

# Real Property, Probate & Trust



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## “The Times They Are A-Changing ...” Has Time Come to a Standstill for Washington’s Estate Tax?

by Cindy Evans, Washington State Department of Revenue, Legislation & Policy Division

The times for Washington estate tax planners have changed. Gone are the days of using stock formulas to fund credit shelter trusts. The estate tax planning world changed on June 7, 2001, when the President of the United States signed the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA).<sup>1</sup> This Act substantially changed the federal estate tax and had a major impact on estate tax planning in the state of Washington.

As a result of EGTRRA, Washington’s estate tax statutes no longer conform to the current provisions of the Internal Revenue Code (I.R.C.). The Washington statutes (RCW 83.100 *et seq.*)

continue to refer to the Internal Revenue Code as it existed on January 1, 2001.<sup>2</sup> Operating under the 2001 version of the Internal Revenue Code means that for deaths occurring after December 31, 2001, there are significant differences in planning for Washington’s estate tax and the federal estate tax. The table below outlines the major differences between the version of the Internal Revenue Code that is relevant for Washington estate tax purposes and the current version of the Internal Revenue Code applicable for federal estate tax purposes.<sup>3</sup>

### I. Comparison of Major Differences Between State and Federal Estate Tax Laws

	Washington - 2001 I.R.C.	Federal Estate Tax - Current I.R.C.
<b>Filing threshold/ Unified credit</b>	The filing threshold/unified credit for 2002 - 2003 is \$700,000. The filing threshold/unified credit rises to \$850,000 in 2004, \$950,000 in 2005, and tops out at \$1,000,000 for deaths occurring in 2006.	The filing threshold/unified credit for federal estate tax is \$1,000,000. The filing threshold/unified credit continues to rise to \$3,500,000 by 2009.
<b>Federal credit for state death taxes</b>	Washington collects 100% of the credit for state death taxes.	The estate of a decedent dying during the year 2002 can claim a credit equal to 75% of the amount paid to the state of Washington. For deaths occurring in 2003, the estate can claim 50% of the credit paid to Washington. For deaths occurring in 2004, the estate can claim 25% of the credit paid to Washington. For deaths occurring in 2005 and thereafter, the estate can take a deduction equal to the amount of state death taxes paid. See 26 U.S.C. § 2058.

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## **“The Times They Are A-Changing ...” Has Time Come to a Standstill for Washington’s Estate Tax?**

### **I. Comparison of Major Differences Between State and Federal Estate Tax Laws** *continued*

	<b>Washington - 2001 I.R.C.</b>	<b>Federal Estate Tax - Current I.R.C.</b>
<b>Maximum rate of taxation</b>	The top rate of taxation remains at 55% and the 5% surcharge remains on estates over \$10,000,000.	The top rate of taxation is reduced to 50% for deaths occurring in 2002 and is reduced by 1% each year until the top rate for years 2007 - 2009 is 45%. The 5% surcharge for estates over \$10,000,000 is eliminated for deaths occurring after December 31, 2001.
<b>6166 Election</b>	The extension of time for payment of estate tax is limited to interests in a closely held business. The definition of closely held business means a partnership or corporation with 15 or fewer partners or shareholders.	The extension of time for payment of estate tax is limited to interests in a closely held business. The definition of closely held business means a partnership or corporation with 45 or fewer partners or shareholders.
<b>Generation-skipping transfer tax</b>	Washington collects the 5% credit allowed on taxable terminations and distributions. See federal form 706-GS(T) part III, line 11 and 706-GS(D), part III, line 8. Washington follows the special generation-skipping transfer tax allocation rules outlined in the 2001 IRC (26 U.S.C. § 2632).	<ol style="list-style-type: none"> <li>1. Generation-skipping transfer (GST) tax exemption automatically allocated to transfers made during life that are “indirect skips.”</li> <li>2. GST tax exemption can be allocated retroactively when there is an unnatural order of death.</li> <li>3. Trust can be severed in a qualified severance.</li> <li>4. Value of property for purposes of inclusion ratio shall be its finally determined gift tax or estate tax value depending on the circumstances of the transfer.</li> <li>5. Secretary of the Treasury is authorized/directed to grant extensions of time to make the election to allocate GST tax exemption and to grant exceptions to the time requirement, without regard to whether any period of limitations has expired.</li> </ol>
<b>Qualified Conservation Easements</b>	Land subject to a qualified conservation easement means land located in or within 25 miles of a metropolitan area; land in or within 25 miles of an area which is a national park or wilderness area; or land in or within 10 miles of an area which is an Urban National Forest. See 26 U.S.C. § 2031 (2001).	Land subject to a qualified conservation easement means land located in the U.S. or any possession of the U.S. which was owned by the decedent or decedent’s family at all times during 3 year period ending on the date of decedent’s death, and the election made by a qualified individual. <sup>4</sup>

### **II. Washington Estate Tax Return**

Because Washington’s estate tax does not conform to current federal law, there are now instances where an estate must file a Washington estate tax return but not a federal estate tax return (IRS Form 706 – United States Estate and Generation-Skipping Transfer Tax Return). An estate that must file a federal return may simply complete the first three pages of Washington’s estate tax return and attach the federal return and any applicable schedules.

The lack of conformity between Washington’s estate tax laws and current federal estate tax law required the revision of Washington’s estate tax return. The revised estate tax return and instructions are currently available in PDF format at the Washington State Department of Revenue Web site ([www.dor.wa.gov/Docs/forms/Misc?EstateTransTxRtrnInst.pdf](http://www.dor.wa.gov/Docs/forms/Misc?EstateTransTxRtrnInst.pdf)).

### **III. Washington Estate Tax Rules**

On October 1, 2002, the revised estate tax rules, WAC 458-57 *et seq.*, took effect. The revised rules emphasize Washington’s operation under the Internal Revenue Code before amendment by EGTRRA (i.e., filing threshold/unified credit at \$700,000 and 100% of the federal credit for state death taxes being collected) and allows estates that are not required to file a federal return to request a one-time automatic six-month filing extension. The Washington State Department of Revenue also added a new rule relating to the calculation of the generation-skipping transfer tax and the allocation of the generation-skipping transfer tax exemption. The following table lists the sections and titles of the pertinent sections of the Washington Administrative Code:

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## **“The Times They Are A-Changing ...” Has Time Come to a Standstill for Washington’s Estate Tax?**

<b>WAC</b>	<b>Title</b>
458-57-005	Nature of estate tax, definitions
458-57-015	Valuation of property, property subject to estate tax, how to calculate the tax
458-57-017	Property subject to generation-skipping tax, how to calculate the tax, allocation of generation-skipping tax
458-57-025	Determining the tax liability of nonresidents
458-57-035	Washington estate tax return to be filed – Penalty for late filing – Interest on late payments – Waiver or cancellation of penalty – Application of payment
458-57-045	Administration of the tax – Releases, amended returns, refunds, heirs of escheat estates

### **IV. The Future**

Estate tax planning has changed, but the Washington estate tax law has not. The present focus of the Washington State Department of Revenue is on educating practitioners and the general public about the state estate tax.

An electronic mailing list service is available to persons who wish to remain apprised of future changes to the state laws, rules, and other estate tax news. To use the service or to communicate with the Washington State Department of Revenue, please contact:

- Web site: [www.dor.wa.gov](http://www.dor.wa.gov)
- Links to new Washington estate tax return:  
<http://www.dor.wa.gov/Docs/forms/Misc/EstateTransTxRtrn.pdf>
- Links to new Washington estate tax return instructions:  
<http://www.dor.wa.gov/Docs/forms/Misc/EstateTransTxRtrnInst.pdf>
- Link to Washington estate tax electronic mailing list: [http://www.dor.wa.gov/Content/Contact/email/con\\_email\\_listserv\\_app.asp?listtype=estate](http://www.dor.wa.gov/Content/Contact/email/con_email_listserv_app.asp?listtype=estate)
- Estate tax telephone contact numbers: (360) 753-5547 or (360) 753-7518
- Mailing address:  
State of Washington  
Department of Revenue  
Special Programs Division  
P.O. Box 448  
Olympia, WA 98507-0448

- 1 The changes made to federal law by EGTRRA will sunset on December 31, 2010, unless Congress acts to make the changes permanent.
- 2 See RCW 83.100.020(15).
- 3 This article does not address changes made by EGTRRA to qualified-family owned business interests, estate and gift taxation of non-resident non-citizens, or changes made to basis of property acquired from a decedent.
- 4 During the 2002 legislative session, the Washington Legislature amended RCW 11.98.070 and RCW 11.96A.030. These amendments allow a trustee to donate land as a conservation easement in order to qualify for *federal estate tax exclusions or deductions*. Laws of 2002, c. 66. Under EGTRRA, Congress broadly expanded what land qualifies to be a conservation easement. Consequently, a Washington trustee may donate land to a conservation easement that qualifies under current I.R.C. section 2031 and receive a deduction for federal estate tax purposes but may not use the same deduction on the Washington estate tax return. If the land qualifies under the more restrictive 2001 version of the Internal Revenue Code as applicable in the state of Washington, the estate may claim the deduction on the Washington estate tax return by completing Schedule U.

## State Estate Taxes: After 22 Years, Back Again?

by Charles R. Lonergan, Jr. and Ray Siderius, Siderius, Lonergan & Martin LLP, Seattle

For almost 22 years, citizens of the state of Washington have been indifferent to the amount of tax paid on a decedent's estate. They knew it would amount exactly to the maximum amount the Internal Revenue Service permitted as a credit against federal estate taxes.

