might consider the use of a somewhat generic, somewhat customized, list of risk factors. Giving clients who wish to engage in various estate planning endeavors (such as DAPTs, SLATs, IDGTs, GRATs, etc.) a "Listing

of Some Risk Factors that May Affect Your Plan" might prove helpful. Such a list could also communicate to the client that there are risks involved in every estate plan. No legal or ethical rule requires a practitioner to lay out all of the risk factors in writing, and there may be reasons not to provide the IRS (and perhaps other creditors) with a roadmap as to the purposes and intentions behind an estate plan, but proving that a client was advised of risks, particularly after the client has died or become incapacitated, may be difficult without some level of contemporaneously created documentary evidence.

- Highlight Assumptions in any Illustrations. One might also consider highlighting assumptions that underlie any illustrations that are provided, especially if the illustrations reflect recent changes in the law or anticipate future changes in the law, or an individual client's circumstances. Illustrations are a helpful means of demonstrating the potential impact of specific assumed factors (interest rates, cash flow, etc.) on a plan, but practitioners might consider how allied professions handle similar projections. It is standard practice for wealth advisers, trust companies and insurance consultants to include disclaimers on each page of a forecast and a page or more of express caveats and limitations at the end. Why shouldn't estate planners consider doing the same?

- Clearly Delineate when Representation Starts and Ends. A written confirmation that the engagement has been completed may start a statute of limitations (or repose) and protect against claims brought many years later, such as those raised in *Raia*. Consider having a new engagement letter (and perhaps billing matter number) whenever the client seeks to review or modify the plan. If annual reviews are contemplated under the initial engagement, it is prudent to state that each such review is a separate and distinct service and have a separate engagement letter for each review. Failure to create a clear demarcation of the start and end of the representation may cause continuing services to extend the statute of limitations (or repose). The "last treatment" rule in malpractice cases states that the end of the continuing services, and not the specific event most associated with the injury constitutes the "matters out of which the claim for malpractice arose."[xxii] In *Levy v. Martin*, [xxiii] this rule was applied in an accounting malpractice case, permitting the plaintiff to seek damages relating to tax returns filed over a number of years, because the claim for malpractice did not begin to accrue until the

defendants ceased providing generalized tax services to the plaintiffs years later, even though some of the returns had been prepared many years earlier. Rather than receiving professional advice for a specific problem, plaintiffs were receiving generalized tax preparations services from defendants. These continuing services were held to constitute the matters out of which the claim for malpractice arose. For this reason, practitioners who engage in and recommend annual reviews should consider treating each review as a separate engagement. Of course, one may also note that recommending annual or other periodic reviews points out that no plan can succeed if not properly administered and reviewed by appropriate professionals. That lack of follow up by clients, often those seeking to avoid professional fees, is often the key factor in many plans going awry.

- Use Engagement Letters and Retainer Agreements. Consider revising your standard forms and adding express language cautioning clients that tax laws are uncertain, change with frequency, have varying interpretations and so on. Incorporating these significant and general caveats into standard agreements might enhance the likelihood that a client would have to understand, and could not deny, that no planning result was guaranteed.

A "Risk Factors" memorandum/checklist or illustrations should merely supplement any traditional planning memorandum and letters that practitioners historically utilize, and provide additional and directed caution to clients about risks and issues in their planning and transactions.

Practice Safer Writing

Given the some of the issues raised in the *Raia* complaint, practitioners might consider exercising greater caution and attention to the choice of words and how issues are framed in letters and memoranda. The *Raia* complaint states: "*In this memorandum, Mr. Weinstock stated that the recommendations "are designed to achieve the following planning goals to the maximum possible extent [highlight added].*" Given the litigious environment we face, practitioners may prefer utilizing less definite statements, such as "…may achieve some of the following planning goals."

Practitioners might banish the use words like “assured,” “will,” “optimal,” and “maximum,” in favor of words that suggest only possible, desired or intended results based upon the client’s current circumstances, stated goals and current tax laws (since a clear indication of “intent” may establish a basis for reformation which could thereby negate unanticipated negative tax consequences). Clients no doubt prefer shorter, clearer and more definite language, but the practitioner using such language might assume additional risk. Stating that certain tax savings “might” be achieved clearly implies that they also might not be achieved.

Given the technical nuances of the modern tax laws and the ongoing changes in those laws, not only by acts of Congress but also by new administrative and judicial interpretations, little should be assured as a future result.

Engagement Letter/Retainer Agreement Considerations

The complaint against the accounting firm in *Raia* included the following:

> *Prior to the execution of the letter on behalf of Raia Properties Corporation by Jim D' Aiuto, Lawrence C. significantly modified it, via initialed handwritten interlineation, striking out a portion of the letter relating to whether J.H. Cohn could use Raia Properties' name and contact information in marketing materials. Accordingly, the letter executed by Mr. D' Aiuto was not the same agreement that previously had been executed by Ira S. Herman. Therefore, the engagement agreement of March 20, 2012, is not a binding contract in any respect upon any plaintiff, since there was no meeting of the minds and because the parties to the agreement signed different agreements*.

Crossing off a marketing authorization that permits use of a firm or client’s name might be viewed as tangential or even superfluous to the remainder of an engagement letter, but is it a sufficient basis for negating the entirety of an agreement?

Whenever a client makes changes to an engagement letter, the practitioner might consider whether to engage with the client at all. If the engagement will proceed, it might be advisable for all parties to initial the changes or perhaps create a new engagement letter. A practitioner who proceeds after a client has made changes to the engagement letter, and a client who has

paid pursuant to the terms of the engagement, generally reflects offer and acceptance, as well as reliance by both parties on the modified terms and conditions of the engagement.

