

The Estate Analyst®

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Mid-Year Review of Trusts and Estates

What were they thinking?

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We've arrived at the midpoint of 2011, and a summary of recent developments and cases that have made the news may lead one to wonder where we're heading economically. The outlook for real estate is of particular concern.

Several cases may also raise eyebrows, begging the question: What leads certain testators to the path less traveled?

Interesting estates that have taken a different tack include a timber baron whose fortune was only distributed after the last of his grandchildren had died, and the estate of Leona Helmsley that left millions for a dog but disinherited two grandchildren. It is also the 100-year anniversary of a "financial starvationist" who ran a sanitarium with a fasting cure.

**Two roads diverged in a yellow wood,
And sorry I could not travel both
And be one traveler, long I stood
And looked down one as far as I could
To where it bent in the undergrowth.**

—Robert Frost, *The Road Not Taken* (1915)

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Economic Outlook

Several prominent forecasts have downgraded the outlook for the nation's economy for the remainder of 2011. The International Monetary Fund has lowered its expectations for the United States from 2.8% growth to 2.5% growth for 2011 and from 2.9% to 2.7% for 2012.

In June, experts were predicting a gloomy forecast from Ben Bernanke, Chairman of the Federal Reserve, even before he gave an opinion. So, in addition to actual data about the economy, there are economists who are studying Bernanke himself for harbingers of economic activity. Actually, Bernanke has not been hard at all to interpret. He has described our recent economic growth as "frustratingly slow."

One indicator is that unemployment numbers are higher than anticipated.

The downward trend is attributed to some weather-related factors, such as storms in the Southern portion of the nation, as well as the continued repercussions of the earthquake and tsunami in Japan (which disrupted critical supply chains for cars, technology, and other key industries). On the brighter side, growth of 2.5% is far better than the double dip recession that some still feel is possible.

Global Recovery

To fully channel the most pessimistic view, one has to take in the broader global consciousness, in which "Europe's sovereign debt crisis" is the main issue. As catchphrases go, "euro-zone debt crisis" may win out because it is easier to spell, but the subject that arises the most is the "fragile global recovery."

Apparently, the global economy is in a state of delicate balance that might be thrown off by various factors. For instance, if Greece defaults on its debt, there could be a chain reaction of defaults, and the global economy could be sent spiraling into recession.

Similarly, a mishandling of the American debt ceiling is supposed to have the potential to trigger a global shockwave. If China or Brazil have too much inflation, then there will be trouble. Catastrophes can happen at any time, but those who announce a specific date for apocalypse and rapture tend to end up having to explain their embarrassing miscalculations.

Just as a dog attempts to interpret the entire world through its nose alone, some economists try to forecast the entire global economy based on one economic indicator. This is not to compare practitioners of the "dismal science" to dogs; this would unnecessarily disparage our canine companions. But even a dog could discern that Japan, the world's third-largest economy, has suffered a horrendous economic injury and will need time to recover.

While experts initially projected growth of 1.5% for Japan in the near term, a more recent projection based on an average compiled from 22 think tanks and financial institutions has now projected Japan's growth to be 0.2 %. The IMF has projected "negative growth" for Japan in 2011. That is a polite way of describing the opposite of growth. This, however, is temporary. Japan is a tremendous economic force and will rebound impressively.

Real Estate Outlook

The good news about the real estate market is that it will recover. The bad news is that the recovery might not be manifested until 2014. A "long, drawn-out recovery" was predicted by Fed Vice Chairman Janet Yellen in June.

A significant concern is the number of homes that are "underwater," i.e., with negative equity. Home values remain about 29% below their 2006 peak. In May, sales of existing homes dropped to an annual rate of 4.8 million, the lowest rate since last November. Values fell 3% during the beginning of 2011, and Zillow estimates that 28.4% of homes with mortgages are underwater (more than 16 million). Zillow predicts that the market will hit bottom in 2012 at the earliest.

On the brighter side, the National Association of Realtors has issued a press release dated May 24, 2011, that anticipates a steady positive trend for commercial real estate. Assuming a modest but steady amount of job growth over the next two years and a minimal new supply of commercial space, vacancy rates on existing commercial property would gradually be reduced.

The Society of Industrial and Office Realtors anticipates similar positive trends with lower vacancies over the next year but concedes that it will remain a tenant's market.

The strongest improvement has been in the multifamily sector, and that has prompted the National Realtor Association to go so far as to say that higher rents could lead some tenants to consider home ownership. This in turn might help the process of moving excess inventory of foreclosed homes back into private ownership.