### I. Washington State Initiative 402

By Initiative 402, passed in 1981, the state of Washington abolished all inheritance taxes, imposing instead a Washington "estate tax," crafted to add no increase in net tax cost to an estate required to pay federal estate taxes. The amount payable to Washington was to be equal to the credit allowed the estate on its federal estate tax return. Here, as in other states with similar legislation, the estate tax was a "pickup" tax, meaning the state "picked up" the amount of the credit for state death taxes allowed on the federal return. Initiative 402 provided further, that if the estate was not required to file a federal return, no Washington return need be filed.

Initiative 402, imposing the estate tax, referred to the Internal Revenue Code of 1954, in effect when the initiative was passed. The Washington Legislature periodically updated the definition of the Internal Revenue Code in the estate tax statutes to correspond with *existing* federal rules, regulations and statutes. This was necessary to avoid a challenge that Washington's law-making power had been impermissibly delegated to Congress.

Over time, the Washington Legislature made limited "housekeeping" amendments to the original initiative to update the reference to the Internal Revenue Code, as of the date of the legislation. The most recent change was Chapter 320 of the laws of 2001, titled "An Act Relating to Simplifying Excise Tax Application & Administration." It changed the definition of "Internal Revenue Code" to read "the United States Internal Revenue Code of 1986, as amended or renumbered as of January 1, 2001." The legislative history of this provision described it as a "housekeeping amendment," and the amendment passed both houses without a dissenting vote.

### II. Impact of Federal Economic Growth and Tax Relief Reconciliation Act of 2001

In 2001, by Public Law 107-16 (also known as the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA)), Congress substantially reduced the amount of the federal credit that estates could receive for state estate taxes paid. The new limited federal credit is based upon a graduated table that appears in Internal Revenue Code section 2011 (26 USC 2011). Public Law 107-16 provides that for deaths occurring during 2002, only 75% of the table would be allowed as a credit. For deaths during 2003, 50%, and for deaths occurring in 2004, 25% of the table. The new federal law also raised from \$700,000 to \$1,000,000 the gross value of an estate for which any federal return is required.

The effect of this change was to substantially reduce estate taxes that would be payable to a state, like Washington, that had a "pickup" tax. Faced with this loss of revenue, several states amended their estate tax provisions.<sup>1</sup> There has been no legislation enacted by the Washington Legislature amending the Washington estate tax, other than Chapter 320 of the Laws of 2001 which, as stated, simply updated the definition of the Internal Revenue Code. The title of that bill (H.B. 1361) did not advise the Legislature it would result in a substantial increase in the Washington estate tax.

### III. Washington State Response to EGTRRA

The Washington State Department of Revenue, relying on the amended reference to the Internal Revenue Code in the Revised Code of Washington, has now concluded that:

1. Even though RCW 83.100.050 states: "No Washington return need be filed if no federal return is required," and even though there is no federal return required unless an estate has a gross value in excess of \$1 million, estates between \$700,000 and \$999,999 are nevertheless required to file an estate tax return with the state of Washington and to pay estate tax.
2. The Washington estate tax is 100% of the credit for state death taxes provided in the graduated table in Internal Revenue Code section 2011, even though for deaths occurring in 2002, Congress has reduced by 25% the amount of that credit that will be allowed in the federal return.
3. For estates that are required to file a federal return but do not owe any federal tax and do not receive any credit for state death taxes, the estate must still pay to the state of Washington an estate tax which can be as much as the full amount of the credit in the federal graduated table.

### IV. Is the Response of the DOR Constitutional?

This administrative elimination of the statutory exemption from the duty to file a state return (if no federal return is required), together with the requirement estates, for the first time since 1981, pay a tax to the state of Washington in excess of the amount of the federal credit for state death taxes, are contrary to the language and intent of Initiative 402, and amount to the imposition of a Washington estate tax without the necessary legislative basis. It is the opinion of the authors that the actions of the Washington State Department of Revenue constitute an unconstitutional seizure of legislative power, in excess of the authority granted that department by the Washington State Legislature, and an attempt to amend by department action validly enacted legislation, including Initiative 402, as later codified.<sup>2</sup>

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## NOTE

The firm of Siderius Lonergan & Martin LLP, in association with G. Lawrence Salkield, Attorney at Law and Orly J. Sorrel of Sorrel & Tall, Inc., P.S., has filed a lawsuit in Thurston County (denominated as a class action) requesting a refund of the Washington estate taxes *paid under protest*. The proposed classes to be certified by the court in this litigation are Class A, Class B and Class C as follows:

### Class A:

The estates of all Washington residents where the deceased died after December 31, 2001, where the total assets of the estate exceed \$1,000,000 and where the estate has paid to the Washington Department of Revenue under written protest a Washington estate tax in excess of the credit for state death taxes on its federal return.

### Class B:

The estates of all Washington residents where the deceased died after December 31, 2001, where the total assets of the estate exceed \$700,000 and are less than \$1,000,000 and no federal return is required and where estate taxes have been paid to the Washington Department of Revenue under written protest.

### Class C:

The estates of all Washington residents where the deceased

died after December 31, 2001, where the estate is required to file a federal estate return but does not receive any credit for state death taxes on that return and where estate taxes have been paid to the Washington Department of Revenue under written protest.

These three classes, as defined, require the filing of a written protest. Shortly after the lawsuit was filed, the attorneys for the plaintiffs received communication from several attorneys who had clients who had paid Washington estate taxes but had not filed any protest. Thus, amended and supplemental class definitions have been filed to include such estates if the court rules – as some cases have held – that in the case of excise taxes, no protest is necessary.

Though the Thurston County case has been filed as a class action, the plaintiffs' attorneys indicate that there is no certainty that the claims will be certified as class claims by the court nor is there any certainty that the representative plaintiffs will be named by the court as class representative plaintiffs. There is even a remote possibility that a successful decision holding the Department of Revenue's interpretation unconstitutional can be held to be prospective only and not retroactive, thereby denying refund. Further information about this lawsuit may be obtained by visiting the plaintiffs' attorneys' Web site at <http://www.estatetaxesWashington.com>.

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## State Estate Taxes...

It is also the opinion of the authors that the Department of Revenue's proposed administration of Chapter 320 of the Laws of 2001 violates Article II, Section 19 of the State Constitution, because title to the enactment failed to advise legislators or the public that a large increase in estate taxes would be imposed 22 years after such estate taxes were specifically repealed. The Washington State Department of Revenue, without legislative authority, has announced that for deaths after January 1, 2002, there is a new "filing threshold," requiring estates in excess of \$700,000 to file estate tax returns and pay taxes to the state of Washington. This, though RCW 83.100.050, which was part of Initiative 402 in 1981 and has been in effect to this day without substantive change, exempts from the necessity of filing a Washington estate tax return all estates that are not required to file a return with the Internal Revenue Service.

An estate that seeks a refund of wrongfully imposed taxes should pay the taxes under written protest and then sue for refund. There are penalties, interest and possible criminal penalties for non-filers. RCW 83.100.070 provides for interest and a penalty

equal to 5% of the tax due for each month, with a maximum penalty of the lesser of 25% of the tax due or \$1,500.00. RCW 83.100.140 provides criminal penalties for failing to file and/or willfully filing a false return – a gross misdemeanor.

1 See, for example, Senate Bill 373 in Maryland, titled "Maryland Estate Tax—Effect of Act of Congress Repealing or Reducing Federal Credit." A similar law was enacted in the District of Columbia. The text writers refer to these as "decoupling" legislation, meaning legislation separating the state estate tax provisions from provisions of the federal code. For example, the title of the bill enacted by the District of Columbia is:

To amend, on an emergency basis, section 47-3701 of the District of Columbia Official Code to fully decouple District of Columbia estate and inheritance taxes from federal law to ensure the continued collection of the taxes at a level comparable to the tax collected prior to the enactment of recent amendments to the Internal Revenue Code of 1986.

2 In 1988, the Washington Legislature enacted the "Estate and Transfer Act of 1988" which restated the principle that the Washington estate tax continued to be a "pickup" tax.

## Revisiting *In re Stanton*

by Tim J. Filer, Foster Pepper & Shefelman PLLC, Seattle

The United States Court of Appeals for the Ninth Circuit recently resuscitated the long-dormant “optional advance” rule for determining the priority of disbursements to borrowers under a “future advances” clause in a mortgage or deed of trust. See *In re Stanton*, 285 F.3d 888 (9<sup>th</sup> Cir. 2002) (“*Stanton I*”) (discussed at pages 9-10 of the Summer 2002 edition of the RPPT Newsletter). The *Stanton I* court held that “optional” advances under a mortgage would have a lower priority than liens that had attached after the deed of trust was recorded, but before the advances were made. *Id.* The decision was a concern to Washington lenders who provide secured lines of credit or other secured loans with fluctuating balances or future advance provisions, who had long believed the rule to have been abrogated by the 1973 adoption of Washington’s lien priority statute (now codified at RCW 60.04.226).

The revival of the “optional advance” rule was short-lived. The secured party filed a petition for rehearing and the Washington Financial League and the Washington Bankers Association filed a joint amicus brief urging the court to reconsider the decision. In September 2002, the Ninth Circuit issued an amended opinion withdrawing its adoption of the “optional advance” rule. *In re Stanton*, 303 F.3d 939 (9<sup>th</sup> Cir. 2002) (“*Stanton II*”). The new opinion expressly declines to decide whether the “optional advance” rule is still alive under Washington law. *Id.* at 943-44.

### I. *Stanton* Statement of Facts

*Stanton* involved a corporate borrower whose shareholders had signed a guarantee and a deed of trust against their home that secured their obligations under the guarantee. The secured guaranty included future advances to the corporation. The shareholders filed for bankruptcy protection, but the corporation continued in operation. The secured party (a factor) advanced funds to the corporation after the shareholders filed bankruptcy. The shareholder’s bankruptcy trustee subsequently sold the home. The secured party and the bankruptcy trustee both asserted claims against the sale proceeds.