Another approach could be to state in the engagement letter that if a client modifies any term, the remainder of the agreement when signed shall be binding, but that the modified provisions do not bind the professional unless he or she expressly agrees in writing to the change by initialing it. The engagement letter might further provide that if a change is made it doesn't affect the remainder of the agreement.

Engagement Letter/Retainer Agreement Additional Provisions

Practitioners might wish to include in their retainer agreements language confirming that there are risks with all plans and that all possible risks are not enumerated. Consider:

> **No Guarantee/Risks**: Results of any plan aren't guaranteed. Aspects of many estate and related plans are uncertain and could be subject to a wide spectrum of different views by other advisers, the courts, the IRS, and other authorities. Most strategies have negative consequences (e.g. save estate tax but lose basis step-up). Many common strategies, techniques and transactions are subject to tax as well as other legal, financial, and other risks and uncertainties. While we endeavor to identify some of the risks of a plan, all risks and issues with each component of a plan may not be possible to identify or advisable to communicate in writing. Creating a collaborative team may help identify more issues. Further, the fact that we communicate verbally or in writing certain risks should never be interpreted as an indication that any such listing or communication is a comprehensive listing or communication of every risk involved. The risks of any transaction can be further compounded by: improper administration of the plan, a failure to regularly review and update the plan in order to address changes in the tax and other laws that may reduce hoped for benefits or even result in more costly results then had no planning been pursued as well as the potential implications of changed goals, desires and family and business dynamics and objectives. Annual or other meetings with a collaborative advisor team may help identify existing or new risks and help to identify provisions of the plan (or its administration) that may be beneficial in addressing changes in the

> law and mitigation of risks, but even such vigilance will not provide certainty. A failure to regularly revisit and evaluate the plan, with the assistance and input of a collaborative team of advisers, may have adverse consequences and result in your plans not meeting your estate planning objectives.

Practitioners might also wish to include in their retainer agreements language that confirms that tax audit risks exist with all plans and that the client will be responsible for the costs of such an audit. Consider:

> **Audit and Other Risks**: To the extent that you engage us, or engaged us in the past, to perform tax, estate, asset protection and other planning, which may include, or may have included, estate, gift, wealth preservation and/or wealth transfer planning and other services, we may have suggested a number of strategies, and may have assisted in implementing strategies, that the IRS or state tax authorities, or others, might challenge. Possible challenges could be asserted even though we communicated several of the risks associated with such strategies and despite such strategies having been formerly recognized as acceptable techniques. Possible challenges could be asserted also for risks that were not discussed, including challenges by the government that could cause inclusion in your taxable estate of assets previously transferred out of your estate. Assets transferred out of your estate as part of a recommended strategy will likely not be adjusted to a date of death value and could result in the imposition of capital gains tax, possibly a depreciation recapture tax, and/or a negative capital account recapture liability. You agree that we shall not be liable, to any extent, for any assessments of tax, interest, or penalties resulting from the implementation of any recommended strategy.

Billing

Practitioners may wish to add some variation of the above "no guarantee" and "audit" provisions to their bills, perhaps as a standard footer to all bills. Many common billing programs permit adding standard text as footers. Claims by clients reminded of these limitations on each bill (especially if they pay the bill without objection), may be limited when those claims are

premised upon allegations they were unaware of these risks and limitations.

Caveat to All Memoranda

Generally, financial firms, trust companies, wealth advisers, and life insurance firms don't issue a forecast, memorandum or other client specific communication without cautionary language. Perhaps it might be advisable for the same procedure to be utilized routinely by estate planning attorneys and CPAs. Clients rarely authorize an unlimited budget for a memorandum, so time and budget are factors constraining virtually every legal or accounting memorandum. Cost constraints assuredly limits the issues that may be identified and the research that can be done. Given the inherent uncertainties of the estate planning process, many memoranda simply won't provide assurance or address every point. The *Raia* complaint arises from clients who claim some uncertainties and limitations were not communicated. Therefore, it is advisable that practitioners endeavor to confirm, in some form, that they've informed the client that risks exist, but that not all can be identified and that no assurance as to results can be provided.

It is impossible to delineate every possible adverse event that might result from a proposed strategy, because many will result from future changes in the law that one could not reasonably anticipate. No one can foresee every possible issue and few clients would pay the cost for the depth of analysis that would be required in an attempt to approximate a comprehensive listing of future potential changes and ramifications. Nonetheless, depending upon the type of plan or transaction envisioned (and the size of the same) a longer listing of such issues than may have historically been provided may be appropriate, in light of *Raia*.

Practitioners might also add a paragraph on risks and issues to cover letters used to transmit wills, trusts and other significant estate planning documents. That paragraph might address:

1. Estate planning is inherently complex, subject to varying interpretations, and laws that frequently change.

2. The manner in which a plan is implemented (e.g. how assets are titled or the assets utilized in funding) can have a significant impact upon the plan.

3. Ongoing review and maintenance of every plan, the assets held, and documents is essential.

4. There is no assurance that any particular result will be realized.

5. There are risks and negative consequences to every planning step and technique, not all of which have been enumerated in this letter or other communications.

6. By proceeding with this plan, you accept these risks.

Consider the following language for possible inclusion in estate planning memorandum:

Statements and Risks

Limitation to Client: This Planning Memorandum is solely for the benefit of *name of client* and is not to be relied upon by anyone else without the written consent of *name of firm*. We assume no responsibility for income tax, gift tax or estate tax, or any other consequences, to any other persons. All other persons should consult and rely upon their own independent legal counsel and other advisors. Except for the information expressly stated herein, no other suggestions, information or analysis is implied, and no other suggestions, information or analysis should be inferred. Any strategies suggested are intended solely for the use of the client named above, and cannot be relied upon by others. Any strategies suggested merely represent options for the client's consideration and are not an expression of opinion that the client should engage in the transaction. The decision to proceed with implementation of any transaction or plan is within the sole discretion of the client and it is the client's responsibility to let *name of firm* know if the client requires further explanation or doesn't understand any provision or aspect of the plan, so that further explanation can be provided.