Cyber Currency, Virtual Millionaires

Last year, we reported on a sale of virtual real estate, Club Neverdie, for a very real \$635,000. This virtual property is part of an online game called Entropia. Because there's an ongoing and apparently growing interest in this activity, investors are bullish on owning this nonexistent "property" and may even make a profit.

In another development, a gentleman can now have a virtual girlfriend, using a dating simulator program. In fact, an iPhone "app" can then insert said virtual girlfriend into travel photos to impress...one's imaginary friends.

This may be strange and childish, but a more serious use of virtual reality has now arrived in the form of a cyber currency. Bitcoins are not based on anything from anywhere and are not regulated by any particular nation. Bitcoins are not backed by gold or any other actual substance of value.

Yet the website that establishes bitcoins is making \$40,000 per day, and the value per unit jumped from \$0 to \$10 in its first year—and then tripled to \$30 per unit in a matter of weeks.

There are now 6 million bitcoins, and the supply will grow to 21 million over time, based on an algorithm. The latter information is no doubt intended to be reassuring, as though there is a logical design with built-in protections. It is a peer-to-peer cyber currency, in which value is supposed to be determined by supply and demand.

Nevertheless, skeptics may wonder, “Where’s the beef?” Somewhere, there is a real person behind a curtain who is processing this “algorithm,” and if one’s bitcoins suddenly drop in value, neither the United States nor any other nation has the authority, jurisdiction, or means to step in and sort it out.

The danger of such an anonymous system was apparently manifested when a bitcoin user ironically named “Allinvain” claimed that someone used malware to grab \$500,000 of his bitcoins. However, due to the anonymity of such currency, tracking the alleged perpetrator may be impossible. Moreover, authorities now fear that drug dealers and criminals will utilize this system for their purposes with impunity.

Could villainous geeks armed with their own algorithms corrupt this cyber marketplace, steal your virtual girlfriend, escape to Club Neverdie, and leave you holding a virtual bag of worthless bitcoins? The only reality about all this is the headache it gives grown-ups.

The Well-Trodden Path

Many lives are typical and are followed by predictable estates.

“I leave all to my spouse, but if he/she fails to survive me by 30 days, then it shall be divided between my two children, equally, share and share alike, with heirs of any of these beneficiaries who predecease me inheriting their parent’s share, equally, by representation, per stirpes, but if any of these beneficiaries shall predecease me without leaving surviving children, their shares shall go to the other beneficiaries hereinbefore identified.”

Ahh, the familiar per stirpes formula that works in typical estates from one generation to the next. Yet those inclined to utilize valuable financial tools have options and choices. If there is a growing business or significant assets, for example, several alternative pathways can be appealing. Generation skipping, dynasty, inheritor, defective grantor, and life insurance trusts can all contribute to various estates. The use of corporate entities and

the selection of domiciles and jurisdictions can protect assets and avoid unnecessary taxation.

Yet the traditional goals of reducing taxes, avoiding probate, maintaining privacy, or protecting assets may not be the main objectives for certain people, as demonstrated by the next two cases.

A Time Capsule

Wellington R. Burt of Saginaw, Michigan, was one of the nation’s wealthiest people when he died in 1919. He was a lumber baron, and his estate was possibly worth between \$40 million and \$90 million.

Mr. Burt did not simply distribute his wealth among his children or even his grandchildren. He set up an allowance of \$30,000 annually for one of his children and allowances of about \$5,000 for the others, comparable to what he left his cook and his chauffeur. It was rumored that he was senile at death. On the other hand, he lived alone in a mansion with his servants.

Based on his lifestyle, it begins to make some sense that the detached Mr. Burt required that the remainder of his estate not be distributed until 21 years after the last of his grandchildren had died. This looks similar to the rule against perpetuities, but it is not clear if all the grandchildren were in existence at the time of his death. Nor is it clear that saving taxes or protecting assets were motivating factors for what has been referred to as “the spite clause.”

One of Mr. Burt’s great-great-great-grandchildren summed it up: “I’m pretty sure he didn’t like his family back then.”

In 1989, the last of Mr. Burt’s grandchildren died; 21 years later, in 2010, the conditions of the will to allow distribution were finally met. The fortune, more than \$100 million, was distributed among 12 descendants.

No More Trouble

Leona Helmsley’s beloved Maltese, Trouble, has died at the age of 12. Helmsley left \$12 million to Trouble in a trust and nothing to two of her grandchildren, allegedly because they had failed to name any of their children after Helmsley’s late husband, Harry.

Manhattan Surrogate Judge Reena Roth concluded that Helmsley was mentally unfit when she executed her will. The \$12 million left to Trouble was reduced to \$2 million; \$6 million went to the disinherited grandchildren, and \$4 million went to the Helmsley Charitable Trust.