### II. Ninth Circuit’s Prior Holding

Both of the Ninth Circuit’s opinions primarily address issues arising under the Bankruptcy Code. However, the opinion in *Stanton I* held that the “optional advance” rule adopted in *National Bank of Washington v. Equity Investors*, 81 Wn.2d 886, 506 P.2d 20 (1973) would govern the *priority* of the secured party’s claim to the proceeds from the sale of the collateral for the guarantee. The *Stanton I* court unequivocally held that under Washington law “optional advances” – advances over which the lender had discretion and that were not “obligatory” under the loan documents – would have priority only as of the time the advances were made. *Stanton I*, 285 F.3d at 893. Liens that attached *after* the deed of trust securing the guarantee was recorded, but *before* the “optional advances” were made would have a higher priority as against the sales proceeds. *Id.*

### III. Ninth Circuit’s New Decision

The *amicus* brief urged the court to reconsider its decision based on the lien priority statute, now codified at RCW 60.04.226. The Washington Legislature adopted the original version of the lien priority statute in 1973, approximately two months after the *National Bank of Washington* decision came down. The *amici* argued that the plain language of the statute overruled the *National Bank of Washington* decision and rejected the idea that “optional” advances had a different priority than “obligatory” advances. RCW 60.04.226 (priority established “to the extent of all sums secured by the mortgage or deed of trust *regardless of when the same are disbursed or whether the disbursements are obligatory.*”).

In *Stanton II*, the Ninth Circuit withdrew the portion of its prior opinion holding that the “optional advance” rule still applied in Washington (readers may see an edited version of the Ninth Circuit’s changes to the opinion in this edition’s “Recent Developments” column). Instead, it added language expressly reserving that question. See, e.g., *Stanton II*, 303 F.3d at 943 (“If *National Bank of Washington* is still good law, it would mean that....”). The Ninth Circuit also added a new paragraph recognizing that the lien priority statute might have overruled *National Bank of Washington*:

Following a 1973 amendment to the lien priority statute in the mechanics’ lien chapter, it may be that *National Bank of Washington* is either limited in the mechanics’ lien context or entirely abrogated.

*Id.* The Ninth Circuit decided it would leave this question for the bankruptcy court to decide, if necessary, in further proceedings on remand. *Id.* at 943-44.

### IV. “Optional Advance” Rule – Alive or Dead?

The Ninth Circuit properly held that Washington law recognizes and enforces “future advances” clauses in real property security instruments. *Stanton II*, 303 F.3d at 943. Because it does not decide the “optional advance” question, the *Stanton II* opinion cannot serve as precedent for the application of the *National Bank of Washington* rule to decide what *priority* will be afforded to such future advances.

Nevertheless, the Ninth Circuit failed to account for the plain language of the lien priority statute by raising the *possibility* that the Washington Legislature eliminated the “optional advance” rule only in the mechanics’ lien context. The statute is clear on the questions of scope and priority: “any mortgage or deed of trust shall be prior to *all* liens, mortgages, deeds of trust, and other encumbrances which have not been recorded prior to the recording of the mortgage or deed of trust.” RCW 60.04.226. It is also clear in its rejection of the “optional advance” priority rule. Priority attaches to “all sums ... *regardless of when the same are*

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# Alaska's Five-Year Experience With Self-Settled Discretionary Spendthrift Trusts, Part II

by David G. Shaftel, Law Offices of David G. Shaftel, Anchorage, Alaska

## Introduction

Part I of this article, which appeared in the Fall 2003 edition of this newsletter, discussed the following subjects:

- The Planning Dilemma: Early Gifting Versus Future Possible Needs.
- Alaska's Statutory Change Provides a Solution.
- How a SSDS Trust Is Structured and Funded.
- Trust Owned Life Insurance.
- The Dispositive Plan.
- Choice of Trustees.
- Future Amendments.

## I. Use of SSDS Trusts by Nonresidents of Alaska.

The framers of the Alaska SSDS and perpetual statutory trust provisions considered that persons located outside Alaska may well be interested in using such trusts. Consequently, they enacted statutory provisions which the framers thought would establish a sufficient Alaska nexus so that Alaska law would apply to nonresident trusts.

These provisions require that some or all of the trust assets be deposited in Alaska and administered by a "qualified person," who is either an Alaska resident, or an Alaska trust company or bank.<sup>1</sup> The powers of the Alaska trustee include or are limited to maintaining records for the trust on an exclusive or nonexclusive basis, and preparing or arranging for the preparation of, on an exclusive or nonexclusive basis, an income tax return that must be filed by the trust. Part or all of the trust administration is to occur in Alaska, including physically maintaining trust records in this state.<sup>2</sup>

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## Revisiting *In re Stanton*

disbursed *or whether* the disbursements are *obligatory.*" *Id.* (emphasis added).

The Ninth Circuit could have eliminated the possible confusion caused by its discussion of the "optional advance" rule by deciding the question or by having certified the question to the Washington State Supreme Court. The *Stanton II* opinion simply leaves the question open, so the proceedings in the *Stanton* case will merit continued attention. If the Ninth Circuit's decisions in *Stanton* cause undue uncertainty for lenders and title insurers, the Washington Legislature may have to adopt clarifying legislation.

<sup>1</sup> Tim J. Filer is a member of the Litigation Group at Foster Pepper & Shefelman PLLC and acted as counsel for the amici in support of the Petition for Rehearing in *In re Stanton*.

In order for nonresidents to achieve the transfer tax benefits of an SSDS Trust, they must qualify for the underlying asset protection provided by the Alaska statute. Additional issues have been raised questioning such qualification. These issues are discussed below in the section titled, "How Could a SSDS Trust Fail?"

## II. Subsequent Alaska Legislation Facilitating SSDS Trusts

In addition to the 1997 legislation which reversed the general rule concerning SSDS Trusts, and abolished the rule against perpetuities, the Alaska Legislature has subsequently enacted a number of other provisions which facilitate the use of these trusts and trust administration in the state.<sup>3</sup> Pending 2002 legislation, if enacted, will clarify the definitions of present and future creditors. In addition, this pending legislation will provide express statutory authority for trust protectors and trustee advisors; will clarify that a trustee's power to allow a beneficiary to use trust property does not allow creditors to reach such property; and will provide that creditors may not reach assets which are subject to a limited power of appointment held by a debtor.<sup>4</sup>

## III. How Could a SSDS Trust Fail?

As discussed above, this type of transfer tax planning first depends upon the asset protection foundation. Once an adequate asset protection foundation exists, then the inquiry shifts to analysis of two provisions (sections 2036 and 2038) of the estate tax and the Contract Clause contention. Residents of states which have enacted SSDS statutes have a strong position concerning the asset protection foundation. Nonresidents who form SSDS trusts have additional issues relating to whether they have an adequate asset protection foundation: the Full Faith and Credit Clause and the Bankruptcy Court scenarios.

If the transfer tax issue is contested, the asset protection foundation will be hypothetical. There will not be a creditor trying to reach the assets of the trust. The court will need to decide if an "adequate" asset protection foundation exists for the settlor in question. Such a foundation may well not need to be perfect and without any theoretical weaknesses.

### A. Application of Sections 2036 and 2038

With the above analytical approach in mind, first consider the provisions of the estate tax. If applicable state law prevents the settlor's creditors from reaching the assets of the trust, then section 2038 does not apply because, as of the date of the settlor's death, the settlor does not have the power to revoke the trust by relegating creditors to the trust's assets. The remaining estate tax issue is whether, pursuant to I.R.C. § 2036(a)(1), the settlor has retained enjoyment of, or the right to income from, the trust assets. Initially, the plain language of the statute which requires

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## **Alaska's Five-Year Experience...**

“retention” does not seem to apply to a settlor-beneficiary, who may only receive distributions pursuant to the absolute discretion of an independent trustee.

A number of authorities exist which support the conclusion that section 2036(a)(1) “retention” does not exist with respect to the rights of a discretionary settlor-beneficiary.<sup>5</sup> One critical analyst of these authorities finds some to be indirect or not on point, but concedes there is supporting authority for the conclusion that the trust assets will not be included in the settlor’s gross estate.<sup>6</sup> Another analyst states, “[t]he better rationale for the exclusionary rule here is that the grantor has not ‘retained’ the income from the transferred property.”<sup>7</sup>

Finding “retention” under the existing language of I.R.C. § 2036, based only upon the settlor’s status as a discretionary beneficiary, is a significant stretch. In a similar situation involving questionable coverage by section 2036 of joint purchases of property, the Treasury Department found the need for a statutory change.<sup>8</sup> One analyst concluded, “[i]t was sufficiently unclear whether § 2036(a)(1) would apply to such a case that § 2702(c)(2) specifically addresses this form of transaction.”<sup>9</sup> If section 2036 is amended to expressly include SSDS trusts, and if such amendment is stated to be a change in the law, then its effect should be prospective. Existing SSDS trusts should be grandfathered. If the amendment is stated to only be a clarification of the law, then this statutory interpretation issue will continue for existing SSDS trusts. However, as a practical matter, the Internal Revenue Service may take a much less aggressive position in regard to trusts formed prior to the amendment.

Interestingly, if there was a statutory change of section 2036 in regard to SSDS trusts, there is no certainty that the change would be designed to produce inclusion of the trust’s assets in the settlor’s gross estate. Congress’ recent legislative changes in the transfer tax area have gone in the other direction.<sup>10</sup> A reasonable argument can be made that section 2036 should be amended to expressly allow a settlor to create an SSDS Trust in any jurisdiction in order to solve the “Planning Dilemma” described above. Such an accommodation might help to alleviate the tension between complete repeal and “sunset” that exists under the 2001 Tax Act.