Matters in Purview of other Advisers: Although we may address certain income tax consequences, those matters are also within the purview of your CPA and should be addressed as such. Although we

may address certain insurance matters or investment matters, those matters are within the purview of your insurance and/or investment adviser, and should be addressed as such. Although we may address certain real estate or corporate (entity) matters, those matters are within the purview of your general counsel (or your specific real estate or corporate counsel) and should be addressed as such.

Information Will Not Suffice to Avoid Tax Penalties or Interest Charges: The information in this memorandum, in any attachment, or cover letter (including previous and subsequent correspondence during this engagement) is not intended or written to be used, and cannot be used to: (1) avoid any penalties imposed by the IRS or any state tax authority; or, (2) promote, market or recommend to any other party any tax-related matter such as an investment, product, service, advice or position.

Scope Limitations: The scope of this memorandum is expressly limited to the strategies or matters discussed herein. No other issues are considered and *name of firm* assumes no responsibility beyond the issues to which this memorandum is devoted. Additionally, no analysis is provided on any of the following: (1) any impact of future legislation or other changes in the law, whether retroactive in nature or not; (2) any issues specifically excluded; (3) non-US taxes or taxes in jurisdictions not specifically mentioned; (4) any taxes not specifically mentioned; (5) life insurance or other insurance selection; (6) recommendation of investment products, securities or strategies; (7) Medicaid, elder law, supplemental needs or special needs planning; (8) qualified retirement plan issues; (9) annuities; (10) valuation reports or issues; and, (11) other matters excluded under the engagement or pursuant to another communication.

Law Changes: The suggestions and discussions in this memorandum are based upon information provided by the client and applicable federal, state and local tax and other laws as of the date of this memorandum. Such authority will almost certainly change in the future, and such change may be applied retroactively. A change in state law may affect income, estate or other tax consequences. *name of firm* assumes no responsibility to update this memorandum or notify you of such changes in the law. Federal and state taxing authorities, regulatory agencies, the IRS, and the courts are not

bound by the analysis contained herein and may have different views or interpretations of the law, the facts or both. The analysis contained in this memorandum supersedes all prior oral and written discussions, if any, pertaining to the issues involved, but may be modified by subsequent communications. We may have suggested a number of strategies the IRS or state tax authorities, other governmental agencies, regulatory bodies or courts may challenge. While we have discussed a number of associated risks with you, possible challenges could be asserted which were or were not discussed or even contemplated. We are not responsible or liable, to any extent, for any gift tax, income tax or estate deficiencies or assessments, interest, or penalties that may arise, or the results of any court holding, including, but not limited to the piercing or disregarding of entities, trusts or transactions. There may now be proposed Federal, state tax or other legislation which, if enacted, or regulations which if promulgated, could modify or eliminate the benefits of strategies if not grandfathered. The IRS, state tax authorities, and may attack various strategies and techniques that are suggested in this memorandum.

Your Responsibilities: We have relied upon your assertion that the information provided, facts and assumptions provided are true, correct, and complete. We have not audited or otherwise verified the information, facts or assumptions you provided, even though we may have asked for clarification, done internet or other searches or consulted with your other advisers. A misstatement or omission of any fact or a change or amendment in any of the assumptions we have relied upon may require a modification of all or a part of the discussions or suggestions contained in this memorandum. In addition, our suggestions and discussions are based on the facts and assumptions as asserted to us by you and are only applicable as of the date of this memorandum. It is your responsibility to engage *name of the firm* or another adviser to revisit these matters from time to time, especially if your circumstances change or our general communications or other sources suggests a change in the law, planning approaches or perspectives that might affect you, your planning or the discussions or suggestions in this memorandum. It is also your responsibility to consider all communications we disseminate, information obtained from other sources, as well as general media coverage of events and contact us (or another adviser)

should you become aware that any such change might apply to you, your planning or this memorandum.

Options; Your Decision: Although we have endeavored to aid you in the decision-making process, suggest alternative recommendations verbally or in writing in an attempt to help you achieve your objectives, and assist you in determining how each alternative might meet your estate planning objectives; the responsibility for estate planning decisions is solely yours. These services are not designed, and should not be relied upon, as a substitute for your own judgment, nor do they mitigate the necessity of ongoing review. These services are designed to supplement your own planning and analysis and aid you in achieving your objectives.

Additional Practice Measures to Consider

It is too soon to predict the outcome *Raia*, but there are important lessons to be learned. Some practitioners dismiss this case as an aberration and predict it will be dismissed or settled. The more prudent practitioner, however, will use *Raia* as an opportunity to consider the toll on any practitioner embroiled in a malpractice case -- the loss to time, reputation and earnings even if claims are proven baseless. These costs are incredibly high, and the question becomes what practical things a practitioner might do to reduce the risk of being similarly situated to the defendants in *Raia*.

No doubt, some will dismiss the suggestions below as extreme or unwarranted. They may believe that clients will be put off and not wish to proceed. A client who is put off by being informed of the risks inherent in estate planning generally, and of the transactions they are considering in particular, probably should not proceed with the planning. An attorney loses little when he or she loses a client who has unreasonable expectations or believes a proposed plan will remain the best possible plan regardless of how the law, the economy, and the client's situation may change. This does not change merely because the client is wealthy.

A practitioner who feels the suggested steps are excessive might wish to consider the far more restrictive limitations that allied professions typically put on their work. Often, the estate-planning attorney is one of the few

advisers whose liability is not expressly limited to his or her fees. In light of the desire of clients always to seek the deepest pocket to sue, a mere disclaimer informing a client of risks is not an extreme addition to a planning memorandum.