Leona Helmsley left a two-page mission statement for the charitable trust that directed its use for the well-being of dogs but left some discretion to trustees. The mission statement was never formally incorporated into her will or the charitable trust, and a Surrogate Court judge ruled that the trustees have

absolute discretion over use of the funds. This trust is now focused on health, education, human services, and conservation and is said to have between \$2.6 billion and \$5 billion, including shares of the Empire State Building and eight other office buildings.

A trust that provides funds for the ongoing care of a pet is not that unusual, and the bequest to Trouble has given such trusts a higher profile than ever before. *Fortune* magazine rated Helmsley's bequest to Trouble third among the 101 dumbest moments in business.

Perhaps *Fortune* and Judge Roth were both wrong, and Helmsley knew exactly what she was doing; she may have been eccentric but simply appreciated her dog more than certain people in her life. She may have intended the billions in her charitable trust to be used for animal welfare. She had sufficient clarity of thought to provide a written mission statement. Should she or her advisors have anticipated that courts might rewrite her bequest to Trouble and her charitable trust?

Funds remaining in the Trouble pet trust reverted to the family's charitable trust. Trouble was cremated but cannot join Leona and Harry Helmsley in their \$1.4 million, 12,000-square-foot mausoleum because Sleepy Hollow Cemetery does not accept dogs.

Note: The Helmsleys had lived at Durnellen Hall in Greenwich, Connecticut, a 23,000-square-foot mansion that they purchased for \$11 million in 1983. After Leona Helmsley died, the estate attempted to sell the home for \$125 million in 2008. The home was ultimately sold for \$35 million and then placed back on the market for \$43 million less than a year later.

A Starvationist's Centennial

It is the 100th anniversary of a bizarre crime.

In 1911, Claire and Dora Williamson, two wealthy British heiresses, traveled to America on holiday and decided to obtain daily treatments, at \$60 monthly, from Dr. Linda Hazzard, who had written a book, *Fasting For The Cure of Disease*.

After two months of dining only on vegetable broth and asparagus water, the girls were brought on stretchers to Dr. Hazzard's sanitarium, Wilderness Heights. During this transportation, Dr. Hazzard's attorney appeared, and Claire executed a codicil to her will to provide an annuity to Dr. Hazzard. She also transferred \$1,005 to Dr. Hazzard. The girls, then appearing to be living skeletons, began asking for food but were told the poisons were not yet out of their systems.

As described in *Starvation Heights*, a book by Gregg Olsen, Claire's diamond rings were slipped from her emaciated fingers and placed in Dr. Hazzard's jewelry box. She weighed only 50 pounds at her death on May 19, 1911.

On May 27, 1911, Dora executed a power of attorney for Samuel Hazzard, her doctor's husband, and also transferred \$583 to him. Meanwhile, that same day, Dr. Linda Hazzard filed a probate petition alleging that Dora was incompetent to manage her financial affairs.

But Claire had gotten a note to the girls' childhood nurse before her death, and the nurse arrived in time to save Dora. In the ensuing investigation, it was discovered that Dr. Hazzard's treatments had led to the deaths of 40 patients.

Dr. Hazzard was convicted of manslaughter and was proven to have forged Claire Williamson's will. The prosecuting attorney, Thomas Stevenson, called Hazzard a "financial starvationist" and "a serpent who trod sly and stealthy, yet with all her craft left a trail of slime."

In 1912, Dr. Hazzard was sentenced to 2 to 20 years in prison but was released on parole after two years and received a full pardon from the Governor in 1915. In 1920, she opened another sanitarium that operated as a "school of health" because she had lost her medical license.

Didn't anyone warn these final clients? "Don't go to the spa! You'll be fed asparagus juice and starve to death!" The sanitarium burnt to the ground in 1935. Dr. Hazzard died in 1938, ironically enough, while attempting a fasting cure on herself.

News Briefs

- 275,000 charities recently lost their tax exempt status due to failure to file required forms.
- Nevada enacted legislation making charging orders the exclusive remedy for creditors of corporations, LLCs, and LPs. This is specifically applicable to single member LLCs.
- Oregon contemplated a change to its state estate tax law that would have given it the highest such tax in the nation. The Oregon Law Commission had recommended increasing the estate tax exemption from \$1 million to \$1.5 million and increasing the top estate tax to 19.8%. Instead, the law retains the \$1-million exemption and has a top estate tax rate of 16% for estates exceeding \$9.5 million. The new rates apply in 2012.
- Ohio is considering a repeal its estate tax in 2011.

**I shall be telling this with a sigh
Somewhere ages and ages hence:
Two roads diverged in a wood, and I—
I took the one less traveled by,
And that has made all the difference.
—Robert Frost, *The Road Not Taken* (1915)**