Alternatively, faulty implementation of the trust could result in estate tax inclusion. The specific choices of trustees, documentation, and pattern of distributions may justify a court finding that an agreement existed between the settlor and the trustee to make certain distributions. This would constitute the retention of an income interest, and I.R.C. § 2036 would apply.<sup>11</sup> The result would be inclusion of trust assets in the settlor’s gross estate.<sup>12</sup>

### **B. The Contract Clause**

Next, consider the Contract Clause<sup>13</sup> contention which applies to both residents and nonresidents of SSDS states. To violate the Contract Clause an SSDS statute must substantially impair the

obligations of parties to existing contracts or make them unreasonably difficult to enforce.<sup>14</sup> The violation occurs because of the retroactive effect of the statute upon contracts which exist on the date of enactment of the statute.<sup>15</sup> Creative arguments have been made in support of a Contract Clause violation by the new SSDS statutes.<sup>16</sup> The settlor’s response would be that a contract creditor still has adequate remedies under the state’s fraudulent conveyance statute. The contract creditor would then contend that if the transfer does not constitute a fraudulent conveyance, then the settlor has successfully protected assets which the contract creditor could otherwise have reached.<sup>17</sup>

The relevance of this Contract Clause contention to transfer tax planning involves the completed gift issue.<sup>18</sup> If a settlor has existing contract creditors when the SSDS statute was passed (1997), then the settlor could refuse to pay these creditors. They could then attack the transfer pursuant to the Contract Clause theory. If the contract creditors are successful, then the settlor will arguably have relegated creditors to the trust’s assets. The tax issue is whether in such a scenario the settlor has retained such “dominion and control” as to prevent the gift from being completed. Since this Contract Clause contention only applies to contract creditors who existed on the date of enactment of the statute (1997), as time expires this argument will become factually irrelevant to settlors forming new SSDS trusts.<sup>19</sup>

### **C. The Full Faith and Credit Scenario**

Now consider the Full Faith and Credit scenario involving a nonresident settlor. Assume that a hypothetical creditor sues the settlor in the settlor’s domiciliary state and obtains a judgment. Next, assume that as part of that suit, or in a separate action in the domiciliary state, the creditor proceeds against the trustee of the SSDS Trust in order to enforce the judgment against the trust’s assets. The first issue is one of choice of law. Which state’s spendthrift trust rules apply: Alaska’s or the rules of the settlor’s state of domicile? A sub-issue is whether this question is one of administration or validity of the trust.<sup>20</sup> Depending upon how this sub-issue is resolved, ultimate resolution of this conflict of laws issue may be factually dependent.<sup>21</sup> The public policy of the domiciliary state may need to be determined.<sup>22</sup>

Assume that the domiciliary court chooses its spendthrift trust rules and enters a judgment against the trustee. The hypothetical creditor then proceeds to Alaska and asks its court to enforce the judgment against the trustee based upon the Full Faith and Credit Clause.<sup>23</sup> A basic requirement for full faith and credit is that the judgment be valid.<sup>24</sup> One requisite for validity is that the forum court possess jurisdiction.<sup>25</sup> Assume the Alaska trustee did not participate in the domiciliary court action and had few, if any, contacts with that state.<sup>26</sup> Then, the domiciliary state’s jurisdiction over the Alaska trustee and the assets such trustee holds will be highly questionable.<sup>27</sup> Consequently, full faith and credit may well be denied.<sup>28</sup>

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## **Alaska's Five-Year Experience...**

### **D. The Bankruptcy Court Scenario**

The bankruptcy court scenario must also be considered when analyzing the asset protection foundation of a nonresident settlor. This scenario includes both statutory interpretation and choice of law issues. First, assume that a creditor has forced the settlor into involuntary bankruptcy. However, section 541(c)(2) of the Bankruptcy Code expressly exempts spendthrift trusts. Therefore, the creditor must persuade the court to narrowly construe this provision to exclude the recent Alaska, Delaware, Nevada, and Rhode Island SSDS Trust statutes.<sup>29</sup> Then, the Supremacy Clause<sup>30</sup> would give section 541(c)(2) precedence over conflicting state SSDS provisions. As a result, the trust assets would be included in the bankruptcy estate.<sup>31</sup>

The choice of law issue assumes that the creditor forces the settlor into involuntary bankruptcy in the settlor's state of domicile. The bankruptcy court will have personal jurisdiction over the Alaska trustee based upon the court's national jurisdiction. The court will need to resolve the choice of law issue.<sup>32</sup> If the bankruptcy court applies the domiciliary state's choice of law rules, and if those rules follow the restatement,<sup>33</sup> and if the court determines the issue is one of validity of the trust, then the bankruptcy court may determine that the Alaska SSDS statute violates a strong public policy of the domiciliary state.<sup>34</sup> As a result, the trust assets will be included in the bankruptcy estate.

This choice of law bankruptcy scenario involves a number of obstacles. First, all of the legal assumptions described above must fall into place. Next, it assumes the creditor is successful in forcing the settlor into involuntary bankruptcy.<sup>35</sup> More importantly, if the settlor anticipates this scenario, the settlor may voluntarily declare bankruptcy in Alaska. This may lead the bankruptcy court to apply Alaska's SSDS rules.<sup>36</sup>

### **E. Summary for Nonresidents**

First, it is important to consider the difference between pure asset-protection cases and transfer tax litigation. The highly publicized recent asset-protection cases involved extreme facts and equities that would influence most courts to sympathize with the plaintiff-creditor.<sup>37</sup> The situation is quite different when the asset-protection issue is hypothetical, and only needs resolution so that the transfer tax issue may be determined.

The above analysis establishes that the asset-protection foundation for a nonresident settlor using an Alaska SSDS Trust is not absolute. The interesting question is whether such a foundation needs to be perfect for transfer tax purposes. The above analysis describes theoretical approaches for a creditor to reach the SSDS Trust assets, if the facts are right and if a court follows a specific decision-tree. Are these approaches certain enough to undermine the asset-protection foundation, for transfer tax purposes, of a carefully implemented Alaska SSDS Trust created by a nonresident? This is the crucial issue for nonresident settlors.

### **IV. Why Don't We Have More Authority?**

Five years have elapsed since the enactment of Alaska's SSDS Trust statutes. However, authority and review remain sparse. The Internal Revenue Service has refused to rule further on such trusts.<sup>38</sup> Despite the formation of numerous SSDS trusts, practitioners in Alaska and Delaware report that as yet there is no audit experience. Consequently, there has been no administrative or judicial review of such trusts.

With respect to residents of states which have enacted SSDS statutes, the Internal Revenue Service's estate tax statutory position appears weak. The Contract Clause contention becomes factually irrelevant as time expires. Therefore, a challenge may only occur if there is faulty implementation of the trust. Resolution of such a fact-dependent case will not be helpful for the resolution of other cases involving properly implemented trusts.

With respect to nonresidents, the additional issues revolve around whether the asset protection foundation exists. The discussion of the Full Faith and Credit and Bankruptcy Court scenarios demonstrates that most of these issues are both highly fact-specific and depend upon unpredictable decisions of domiciliary, Alaska and bankruptcy courts.

When cases are decided in the future, the decisions may be narrow and limited to the specific situation involved.<sup>39</sup>

A legislative resolution of the effectiveness of transfer tax planning with SSDS trusts is also unpredictable. At some point before 2010, Congress will likely rethink the transfer tax changes enacted by the 2001 Tax Act. Section 2036 could be amended to resolve this area. But which way?

In view of the above-described limited arguments available to the Internal Revenue Service with respect to residents of an SSDS state, and the fact-specific character of the issues involving nonresident settlors, there may continue to be a lack of significant judicial authority in this area.<sup>40</sup> If the tax question does arise, the Internal Revenue Service and the estate's representative often may find a negotiable resolution.

### **V. What Should the Planner Do?**

Clients considering the use of an SSDS Trust for transfer tax reduction purposes should be fully advised of the present lack of significant authority. Planners and their clients need to be aware that such authority in this area may continue to be slow in coming. Those uncomfortable with such ambiguity should not use an SSDS Trust. For clients who are still interested, an analysis should be made of the downside.

If the SSDS Trust approach were to fail because of one of the issues discussed above, then the following transfer tax consequences would occur. The trust assets and their appreciation will be included in the settlor's gross estate and be subject to estate tax.<sup>41</sup> Further, the settlor has lost the benefit of the annual exclusion gifting that was made to the trust. The settlor's estate

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## Alaska's Five-Year Experience...

retains the use of the applicable credit amount that was originally allocated to the completed gift to the trust.<sup>42</sup> The settlor has lost the cost of creating and maintaining the trust.

What if the settlor made attempted completed gifts that were larger than the settlor's annual exclusion and applicable credit amounts and, as a result, paid out-of-pocket gift tax? In addition to the above consequences, the settlor would have lost the use of the out-of-pocket tax amount during the settlor's lifetime. Moreover, if the federal estate tax is permanently repealed, the payment of the gift tax would have been unnecessary.

The main downside would appear to be that the settlor has lost the opportunity to do some different planning with the settlor's annual exclusion gifts and with the portion of the settlor's applicable credit amount used for the SSDS Trust. Would the settlor have done such different planning? How do the risks and rewards of such different planning compare to the SSDS approach? These are the key questions which the estate planner and interested clients need to resolve.