Other Lessons for Practitioners

Again, the example of how good tax shelter private placement memoranda were prepared before the Tax Reform Act of 1986 may provide a format for improving communications with clients regarding the potential risks involved in an estate planning strategy. For example, assume that a client creates a simple irrevocable non-grantor trust to salvage a charitable contribution deduction in light of the new higher exemptions. It is not only the trust instrument that determines whether the terms of the trust meet the governing instrument requirements, but also its administration; are donations paid currently and out of income in a manner that comports with Section 642(c)? The practitioner may not be advising the trustee, but the practitioner can warn the client that these factors are important and must be overseen by someone.

Practitioners might wish to send many clients a Risk Factors" memorandum, many of which could be generic (determined by the specific transactions suggested), but each of which is could be moderately tailored to the client's specific situation. It is advisable that any such checklist or memorandum be marked "Attorney Client Privilege" when sent by counsel. The implications of *Raia* are also relevant to CPAs, wealth planning and other advisors, and communications with such advisors are not always afforded such protections. Clearly, such a memorandum can't include every possible risk, but it can clarify that the transaction involves numerous risks and uncertainties, as most transactions do. Educating clients as to the uncertainty of the tax and legal system, and hence the uncertainty of any predicted planning result, is a point that we as a profession have not historically focused on, and in the wake of, may wish to now endeavor to do.

Some risk factors to consider disclosing might include:

> 1. Absent further action, assets transferred to irrevocable trusts may not be included in the transferor's gross estate and if not

included in the grantor's estate afforded a new adjusted basis at the grantor's death.

2. A power of substitution in a trust that is not monitored and exercised at the right time may not achieve the optimal basis for income tax purposes at the grantor's death.

3. Powers of substitution are inherently risky. If the valuation of the assets swapped or substituted is not identical, the IRS may challenge the transaction. If a swap power substituting assets is exercised in a manner that can shift benefits among the trust beneficiaries it may trigger tax problems.[xxiv] When a power of substitution is exercised in a manner that changes who ultimately receives an asset (such as a closely held interest), some of the goals and estate planning objectives of the grantor may be thwarted and it may trigger estate tax inclusion.

4. Several tax cases have expanded the risk of estate inclusion of assets where the decedent "in conjunction with" others could control the use or enjoyment of the assets or its income. The scope and reach of these cases is still unclear, but it could potentially be very broad.[xxv]

5. An irrevocable grantor trust under Section 673 *et sec* may not be taxed as part of the grantor's gross estate for estate tax purposes, but the trust income will be taxed to the grantor during his or her lifetime. Such treatment enhances the transfer tax savings of the trust, but it can deplete the grantor's estate over time and possibly cause cash flow and other financial hardships.

6. Grantors who seek to toggle off grantor trust status, even if expressly authorized by the trust instrument, may face objections and even litigation from the trustee and beneficiaries, who prefer that the grantor continue to pay the taxes. Such litigation can be very expensive.

7. The attorney only represents the grantors in this matter and not the current or future beneficiaries or the fiduciaries.

8. Provisions within an irrevocable grantor trust that provide for the potential reimbursement of income tax consequences incurred by the grantor due to the trust's grantor trust status, are subject to the exercise of the Trustee's discretion. There is no guarantee that that

discretion will be exercised in grantor's favor, as the Trustee's fiduciary duty will generally be owed to the beneficiaries of the Trust.

9. The attorney recommends that the client have a forensic analysis done to corroborate that the transfers to the trust aren't fraudulent conveyances, but the client has elected not to do so.

10. The attorney recommends that the client have an actual life analysis conducted with regard to each grantor by an independent actuarial firm, to document estimated life expectancies based upon the grantor's actual health and lifestyle factors, as opposed to reliance on standard life expectancy tables (which are often out of date from their inception). This may be relevant to having the IRS respect various components of the transaction, such as the validity of any promissory notes and the length of the trust terms.

11. The client is advised not to hold any power or control over entities held by the trust with regard to decisions to make distributions or to liquidate or sell underlying assets, because retaining such powers, whether officially or informally, could have an adverse impact upon the effectiveness of the plan.

12. We are admitted to practice only in [list jurisdictions] and have relied on local counsel for advice about the law in other jurisdictions, to the extent applicable.

13. A gift tax return must be filed adequately disclosing all aspects of any gifts or other irrevocable transactions or the statute of limitations on an audit and tax deficiencies will not run.

14. Gift tax returns may need to allocate GST exemption [or opt out of automatic allocation]. The attorney is willing to prepare or review these returns, but cannot take any responsibility for returns that the attorney neither prepares nor reviews.

15. Defined value mechanisms used in the transaction to deflect a valuation challenge by the IRS may not be respected by the IRS. The IRS has challenged these and may again do so, though some forms of these mechanisms have been sustained by various courts.

16. You should always expect a gift tax audit. While an audit doesn't always occur, when it does it will entail significant additional professional fees none of which are included in the fees billed to date and a separate engagement for such services accompanied by additional fees will be required. In anticipation of an audit, we have

suggested that assets be formally appraised; you have elected not to do so. An audit may require the involvement of (additional) appraisers, litigators, and others and the failure to supply an appraisal may have an adverse effect on your ability to defend the gift tax return (or a charitable deduction). The result of an audit can be costly and unpredictable. While you should always expect a gift tax audit, again not all returns are audited. Sometimes you get lucky.

17. GRATs must be administered precisely in accordance with the regulations, including but not limited to the proper payment of the periodic annuity payment and not making additional gifts to the trust after its initial funding. The IRS may argue that a spillover of value into the GRAT as part of a defined value mechanism is a second prohibited contribution and not respect the defined value mechanism or the GRAT. We will not monitor or record such payments unless you request in writing that we do so and sign a new retainer agreement to that effect; consequently, you or another adviser must do so.

18. The IRS may not respect the use of an incomplete gift trust as part of a defined value mechanism.

19. The terms of notes in installment sale transactions must be adhered to strictly; interest must be paid in accordance with the terms of the note. We will not monitor or record such payments unless you request in writing that we do so and sign a new retainer agreement to that effect; you or another adviser must do so.

20. The value of assets may not increase as anticipated undermining the goals for the transactions.

21. If you die while your grantor trust owes you part of the sales price under an installment sale transaction, the IRS may argue that the remaining gain on that note is includible in gross income on death. Many commentators disagree with this position and there is nonbinding precedent to the effect that death is not a recognition event, but there is no assurance how an audit of this might conclude.

22. If you transfer negative basis real estate to a grantor trust, any cessation of grantor trust status during your lifetime might trigger taxable gain.

23. If you transfer negative basis real estate to a grantor trust, the IRS may argue that the cessation of grantor trust status upon your

death triggers taxable gain. Many commentators disagree with this position, but there is no assurance how an audit of this might conclude.

24. The IRS could challenge the valuation of assets and any discounts claimed, even though you have one or more independent professional appraisals. The IRS almost certainly will challenge such valuation and discounts if you do not have at least one or more independent professional appraisals.

25. The tax laws are almost guaranteed to change during the course of your life and/or these transactions and it is impossible to anticipate how those changes may affect your planning. We will be happy to discuss any such changes in the law, but such discussions are a new engagement and require a new retainer agreement, and we have not undertaken the obligation to keep you abreast of changes in the law even if we send you periodic communications, such as newsletters or email blasts. This is one reason why we suggest that you consider and you initiate periodic reviews of your estate plan.

26. Family dynamics, such as your relationship with various family members and the capacity of various family members to handle financial and business assets, can change, and those changes may render parts or the entirety of a plan undesirable or less than optimal.

27. You may wish to inform all heirs of the overall nature of the plan so that they understand the trusts involved and the potential impact on any future inheritance. We strongly urge that, if you wish to do so, you schedule a meeting with the heirs and your attorney in which the plan and its risks and expected benefits can be accurately discussed. Such a meeting is a new engagement and requires a new retainer agreement with you as the client.

28. As you acknowledged in our engagement letter, we are not guarantors of results. All the planning undertaken faces an array of tax, legal, and other risks. We do, however, promise to use our very best efforts to provide you with options which endeavor to meet your estate planning goals and answer any questions you may pose (in light of current law and your present circumstances) to the best of our ability.

29. There are other risks and issues that we have not identified in this partial listing. This listing is not intended to supplant or otherwise

undermine other verbal, email, and written communications we have provided during the course of the engagement that identify additional risks and considerations.

Clearly, informing clients that the outcome is not fully predictable puts them on notice that they assume some level of risk, and that risk is inevitable with estate planning. The planner is not a guarantor of outcome, but rather a professional who attempts to integrate the client’s stated desires with available options selected by the client, just as the client would determine for any other business endeavor or decision. Therefore, caution on the part of the client is still in order.

While a general risk factor listing is helpful, it is not a substitute for a client specific letter or memorandum, especially when specific risks are identified but aren’t delineated in generic communications.

Limitations Allied Professionals Incorporate into Their Retainer Agreements

A complex estate plan for a wealthy client generally involves a planning team consisting of the attorney, CPA, appraiser and wealth adviser. The attorney generally won’t be able to limit his or her liability, under the rules governing attorney ethics.[xxvi] The CPA and appraiser, however, may impose stringent limitations on their liability; they may limit the dollar value of their liability to their fees earned, or perhaps even just to a portion of the fees involved. These other professionals might also be able to limit the period during which a claim can be brought, providing them with further protection. The wealth adviser may attempt to limit its liability by stating clearly that it does not provide legal or tax advice thereby perhaps shifting the burden back to the attorney and CPA (with the CPA but not the attorney having the ability to limit its liability to the fee it earns).

A trust company involved in a directed trustee capacity may be able to limit its liability to cases of bad faith or reckless indifference to the purposes of the Trust or the interests of the beneficiaries.[xxvii] Willful misconduct is more than no liability as the absence of any liability might negate the existence of a valid trust. However, willful misconduct is something less than good faith. Providing willful misconduct is a high burden.

\The point is that the estate-planning attorney may be the only person who has not, and may not, limit personal liability. This can be inherently unfair and inappropriate, but it generally represents the current state of the law. Perhaps it is time for the profession to reconsider these rules especially in light of what appears to have become the norms of practice for most other allied professions.

Consider the following language similar to that used by some appraisal firms:

> **Sample clause**: Our sole obligation is to correct any non-conformance with the services provided, but only if you give us written notice within 24 months after the services are performed. The notice must specify and detail the non-conformance and, if you and we agree that a non-conformance exists, we will have a reasonable amount of time to correct the non-conformance. You agree that our total liability relating to the professional services provided shall not exceed an amount equal to the fees we receive for the engagement, and will not include any special, consequential, incidental or exemplary damages or loss, lost profits, or lost business opportunity.[xxviii]

A Caution to Financial Advisers, Wealth Advisers and Trust Companies

The state of the wealth management industry has evolved but perhaps not all practices have kept pace with that evolution. That creates risks that some in the industry may not have fully evaluated. *Raia* alleged the following with respect to the wealth advisers involved:

> *We note, pursuant to Rule 4:5-1(b), that entities other than the defendants named here and …were involved in rendering related advice and in related conduct. Such persons are …The Private Bank, J.P. Morgan. However, it is our view that their involvement was such that they should not be made a part of this lawsuit.*