- 1 Alaska Statute 13.36.390(2).
- 2 Alaska Statute 13.36.035(c).
- 3 These changes are discussed in Greer and Shaftel, "Alaska Enacts Additional Estate Planning Legislation," *Estate Planning*, Vol. 27, No. 8 (Oct. 2000), and Shaftel, "Newest Developments in Alaska Law Encourage Use of Alaska Trusts," *Estate Planning*, Vol. 26, No. 2 (Feb. 1999).
- 4 House Bill 316, Alaska State Legislature (2002).
- 5 See the authorities cited in the articles discussed in note 13.
- 6 Pennell, *Estate Planning*, Vol. II, § 7.3.4.2 (Aspen, 6th ed.). This commentator concludes, "[t]he answer to that question has not adequately been provided by case law or rulings." (*Id.*, p. 7.345.)
- 7 Dodge, 50-5th T.M., "Transfers With Retained Interests and Powers," p. A-23.
- 8 I.R.C. § 2702(c)(2), enacted in 1990.
- 9 Pennell, *Estate Planning*, Vol. II, § 7.3.4.1, p. 7.334 (Aspen, 6th ed.).
- 10 The best example is the 2001 Tax Act (EGTRRA), which has as its ultimate goal the repeal of the estate tax.
- 11 See note 23 and the text to which it relates.
- 12 If the settlor's interest applied to all the trust's assets, then they would all be included in the settlor's gross estate. However, if the settlor only desired an interest in part of the trust's assets, then only the proportion "retained" would be included in the settlor's gross estate. (Reg. § 20.2036-1(a). See *Mahoney v. United States*, 831 F.2d 641 (6th Cir. 1987); *Estate of Tomac v. Comm'r*, 40 T.C. 134 (1963); Rev. Rul. 79-109, 1979-1 C.B. 297.) This provides a hedge for the more conservative settlor and planner.
- 13 U.S. Const. art. I, § 10, cl. 1.
- 14 Osborne, "Asset Protection and Jurisdiction Selection: Clearing Up Your Situs Headaches," *supra*, note 6, at 14-26.
- 15 *Id.*
- 16 *Id.* See also Boxx, "Gray's Ghost: A Conversation About the Onshore Trust," 85 Iowa L.R. 1195, at 1230 (2000).
- 17 *Id.*, Boxx at 1240.
- 18 See section entitled, "The Planning Dilemma: Early Gifting Versus Future Possible Needs."
- 19 Boxx, "Gray's Ghost: A Conversation About the Onshore Trust," *supra*, at 1240, n.295.
- 20 If administration, then the settlor's choice of law in the trust instrument controls (Restatement (Second) Conflict of Laws § 273(b).) If validity, then again, the settlor's choice will prevail, "provided that this state has a substantial relation to the trust and that the application of its law does not violate a strong public policy of the state with which, as to the matter at issue, the trust has its most significant relationship under the principles stated in § 6 ...." (*Id.*, § 270.)
- 21 For example, factual determinations may need to be made concerning whether Alaska has a substantial relation to the trust, and which state has the most significant relationship to the trust.
- 22 Further analysis of this conflict of laws issue may be found in Blattmachr and Zaritsky, "North to Alaska: Estate Planning Under the New Alaska Trust Act," *supra*, note 13; Hogan, "Once More Unto the Breach: Planning for a Conflict of Laws With Alaska and Delaware Self-Settled Spendthrift Trusts," *supra*, note 6; and, generally, in Moore, "Choice of Law in Trusts: How Broad is the Possible Spectrum?" 36th U. of Miami Heckerling Inst. on Est. Plan. (2002).
- 23 U.S. Const. art. IV, § 1.
- 24 18 Moore's Federal Practice § 130.04[3] (Matthew Bender 3rd ed.).
- 25 *Id.* Restatement (Second) of Conflict of Laws § 92, comment e.
- 26 Jurisdictional issues may be very fact dependent. For example, there may be arguments that long-arm jurisdiction is appropriate due to a corporate trustee's activities in the domiciliary state, which may include advertising, attendance at conferences, articles in national press, and Web site material. (See Boxx, "Gray's Ghost: A Conversation About the Onshore Trust," *supra*, at 1211-12.)
- 27 *Id.* at 1227.
- 28 *Id.* at 1215.
- 29 See Osborne, "Asset Protection and Jurisdiction Selection: Clearing Up Your situs Headaches," *supra*, note 6, at 14-24 for a full discussion of this statutory interpretation argument.
- 30 U.S. Const. art. VI.
- 31 Resident settlors could still rely on the Alaska SSDS Trust statute as a state law exemption independent of section 541(c)(2). Nonresident settlors could not because section 522(b)(2) of the Bankruptcy Code limits state law exemptions to those of the debtor's domicile state.
- 32 See the choice of law discussion above with respect to the Full Faith and Credit Clause scenario.
- 33 See note 48.
- 34 This scenario has occurred involving offshore trusts. See Boxx, "Gray's Ghost: A Conversation About the Onshore Trust," *supra*, at 1227-30.
- 35 *Id.* at 1229.
- 36 *Id.*
- 37 *E.g.*, *Federal Trade Comm. v. Affordable Media, LLC*, 179 F.3d 1228 (9th Cir. 1999).
- 38 See note 13. Only two private-letter rulings exist: P.L.R. 9837007, which held gifts were complete when made to an Alaska SSDS Trust designed for transfer tax reduction, and P.L.R. 200148028, which held gifts were incomplete when made to a Delaware trust designed only for asset protection and also held that the Delaware trust was not a grantor trust for income tax purposes.
- 39 In regard to personal jurisdiction issues, Professor Boxx states, "unfortunately, a decision that would expose the trust assets to the judgment in this context would be too fact-specific to have much relevance to future cases, since it would turn on personal jurisdiction of a particular state over a particular trustee. However, depending on the policy analysis done to determine personal jurisdiction, the decision could be a sufficient cautionary tale that would make the trusts less attractive or, at least, affect future litigation strategy." ("Gray's Ghost: A Conversation About the Onshore Trust," *supra*, at 1221, n.149.)
- 40 In regard to the I.R.C. § 2036(a)(1) issue, one commentator concludes, "[t]his issue will take time to resolve, and there may be fits and starts as various courts analyze the question." (Pennell, *Estate Planning*, Vol. II, § 7.3.4.2, pp. 7.345-346 (Aspen, 6th ed.).)
- 41 If spouses are co-settlors, conservative drafting will include a provision that states that if trust assets are included in the gross estate of the first settlor to die, then such assets will be distributed to a QTIP trust for the surviving spouse.
- 42 Code section 2001(b).

## Recent Developments

### Real Property

by Scott B. Osborne, Preston Gates & Ellis LLP, Seattle

#### Old Business

There are two cases that were discussed in prior editions of the Newsletter that need to be revisited.

First, the Ninth Circuit modified the opinion in *In re: Stanton*, 285 F.3d 888, 2002 U.S.App. LEXIS 6495 (9<sup>th</sup> Cir. 2002). This opinion, noted in the Summer 2002 edition of the newsletter (pages 9-10) and discussed by Tim J. Filer in this edition, used the doctrine of discretionary versus mandatory advances to allow a trustee in bankruptcy to gain priority over a recorded deed of trust securing a guaranty of a line of credit. As noted in Tim Filer's article, several groups (with a lender orientation) petitioned the Court of Appeals for a rehearing. The Court did not grant the rehearing, but it did amend the opinion.

The Ninth Circuit in *In re: Stanton*, 2002 U.S.App. LEXIS 18773 (September 13, 2002) made modifications to its original opinion that eliminated language that could be interpreted as holding that application of the optional versus mandatory advance theory rendered the line of credit lender secured by a mortgage on the bankrupt guarantor's residence junior to the trustee in the guarantor's bankruptcy. The language below shows the changes in the opinion (strike-through is deletion; underlining is new text) including the replacement of the text of an entire footnote:

This does not necessarily mean that International Factors necessarily wins all the marbles. Under *John M. Keltch* (n.15) and under *National Bank of Washington v. Equity Investors*, (n.16) it matters would matter that the factor had discretion whether to make the subsequent advances to Fleet, and was not obligated to do so. *National Bank of Washington* holds that "where the advances of promised loan moneys are, under an agreement to lend money, largely optional . . . liens attaching prior to an optional advance would thus be superior to it." (n.17) This does *not* mean that when International Factors loan money to Fleet after the Stantons went bankrupt, a *new lien* was created on the Stantons' house. If National Bank of Washington is still good law, it would mean ~~It means~~ that when these optional advances to Fleet were made, the factor's lien on the house, to the extent of these subsequent advances, was junior to the priority of intervening claims. National Bank of Washington thus would affect ~~Thus, the bankruptcy trustee was senior to the factor's lien for advances the factor made after the Stantons filed for bankruptcy. Washington law thus affects the priority of an optional lien but does not change the existence of the lien itself. Following a 1973 amendment to the lien priority statute in the mechanics' lien chapter, it may be that National Bank of Washington is either limited in the mechanics' lien context or entirely abrogated. (n.18) But the parties neither briefed this issue nor addressed it in their argument to us. We thus need not reach the question whether~~

any advances made post-petition are subordinate to intervening claims, and we leave that to the bankruptcy court to determine if necessary or remand.