Regardless of the outcome of *Raia*, the mention of the wealth adviser in the complaint should cause concern to wealth advisers, financial planners, and similar professionals. It is not uncommon for wealth advisers and trust

companies to indicate that they provide comprehensive planning advice. Consider the following from a major firm's website:

> *Estate Planning & Trust…How can you turn your dreams into a tangible plan of action that incorporates all aspects of your financial and personal life? See how our estate planning and trust services can help you accomplish your many goals….Planning for the future…Our planning services are fully integrated to meet your many objectives…Estate planning and strategic wealth transfer…Let us help develop a plan to efficiently transfer wealth to your heirs and favorite charities, protect your family and business, grow your assets, and minimize taxes.*[xxix]

It is uncertain whether a wealth adviser who advertises that it provides comprehensive financial and estate planning services can really avoid responsibility for the types of claims set forth in *Raia,* particularly when the wealth advisor serves as the trustee of one or more of the trusts involved in the plan, has in house attorneys who review the trust instruments involved in the transaction, provides standard clauses it requires be inserted into the governing instruments, has a financial adviser review the plan, and does financial forecasts that address the plan), and is integral to the financial underpinnings of the plan. As more wealth advisers provide broader and deeper services that overlap the tax planning of CPAs, the estate planning provided by attorneys, etc., the risk they face may also commensurately increase. Therefore, the recommendations offered in this article may also be applicable to wealth advisers. Wealth advisers might consider:

- Adding to the caveats and limitations that accompany reports and memorandum.
- Following up on meetings with written summaries containing disclaimer language rather than relying on what cautions were verbally stated at a meeting.
- Providing clients with planning risk factors to educate clients as to the fact that risk is inherent in all estate plans.
- Encouraging clients to meet periodically with all members of their advisor team, not just the wealth adviser's internal team, in order to have the team as a whole assist in identifying and addressing risk factors and corroborate that the other advisers, not just the wealth adviser, are regularly involved in the planning and administrative processes. If wealth advisers do not provide tax and legal advice,

then encouraging (perhaps insisting) that clients meet with their entire advisor team annually may be a useful means of demonstrating that the tax and legal advisers were in fact involved and reliance solely on the input of the wealth advisor didn't occur.

It would be beneficial to the client, and their ability to understand and analyze risks, to have meetings with the client that include all of the professionals involved in creating, implementing and monitoring the plan. This should include the client's financial advisors, counsel and CPA, and any other professionals deemed relevant to the process. Such meetings, when conducted at regular intervals, may identify issues as they arise and provide options for proactively addressing them. Moreover, it is not uncommon that no single member of the team will have all the information pertinent to a strategic plan or analysis. Collaboratively approaching these issues helps to facilitate members of the team sharing pertinent information.

Might Arbitration Provide an Option?

In light of the disproportionate risks borne by estate planning attorneys, should including a mandatory arbitration clause in engagement letters be viewed as a possible option?[xxx] Apart from whether mandatory arbitration is legally or ethically permissible, the preliminary threshold questions should be whether it is feasible, and if so, would it help. The answers are not at all clear. Moreover, when such provisions are included, consider how the client will react when you advise them that they should seek independent counsel before executing an engagement letter that contains a mandatory arbitration provision.

Several litigation attorneys advised that they viewed arbitration as ineffectual and not a preferable approach to mitigate liability exposure for estate planning attorneys. Others disagree. Some believe that arbitration may provide quicker resolution at lower cost.

State ethics rules sometimes also proscribe the inclusion of a mandatory arbitration provision in their client retainer agreements. In a New Jersey case, *Darcy Smith, Ph.D. v. Cynthia Borsella Lindemann, Esq.,*[xxxi] on the enforceability of an arbitration clause for a malpractice claim in a retainer agreement, the court stated:

Darcy Smith, Ph.D., hired and fired a string of four lawyers in connection with her divorce. She later sued in the District of New Jersey all four attorneys and their respective law firms for malpractice. Three settled, but one attorney, Marc A. Calello, asked the District Court to enforce an arbitration provision in his representation agreement with Smith. The District Court obliged, staying Smith's action and compelling arbitration. Smith contends that the provision is unenforceable because New Jersey law does not permit the arbitration of malpractice claims against attorneys brought by their former clients, and, even if New Jersey law did permit arbitration of her claims, this provision fails because it does not specifically use the word "malpractice." Accordingly, she asks us to reverse the District Court or, in the alternative, to certify to the Supreme Court of New Jersey the question whether arbitration provisions like the one in her agreement are enforceable.

Some of the language used by the attorney in that case is reproduced below, and might be of interest to practitioners seeking this avenue of protection:

Arbitration of Differences between the Client and the Law Firm. Should any difference…, disagreement, or dispute between you and the Law Firm arise as to its representation of you, or on account of any other matter, you agree to submit such disagreements in binding arbitration. Signing of this Agreement will be deemed your consent to the methods of alternative dispute resolution set forth in this Section, and constitutes a waiver on your part and on the part of the Law Firm to have such disputes resolved by a court which might include having the matter determined by a jury.

The legal issue with using a mandatory arbitration clause is that the ethical rules governing attorneys in many jurisdictions, including in New Jersey where the above case was litigated, prohibit mandatory arbitration clauses.

The [Federal Arbitration Act ("FAA")] federalizes arbitration law and 'creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate[.]'" John Hancock Mut. Life Ins. Co. v. Olick, 151 F.3d 132, 136 (3d Cir. 1998) (quoting Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 25 n. 32 (1983)). Thus, as the Supreme Court has repeatedly reaffirmed,

"'[w]hen state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA.

***

The Court did explain that for the arbitration clause to be binding the client must be "fully apprised of the advantages and disadvantages of arbitration" and "give her informed consent" to the arbitration provision. ABA Comm'n on Ethics & Prof'l Responsibility, Formal Op. 02- 425 (2002).