The factor's lien preexisted the bankruptcy. No one violated the automatic stay provision. Neither the factor nor Fleet manufacturing needed court permission for the factor to advance additional money to Fleet. To hold otherwise would allow the bankruptcy of a corporation's shareholder to clog the going business of the corporation and its creditors. ~~What did happen to the factor's security because of the bankruptcy is that its priority as to the proceeds from sale of the Stantons' house (rather than its lien) became limited to the extent of its advances prior to the bankruptcy, because subsequent advances were optional. The bankruptcy at most affected the priority of the factor's security interest, but not its existence.~~ (n.18)

n.18 ~~The dissent says "debtors' continued use of their house as collateral for Fleet's debts on new advances resulted in their incurring new and increased liability"; Dissent at 5336; and "they could not encumber [their house] after filing for bankruptcy without obtaining court approval." Dissent at 5336 n.4. Once people have mortgaged their house, it really isn't up to them whether to "continue use of their house as collateral." It already is collateral. The Stantons did not "encumber" it after filing for bankruptcy. They encumbered it prior to bankruptcy, when they gave the factor a lien on it. The Stantons didn't do anything affecting the lien after bankruptcy and the factor didn't do anything without court approval to create or perfect the lien (it had already been created and perfected before the bankruptcy). The factor loaned Fleet, a separate person from the Stantons, more money after bankruptcy, which affected the amount secured by the preexisting lien. See RCW 60.04.226. Compare Comment, Mechanics' Liens: The "Stop Notice" 49 Wash.Law Review 685 (1974) (in the case of mechanics' liens, the optional advances rule no longer applies); and William B. Stoebuck, 18 Wash.Pract. Real Estate: Transactions §17.25 (2002 Pocket Part) ("On its face, the section is not limited to construction mortgages, but, because it was originally enacted as a package with the stop-notice statute, which specifically applies to construction lenders, it might be argued that future-advances mortgages for other purposes are not within its intent.").~~

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## Recent Developments: Real Property

The outcome of the case was not changed; the matter was remanded to the bankruptcy court for further proceedings, albeit with a significantly different "spin." Presumably this will include a determination as to whether RCW 60.04.226 has application beyond mortgages securing construction loans. At least the Circuit Court left this issue open for further determination, rather than send the matter back to the trial court with an opinion that ignored the possibility that RCW 60.04.226 had some effect on the rule announced in *National Bank of Washington*.

The author of this column received a letter from Robert Siderius, who is with Jeffers, Danielson, Sonn & Aylward, P.S. in Wenatchee. He had a comment on the summary of *Howe v. Douglas County*, 146 Wn.2d 183, 43 P.3d 1240, 2002 Wash.LEXIS 252 (2002), which was discussed in the Summer 2002 edition of the Newsletter (page 11). The summary of *Howe* stated that the Court "invalidated" a covenant in a deed purporting to waive damage claims "arising from the construction and maintenance of public facilities." Mr. Siderius believed that this was an overly broad characterization of the ruling, and that may be a fair criticism. What the Court held was that to the extent the covenant attempted to shield the County from liability for its own negligence, the covenant would not be enforced. The Court stated:

The primary question is whether, and if so, to what extent this waiver violates the legislative abrogation of sovereign immunity.... The Howes argue that conditioning a building permit upon an exculpatory waiver violates the letter and spirit of RCW 4.96.010 by resurrecting sovereign immunity. We agree that if this waiver does resurrect sovereign immunity, it violates state law and is thus void. *Howe*, p. 188.

Where governments must, by law, accept streets, public areas, and other improvements constructed by a private developer, they may limit their liability for harms caused by the private developer. That is precisely what RCW 58.17.165

requires, and impliedly what it authorizes.... The County's interpretation of this waiver goes far beyond the type authorized by RCW 58.17.165 and, to the extent it exculpates the county for its own future negligence, violates the Legislature's explicit abolition of sovereign immunity. Blanket grants of immunity secured routinely for the performance of a public function, such as granting a plat or development, differ little from passing ordinances immunizing the granting body from actions for its own negligence, and are not allowed.... A narrowly drafted release for risks specific to a particular activity or condition is not an impermissible attempt to functionally recreate sovereign immunity and does not violate RCW 4.96.010... To the extent that this waiver limits the County's liability for otherwise actionable negligence, it is void. *Howe*, pp. 190-191.

Mr. Siderius' comments are appreciated (not the least because they show that someone actually reads this material!), because they highlight one of the significant implications of *Howe* and its companion case, *1515-1519 Lakeview Boulevard Condo Ass'n v. City of Seattle*, 146 Wn.2d 194, 43 P.3d 1233, 2002 Wash. LEXIS 250 (2002). The Washington Supreme Court has held that covenants purporting to waive damage claims can be effective to bind subsequent owners of the property. Assuming the Supreme Court is willing to apply this holding in the context of non-governmental covenants, these rulings offer private parties increased latitude in shifting liability for certain property related matters. The rationale employed by the Supreme Court should validate covenants imposed by sellers of property seeking to avoid liability to subsequent transferees for hazardous materials or other physical conditions of the property.

In the interest of full disclosure, it should be noted that Mr. Siderius represents one of the defendants in the *Howe* case, and the matter is still pending in Superior Court.

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## SUPREME COURT OF THE STATE OF WASHINGTON

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The holding of the Court of Appeals that an agreement to sell a cooperative apartment unit constituted an agreement to convey an interest in real property was reversed in *Firth v. Lu*, 146 Wn.2d 608, 49 P.3d 117, 2002 Wash. LEXIS 417 (2002). Firth and Lu had entered into an agreement to purchase a cooperative apartment unit in the Maryland Apartments in Seattle. After signing an agreement to sell the unit, the seller sought to renegotiate the purchase price. Firth sued to specifically enforce the agreement, and the trial court entered a summary judgment compelling Lu to transfer the share of stock associated with the apartment.

The Court of Appeals reversed the trial court, ruling that the agreement to sell the unit was an agreement to sell an interest in

real property. Since no legal description had been included in the agreement, the Court of Appeals concluded that it was unenforceable under the statute of frauds, RCW 64.04.010.

The Washington Supreme Court reversed and remanded the case to the Court of Appeals to consider alternative grounds upon which the summary judgment might be affirmed. The majority opinion, written by Justice Sanders, held that the only interest owned by the seller was that represented by shares of stock in the cooperative. While the ownership of the stock entitled the owner to a lease of the apartment unit, the shares were not an interest in real property. The Court drew a distinction between the

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## Recent Developments: Real Property

Washington statute of frauds and provisions of New York and New Jersey law that had been relied upon by the Court of Appeals in reaching an opposite conclusion.

This ruling does not have a particularly widespread application. There have been only a few cooperative apartment buildings in Washington. The cooperative form of ownership has been used for a handful of apartment buildings in Seattle and a number of houseboat communities that have acquired the ownership interest to the dock facilities that provide moorage. The ruling was significant, however, for reasons not mentioned in the opinion. Since sales of cooperative apartment units have been treated as stock sales, the transactions do not require payment of real estate excise tax. Had the Supreme Court held that these transfers involved a transfer of an interest in real estate, it is possible that excise taxes would have been imposed on past transfers. In addition, past transactions that did not conform to the formalities of real estate transfers (legal descriptions and conveyances in deed form) might be subject to attack.

The other interesting aspect of this opinion was that it was authored by Justice Sanders. The last Supreme Court opinion to invalidate a real estate purchase agreement due to the failure to include a legal description of the property was *Key Design v. Moser*, 138 Wn.2d 875, 983 P.2d 653 (1999). Justice Sanders dissented in that case, noting that in his opinion there was little virtue in following a rule that allowed parties to repudiate their otherwise lawful agreements. Given that prior position, it is not surprising that Justice Sanders declined to extend the application of RCW 64.04.010 to cooperative transactions.

As part of real estate financing transactions, it is customary to conduct searches of filings made pursuant to the Uniform Commercial Code to determine if there are any prior liens affecting personal property that might be involved in the transaction. *Puget Sound Financial v. Unisearch*, 146 Wn.2d 428, 47 P.3d 940, 2002 Wash. LEXIS 333 (2002) considered the liability of the company that made the records search in the event the search failed to disclose previously filed financing statements.

Puget Sound Financial proposed to loan \$100,000 to The Benefit Group. PSF ordered a UCC search from Unisearch. The charge for the search was \$25, and the invoice submitted by Unisearch stated that the liability of the company in connection with the search was limited to the fee that was charged. The search proved erroneous; there was a prior security interest in favor of another lender that had been filed under a slightly different version of the debtor's name. PSF sued for damages. The trial court ruled that damages were limited to the \$25 fee charged for the search. PSF appealed and the Court of Appeals reversed the trial court.

The Washington Supreme Court concluded that the limitation of liability stated on the Unisearch invoice was part of the contract between Unisearch and PSF. This contract term was not unconscionable in light of the totality of the circumstances surrounding the transaction between Unisearch and PSF. The Court reinstated the trial court ruling, and limited any damages as a result of the faulty search to the \$25 fee paid.

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## NINTH CIRCUIT COURT OF APPEALS

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Finally, there were two Ninth Circuit cases dealing with "taking" issues. Both cases concluded that the property owner asserting the claim did not own the interest in the property that supposedly had been taken. *King County v. Rasmussen*, 299 F.3d 1077, 2002 U.S. App. LEXIS 16044 (2002) involved a dispute over the title to an abandoned railroad right-of-way. The railroad had sold the right-of-way to King County and a conservancy organization. Abutting property owners contended that the right-of-way reverted to the adjacent property owners.

The determinative issue in the opinion was the character of the original conveyance to the railroad – was this a conveyance of the entire fee or an easement? The Court's opinion is a comprehensive summary of Washington law on the subject of the nature grants to railroads. The Court concluded that since the conveyance did not purport to limit the use of the property conveyed to railroad use, the intention of the grantor was to convey the entire fee interest in the land, as opposed to easement for use only as a railroad right-of-way. Rasmussen did not own

any reversionary interest in the property conveyed to King County, so no taking occurred.

In *Esplanade Properties v. City of Seattle*, 307 F.3d 978, 2002 U.S. App. LEXIS 20803 (2002), the Court affirmed the summary dismissal of a developer's claim against the City of Seattle arising from the denial of development permits. The property owner had acquired tidelands below Magnolia Bluff that had been platted as residential lots. The property was submerged by navigable waters for approximately one-half of the time, and the when not submerged, was a large sand bar. In 1992, the developer proposed to construct homes located on pilings on the property.

The City refused to issue building permits, citing the size of the proposed piers, the design of the causeway leading to the property and the lack of parking on dry land as aspects of the proposal that failed to comply with existing City codes. The developer appealed the City's interpretation of its codes, but the City's position was ultimately upheld in state court. After the

continued on next page

## Recent Developments

# Probate and Trust

by Alice M. McCarty, Graham & Dunn, P.C., Seattle

### SUPREME COURT OF THE STATE OF WASHINGTON

*Estate of Bachmeier*, 147 Wn.2d 60 (2002)

**Summary:** Where there is a three-pronged community property agreement (“CPA”), the court will not imply a termination of the testamentary prong by operation of law where there is a finding that the parties have permanently separated and the marriage is defunct at the time of death.

**Facts:** In 1966, John and Angie Bachmeier were married. In 1977, they executed a three-pronged CPA that provided that all property then owned or thereafter acquired would be declared community property and that upon the death of either of them, all of the community property would immediately vest, in fee simple, in the surviving spouse.

In 1995, the Bachmeiers suffered marital problems. John wrote (but never sent) a letter, indicating that he would “sever ties with Angie” and detailing the items he would keep and allow Angie “to do as she pleases with the rest.” In 1998, John left the family home, filed a petition for legal separation and requested a division of the parties’ accumulated property.

Later in 1998, during the Bachmeiers’ separation, and two days before Angie died, Angie executed a Will, naming her

daughter, Sandra L. Johnson, as personal representative of her estate. Angie left her entire estate to her daughter and named her other six children as contingent beneficiaries. Angie expressly left nothing to John.

Sandra petitioned to admit the Will to appointing herself as personal representative to probate. John moved to dismiss the petition, or alternatively, for orders to appoint him as personal representative. The court admitted the Will to probate, but appointed John as personal representative.

Sandra petitioned the trial court for a ruling either that John and Angie had revoked their CPA or that the CPA had terminated as a matter of law when their marriage became defunct. The trial court dismissed the petition, concluding that the CPA was neither revoked nor terminated.

The appellate court reversed the trial court, holding that a termination clause could be implied in the CPA as a matter of law if the marriage became defunct. The Washington State Supreme Court reversed this decision.

**Discussion:** The Washington State Supreme Court reviewed whether a CPA could be terminated by implication, in the absence of a final divorce decree or mutual revocation, but where the marriage has become defunct. RCW 26.16.120 allows a husband and wife to execute a community property agreement. However, the statute does not address revocation of such an agreement.

Despite the silence of the statute, CPAs that do not include express terms of revocation may be set aside in two circumstances. First, a CPA is rendered inoperable where there is a final divorce decree and not merely a petition for dissolution. *In re Lyman’s Estate*, 7 Wn. App. 945, 950 (1972). Second, the parties may rescind the agreement by mutual assent. *Higgins v. Stafford*, 123 Wn.2d 160, 166 (1994).

Given the facts in *Bachmeier*, the Washington State Supreme Court found that the Bachmeier CPA had not been mutual abandoned either by John’s initiation of legal separation proceedings or by Angie’s execution of an inconsistent Will. The Washington State Supreme Court reasoned that each of these acts, even though executed to reach an arguably similar goal, was considered unilateral and therefore, did not meet the test of mutual revocation. The court also declined to imply a clause terminating the testamentary provision of a CPA where the parties had been separated for a prolonged period of time but where a final divorce decree had not been entered and the parties’ acts were unilateral. Thus, in reversing the appellate court, the Washington State Supreme Court held that a community property agreement did not terminate by implication when a marriage became defunct.

*continued from previous page*

### Recent Developments: Real Property

developer failed to submit a revised application, the City cancelled the permit application in 1998. The developer sued the City in 2000 claiming damages from the inverse condemnation of the property.

The district court dismissed the developer’s claim in a series of summary judgments, culminating in a final ruling that no taking had occurred under the Fifth Amendment of the United States Constitution because the City’s action was not the proximate cause of the claimed damage, and, alternatively, that “background principles” of Washington law would have prevented the development.

The Court of Appeals affirmed on the basis of the district court’s alternative ruling. Under Washington law, the developer never had a right to develop the navigable tidelands in the first place. The “public trust doctrine,” which “unquestionably burdens Esplanade’s property . . . ran with the title to the tideland properties and alone precluded the shoreline development proposed by Esplanade.” Since the developer acquired the property already burdened by this development restriction, the actions of the City could not result in the taking of a non-existent development right.

## Notes from the Chair

by Warren Koons, Davis Wright Tremaine LLP, Bellevue

Greetings! It is indeed an honor to serve as your Section Chair for the 2002-03 business year. The RPPT Section continues to be among the strongest and most active sections in the WSBA. Not only are we the WSBA's largest section (approximately 2,200 members), but we have excellent leadership on the Executive Committee and exceptional editors and assistant editors for the RPPT Newsletter and RPPT Web site. Add to this an increasingly positive and active working relationship with the leadership of the WSBA, and I think it is safe to say that the Section is poised to provide outstanding services to our members in the coming year.

If you missed the Midyear Meeting at Skamania Lodge in June, you missed a good one. Among other highlights, Justice Richard Sanders of the Washington State Supreme Court regaled us with his thoughts from "Behind the Velvet Curtain." Many thanks to our co-chairs for the Midyear, Lora Brown and Zach Stoumbos, for putting together a great program.

You may have wondered whatever happened with the "RPPT Two-Minute Member Survey" sent out last spring. The answer is we had an overwhelmingly positive response—574 members responded to the survey! That is truly remarkable—many thanks to each of you who responded. Thanks to the survey results, we now have a good baseline of information about the makeup of our section, a better understanding of the preferences and opinions of the membership on various section-related issues, and a long list of members (12% of respondents) willing to volunteer for activities within the section. (Some of you volunteers have already been contacted—if you haven't been contacted yet, just wait—you'll likely be called upon one of these days soon.) We will put this information to good use as we plan for future CLEs and Midyear Meetings and as we decide what materials to put in the RPPT Newsletter, on the RPPT Web site, or otherwise make available to section members.

A few interesting highlights of the 2002 RPPT Survey results:

- **55%** in practice over 20 years
- **24%** licensed to practice in states other than Washington
- **8%** actively practicing in other states
- **14%** practice all real property; **14%** practice all probate/trusts/estates
- **29%** practice 25-75% real property; **28%** practice 25-75% probate/trusts estates
- Practice in Eastern Washington (**19%**), Puget Sound (**64%**), other (**11%**).
- Solo practitioners **19%**; lawyers in private firms **64%**
- Lawyers in organizations of less than 5 (**50%**), 5-20 (**19%**), 21-50 (**7%**)

- Level preference for CLEs: advanced (**55%**), intermediate (**36%**), basic (**7%**)
- Active in other WSBA Sections: Elder Law (**10%**), Taxation (**9%**), Business Law (**8%**), Environmental/Land Use (**7%**), World Peace through Law (**0.18%**)
- Would use RPPT Web site if current/relevant: Yes (**68%**), No (**18%**)

The Executive Committee along with the Newsletter and Web site editors and assistant editors plan to continue to improve the currency, content and relevancy of the Section CLEs, Midyear Meeting, Newsletter and Web site. We are committed to trying to make more and better resources available to the section membership—particularly resources that are of practical value to you in your everyday practices. One example of what we are doing is our plan to place selected chapters of the Real Property Deskbook and Community Property Deskbook, in word-searchable forms, on the RPPT Web site in the coming months. We are also continuing to work collaboratively with the WSBA to try and find a way to make the Real Property Deskbook and Community Property Deskbook available to the section members in a more affordable and useable format (either an online or as a CD). In addition, we are contemplating overseeing an effort, in partnership with the WSBA, to put together a single volume set of selected "bread and butter" chapters of the Real Property Deskbook and a single volume deskbook on Trusts and Estate Planning. We will, of course, continue to be active with regard to legislative matters as well.

I would like to close by singling out for special kudos and praise our RPPT Web site editor, Doug Lawrence. Doug is perhaps the most valuable member of our Section leadership team—in the last year he has personally spearheaded a total revamping and upgrade of the RPPT Web site, including establishing separate electronic mail groups for both the real property and probate and trust sides. And he continues to work on making technical improvements, adding useful content, and keeping the Web site current. Thanks to Doug, the RPPT Web site is now a very user-friendly and useful place to go for information about the section, as well as information and materials in the substantive areas of real property and probate, trusts and estates. Given Doug's boundless creative energies, the Web site is only going to get better and better. If you haven't been there lately, I highly recommend that you pay a visit to [www.wsbarppt.com](http://www.wsbarppt.com). You'll be very pleasantly surprised.

*Readers are invited to e-mail the author with comments or suggestions, or to express an interest in assisting in Section activities, at [warrenkoons@dwt.com](mailto:warrenkoons@dwt.com).*

## Technology for Lawyers: Internet 101 – Getting Started

by Jody M. McCormick, Witherspoon, Kelley, Davenport & Toole, P.S., Spokane and  
Brian J. Danzig, Lane Powell Spears Lubersky, LLP, Seattle

Technology is an essential component of today's modern legal practice. Accordingly, the Editorial Board decided to include a technology-focused article as a regular feature in the newsletter. If you are a self-proclaimed "techno-phobe" or feel like the "technology ship" has sailed without you, this feature is here to get you started, help you master the basics, and learn the high art of making technology work for you.