Thus, practitioners should make sure that if they are going to include a mandatory arbitration clause in their client agreements, the agreements includes the language necessary to provide clients with sufficient information so that the client can provide informed consent and reflects they were advised of the impact of waiving their right to have their claims resolved by a court.

Attorneys should also confirm with their malpractice insurance carriers before adding an arbitration clause to their attorney-client agreements. Some carriers may bar such clauses in their insured's attorney-client agreements. However, one carrier responded: "The insurance company responded to your query on adding an arbitration agreement to your contracts and advised this is acceptable."

An illustrative arbitration provision contained in an attorney malpractice policy follows:

The Insured shall follow the Company's direction regarding whether to accept or reject a demand for arbitration of any Claim, and shall not voluntarily agree to arbitrate a Claim without the Company's written consent. No Insured shall, except at the Insured's own cost, make any payment, make any admission, admit liability, waive any rights, settle any Claim, assume any obligation or incur any expense without the prior written consent of the Company. All Insureds agree to tender any Claim covered by this Policy to any other insurers or indemnitors which may provide defense or indemnity coverage for such Claim.

The carrier whose policy contained the above referenced language advised that the purpose of that clause is to ensure that the claim is timely reported and all investigation/discovery is performed prior to the matter going to arbitration. The carrier didn't believe that this clause should be interpreted to prevent an insured from including a Mandatory Arbitration clause in a Scope of Engagement letter, as Arbitration is typically a good way to reduce defense costs and get a quicker resolution. However, just because one carrier interpreted such language in this fashion doesn't mean all other carriers will. A downside of arbitration generally is that decisions typically can't be appealed.

The *Smith*[xxxii] case had another interesting point apropos to the suggestions in this article with regard to written documentation of caveats, risk factors, and limitations on the scope of what an estate planning representation will provide:

> *Smith contends she could not have given her informed consent to the agreement unless Calello orally warned her that she would have to arbitrate any malpractice claims against him. And there is no evidence that he gave such a warning*.

The unfortunate lesson for practitioners is that the effort to document many issues, risk factors, and limitations may be the best evidence available to protect the practitioner from claims by the client that they were not informed of those matters.

Conclusion

The outcome of *Raia* is uncertain, but it may provide cautionary lessons to estate planners in all disciplines. The cost and disruption of suits like this can be horrific, even if the practitioners challenged are victorious. In smaller firms, they could be financially devastating. The harm to a practitioner's or firm's reputation, even if they ultimately prove no wrongdoing, can be incredibly detrimental.

These types of challenges may be deflected, in some instances, by some of the cautious practices suggested above, but it is possible that in *Raia*, the practitioners involved indeed documented their file with memoranda and other communications well beyond what most clients in smaller estates might be willing to pay for. Therefore, the reality for many practitioners is a

catch-22. One should consider taking those steps deemed feasible to protect oneself from claims, which may include better informing clients of the risks of estate planning and documenting the provision of such information. The extent and manner by which the practitioner provides such disclosures may need to be weighed against the risks involved and the fee that may be charged with regard to the engagement, as one also has to earn a living and cannot possibly afford to take all of the steps that they might wish to take. Liability should not be imposed where the practitioner's conduct meets the standard of practice. This is why it may be important that the law recognize the inherent uncertainty and risks associated with estate planning.

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Martin Shenkman
Sandra Glazier
Howard Zaritsky

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CITATIONS:

[i] *Raia v. Lowenstein Sandler LLP and Eric D. Weinstock*, Superior Court Of

New Jersey Law Division: Civil Part Bergen County, Docket No. Ber-L- , 02/01/2019 (“Raia”).

[ii] Howard Zaritsky, Esq. is a retired estate planning attorney in Rapidan VA, Sandra Glazier is an equity shareholder in Lipson Neilson, P.C. in its Bloomfield Hills, MI office. Martin Shenkman, Esq. is an attorney in Fort Lee, NJ.

[iii] *Raia v. Lowenstein Sandler LLP and Eric D. Weinstock*, Superior Court Of New Jersey Law Division: Civil Part Bergen County, Docket No. Ber-L- , 02/01/2019 (“Raia”).

[iv] *Raia v. Cohn Reznick LLP*, Superior Court of New Jersey Civil Division, Bergen County, Docket No.: BER-L- -2018.

[v] See. *Radtke v. Miller, Canfield, Paddock & Stone*, 453 Mich 413, 424 (1996).

[vi] *The Meyer and Anna Prentis Family Foundation v. Barbara Ann Karmanos Cancer Institute,* 266 Mich App 39 (2005), quoting *Vicencio v. Ramirez,* 211 Mich App 501, 508 (1995).

[vii] In some states, this type of cause of action may only be brought by the grantor or the grantor’s estate. In those jurisdictions the issue of standing might result in a dismissal of the action. Nonetheless, the issues raised by *Raia* remain relevant considerations for estate planners.

[viii] Plaintiffs claim they were clients of defendants. However, whether they were “clients” under this particular engagement remains unclear. Regardless of whether a compensable duty ran to these beneficiaries under the circumstances presented, the issues raised remain important in analyzing practices which practitioners may wish to consider, in defining the scope of the engagement, the client, duties and waiver of potential conflicts of interest.

[ix] “…[D]*efendants rendered negligent estate-planning and related advice to the plaintiffs, such that the plaintiffs have been harmed and are at imminent risk of further harm.”*

[x] “*The defendants negligently failed to conduct a proper analysis of the risks and benefits of the estate plan they formulated for the plaintiffs, and negligently failed to apprise the plaintiffs of the risks inherent in conveying the plaintiffs’ real estate ownership interests into dynasty trusts*…”

[xi] “5 *The defendants failed to determine, and failed to alert the plaintiffs,*

that conveying certain interests in real estate into dynasty trusts could eliminate the plaintiffs' ability to transfer assets with a "stepped up" basis, trigger phantom gains that create tax liabilities, cause losses relating to eliminating the depreciation reset of assets, and cause other damages."

[xii] "6. *The applicable standard of care requires that defendants know and apprise the plaintiffs of the consequences of the advice defendants provide and the implementation of that advice. Nonetheless, Mr. Weinstock and the Lowenstein firm failed, over a period of years, during the course of meetings, correspondence and telephone conferences with the plaintiffs, to appreciate these consequences or to advise the plaintiffs of them. This was a breach of the applicable standard of care, which was the proximate cause of damages to the plaintiffs…"*

[xiii] "8. *When the "switch is flipped" on the dynasty trusts, grantor trusts are changed to complex trusts. When this occurs, either voluntarily or through the death of the grantor, the alter ego status between the grantors and the trusts is severed. This eliminates the ability for the grantors to swap assets in and out of the trusts without penalty, and creates a phantom gain tax liability. This results in substantial adverse tax consequences*."

"9. *Because Lowenstein advised the Raias to place their real estate partnership interests into dynasty trusts, these assets in trust will not be deemed to be part of their respective grantors' estates when the grantors pass away. As a consequence, the assets will not be treated with what is known as "stepped up" basis*.

[xiv] "*The years 2012 through 2016 were years of transition for the Raia family business. The family discussed these changes during family retreats and in other contexts. The business was in transition from a regional real estate entity to a national investment management platform. Lowenstein* ***marketed its estate plan*** *to the Raia family as an integral part of this transition [highlight added]*."

[xv] *Wandry v. Comm'r*, 103 TCM 1472, TC Memo. 2012-88.

[xvi] *Estate of Powell v. Commissioner*, 148 T.C. No. 18.

[xvii] *J. King v. United States*, CA-10, 76-2 USTC ¶13,165, 545 F.2d 700 (10th Cir. 1976).

[xviii] *Comm'r v. Procter*, 142 F.2d 824 (4th Cir. 1944), cert. denied, 323 U.S. 756 (1944).

[xix] Clients may be faulted for failing to do those things that they have been told must be done in order for the estate plan to succeed, but failing to die quickly is not really one of the things for which the client should be justly criticized. Few clients are willing to die early just to save estate taxes, despite the fact that they claim that having to pay these taxes may affect them fatally.

[xx] The timing for such meetings can be important. This is because knowledge of the terms of a plan (before implemented) may be utilized as an indicia of procurement, which can be a factor leading to the imposition of a presumption of undue influence.

[xxi] See also *Darcy Smith, Ph.D. v. Cynthia Borsella Lindemann, Esq*., US Court of Appeals 3rd Cir., No. 16-3357, Sept 21, 2017.

[xxii] See *Levy v. Martin*, 464 Mich 478, 489 (2001).

[xxiii] *Id*.

[xxiv] See Revenue Ruling 2008-22.

[xxv] *Estate of Powell v. Commissioner*, 148 T.C. No. 18.

[xxvi] See ABA Model Rules of Professional Responsibility (14), which provides:

> *Agreements prospectively limiting a lawyer's liability for malpractice are prohibited unless the client is independently represented in making the agreement because they are likely to undermine competent and diligent representation. Also, many clients are unable to evaluate the desirability of making such an agreement before a dispute has arisen, particularly if they are then represented by the lawyer seeking the agreement. This paragraph does not, however, prohibit a lawyer from entering into an agreement with the client to arbitrate legal malpractice claims, provided such agreements are enforceable and the client is fully informed of the scope and effect of the agreement. Nor does this paragraph limit the ability of lawyers to practice in the form of a limited-liability entity, where permitted by law, provided that each lawyer remains personally liable to the client for his or her own conduct and the firm complies with any conditions required by law, such as provisions requiring client notification or maintenance of adequate liability insurance. Nor does it prohibit an agreement in accordance with Rule 1.2 that defines the scope of the representation, although a definition of scope that makes the*

obligations of representation illusory will amount to an attempt to limit liability.

[xxvii] See Reporter's Comments to the Michigan Trust Code ("MTC") Part 8. Duties and Powers of Trustee and UTC § 1008. See also, *In re Baldwin's Estate,* 311 Mich 288, 310, 18 N.W.2d 827 (Mich. 1945), where it was found that the absence of a finding that the trustee acted in "bad faith" will mean that the trustee acted in "good faith", and see, *Americans for the Arts v. Ruth Lilly Charitable Remainder Annuity Trust #1 u/a January 18, 2002,* 855 N.E. 2d 592 (Ind. Ct. App. October 19, 2006) and *In Re Wege Trust,* unpublished Mich. App. per curium decision 271244,274217, 274256, 274850, 281244, 2008 WL 2439904 (Mich. App. June 17, 2008)

[xxviii] Use of such a provision generally requires that the client be advised to obtain independent counsel before agreeing to such a limitation. See footnote 25.

[xxix] https://www.wilmingtontrust.com/wtcom/index.jsp?section=WAS&fileid=1179416976020 February 6, 2019.

[xxx] The authors thank Professor Mitchell B. Gans and Jonathan G. Blattmachr for this suggestion and identification of the case discussed below.

[xxxi] *Darcy Smith, Ph.D v. Cynthia Borsella Lindemann, Esq*., US Court Of Appeals 3rd Cir., No. 16-3357, Sept 21, 2017. One should note that, in evaluating the precedential value of this case, the opinion states: "*This disposition is not an opinion of the full Court and pursuant to I.O.P. 5.7 does not constitute binding precedent*." Moreover, different jurisdictions view and may treat mandatory arbitration clauses differently.

[xxxii] *Supra.*