To initiate this feature, we will start with something not commonly encountered in law practice—free advice. There are hundreds of valuable Web sites on the Internet providing access to legal information *for little or no cost*. The following Web sites are 10 that every lawyer should know:

1. [www.findlaw.com](http://www.findlaw.com). This Web site is a great place to start and offers hyperlinks to primary materials, cases, legal publications, forms, etc. The topics are indexed for easy maneuverability. Because of the broad depth of information available at this site, it is particularly helpful when you don't know what you are looking for.
2. [www.megalaw.com](http://www.megalaw.com). This site is very similar to findlaw.com. Try and use both. You may develop a personal preference or find material available only on one of the sites.
3. [www.law.cornell.edu](http://www.law.cornell.edu). Again, similar to findlaw.com and megalaw.com in that it provides access to primary materials, cases, etc. However, its home page lists "Law Events Recently in the News" with hyperlinks to the cases, statutes or articles that are making news. A weekly visit to this site will keep you abreast of legal issues making national news.
4. [www.law.com](http://www.law.com). A Web site for lawyers with an emphasis on the business aspects of the practice.
5. <http://thomas.loc.gov>. This site is U.S. Congress' official site and contains information regarding past, present and pending federal legislation. It provides common names of bills, the ability to search by public law number, committee membership and reports and more.
6. [www.leg.wa.gov/rcw/index.cfm](http://www.leg.wa.gov/rcw/index.cfm). This site contains the text of the Revised Code of Washington. While the annotations are not available on this site, it is useful to access the RCW at your desk. Statutes can be printed or copied for attachment or inclusion in legal memoranda or briefs.
7. [www.secstate.wa.gov](http://www.secstate.wa.gov). This is the Washington Secretary of State's Web site. Most notably, you can search corporate existence and the status of any foreign or domestic corporation, limited liability company or limited partnership

in Washington. The direct address for the corporate database search is [www.secstate.wa.gov/corps/search.aspx](http://www.secstate.wa.gov/corps/search.aspx). As a side note, most states (Delaware being the most notable exception) have searchable corporate databases available for no cost on the Web.

8. [www.pacer.psc.uscourts.gov](http://www.pacer.psc.uscourts.gov). Access the dockets, case assignments and even the actual pleadings (not available for every court, but for a respectable number of courts) filed in federal courts without leaving your office. This service is available for a minimal fee.
9. [www.martindale.com](http://www.martindale.com). Need to refer a case to another state? Know of a lawyer in another state, but have misplaced her address and telephone number? This site can help. You may search for lawyers by name, practice area, law school, etc.
10. [www.anywho.com](http://www.anywho.com). This is the online version of a nationwide telephone book. You can find people or businesses. There are several similar Web sites on the Internet. This site also contains a reverse telephone directory.

Many of these Web sites may be reached through links at the new Real Property, Probate and Trust Section Web site, [www.wsbarrpt.com](http://www.wsbarrpt.com). To bookmark these pages (i.e., to save them in your computer's memory for future reference) in Internet Explorer, go to the site, click the "Favorites" tab at the top of your screen and click on "Add to Favorites." To find the site again, click the "Favorites" tab, slide down to the desired site and click.

Also currently available at [www.wsbarrpt.com](http://www.wsbarrpt.com) is a compendium of additional links to free resources on the Internet, "The Benefits of On-Line Research," by Douglas C. Lawrence, Esq. If you do not yet feel savvy enough to surf the Web alone, the next issue of the Newsletter will identify the top Web sites for real property, probate and trust lawyers.

*Readers are invited to submit ideas for useful and practical technology articles to the authors. Ideas may be sent via e-mail to Jody McCormick at [jmm@wkdtlaw.com](mailto:jmm@wkdtlaw.com) or Brian Danzig at [danzigb@lanepowell.com](mailto:danzigb@lanepowell.com).*

# The Necessity of Family Consent: Assisting Clients with Organ and Tissue Donations

by Peter C. Wolk, Law Office of Peter C. Wolk, Washington, D.C.<sup>1</sup>

A major cause of the shortage of organs is that regardless of a decedent’s wishes, virtually no surgeon will take organs or tissue without permission from the family. Regrettably, family members often withhold authorization because they are unaware the decedent wished to donate organs and tissues, thereby frustrating organ donors’ wishes. Under each state’s law, properly signing an organ donor card or a driver’s license fully satisfies the legal requirements of becoming an organ and tissue donor. However, in practice, virtually no surgeon will take organs or tissue without family consent. Yet, every day lawyers inaccurately advise their clients that signing one of these documents is all clients have to do to become organ donors.

A national study conducted by Gallup indicates that when family members know of their loved one’s wishes, 94% will honor the request. But when family members do not know, only 54% will donate the relative’s organs. Indeed, of all the causes for organs being unavailable from people who wanted to be donors, 37% are lost due to the family’s refusal to consent. Those lost organs (from people who *wanted* to be organ donors) could save many lives.

Attorneys are uniquely positioned to help by asking clients during estate planning and Will intake sessions if they want to be organ donors and if they have told their family. (Whether someone decides to be or not to be an organ donor is a personal decision that is respected; the purpose here is to ensure that people who want to make anatomical gifts do not have their wishes thwarted.) Sharing the decision to be an organ donor also has the effect of sparing surviving family members from the difficulty of having to make a burdensome, personal decision at an emotional time.

The American Bar Association supports more client education about organ donation issues:

RESOLVED, That the American Bar Association urges all attorneys to raise with their clients, when appropriate, the topic of organ and tissue donations and to provide donation forms to those clients who indicate an interest in making a donation.

Summary of Action of the House of Delegates, American Bar Association 1992 Mid-Year Meeting, Dallas, Texas, p. 30 (February 3-4, 1992). (Full text of the Resolutions and additional organ donor information is printed in the ABA pamphlet: “A Legacy for Life” (free on the ABA Web site; \$12/720 pamphlets in print).

## As a lawyer, you can help by asking your clients the following questions during Will intake interviews:

1. Do you wish to be an organ and tissue donor?

Self      Yes \_\_\_\_      No \_\_\_\_

Spouse    Yes \_\_\_\_      No \_\_\_\_

2. If yes, have you signed an organ donor card or indicated on your driver’s license your intent to be an organ and tissue donor?

Self      Yes \_\_\_\_      No \_\_\_\_

Spouse    Yes \_\_\_\_      No \_\_\_\_

3. Have you told your family about your intention to be an organ and tissue donor?

Self      Yes \_\_\_\_      No \_\_\_\_

Spouse    Yes \_\_\_\_      No \_\_\_\_

\*\*\*\*\*

Statistics and additional information about organ and tissue donation is available at the United Network for Organ Sharing Web site ([www.unos.org](http://www.unos.org)) and at the Division of Transplantation, U.S. Department of Health and Human Services Web site ([www.organdonor.gov](http://www.organdonor.gov)). Local organizations that offer assistance and information include LifeCenter Northwest ([www.lcnw.org](http://www.lcnw.org) or 425-201-6563) and for Clark, Cowlitz, Skamania and Walla Walla Counties, Pacific Northwest Transplant Bank ([www.pntb.org](http://www.pntb.org) or 503-494-5560).

1 © 2002 Peter C. Wolk. Reprinted with permission. Mr. Wolk is working on a lawyer education outreach project for the United States Division of Transplantation. This article is adapted from articles published in the D.C. Bar, Texas Bar and Elder Law newsletters.

## Practical Practice Tips: Non-Judicial Foreclosures

by Shelley N. Ripley, Witherspoon, Kelley, Davenport & Toole, P.S., Spokane

The deed of trust has become the favored security device against real property in the state of Washington since the adoption of Washington's Deed of Trust Act, RCW 61.24 *et. seq.*, in 1965. A deed of trust is a three-party mortgage with the power of sale vested in a trustee. Under a deed of trust, the borrower conveys the property to a trustee in trust for the lender to secure an obligation owed to the lender.

Generally, a deed of trust is foreclosed upon non-judicially. A non-judicial foreclosure action is usually more efficient and less expensive than a judicial foreclosure. The non-judicial foreclosure process is strictly statutory.

A non-judicial foreclosure action may be commenced if the following prerequisites have been met: (1) the deed of trust contains a power of sale clause; (2) the deed of trust contains a non-agricultural clause; (3) a default in one of the covenants has

occurred; (4) no other action has been commenced to seek satisfaction of the obligation; and (5) the deed of trust has been recorded in each county in which the real property is situated. RCW 61.24.030.

Published on pages 19 through 22 of this Newsletter is a Non-Judicial Foreclosure Checklist to assist in the non-judicial foreclosure of a deed of trust. The checklist is intended to be used as a guide and is not meant to constitute or be a substitute for legal advice for specific situations.

*We are pleased to introduce the "Practical Practice Tips" column as a new feature of the newsletter. Readers are invited to submit ideas for articles via e-mail to Beth McCaw at [bmccaw@wkg.com](mailto:bmccaw@wkg.com).*

### RPPT Web Site News

The RPPT Web site has moved to a new location – [www.wsbarppt.com](http://www.wsbarppt.com). Readers are invited to visit the site frequently to track pending legislation affecting real property, probate and trust lawyers, to register for continuing legal education seminars, and to read past issues of the newsletters.

Recent additions to the RPPT Web site include selected chapters of the Washington Real Property Deskbook and the Washington Community Property Deskbook. The Web site offers text search capabilities for both past newsletters and the deskbooks to make research easier. The Web site also offers links to many of the online resources featured in this issue's technology column.

The RPPT electronic discussion groups have recently moved to an ad-free host, Topica.com. The groups ([wsbarp@topica.com](mailto:wsbarp@topica.com) and [wsbapt@topica.com](mailto:wsbapt@topica.com)) provide a forum for section members to discuss issues of interest, pose legal questions, and share expertise via e-mail. Readers who have not already joined the discussion groups are invited to do so by visiting [www.wsbarppt.com](http://www.wsbarppt.com) or the group pages, [www.topica.com/lists/wsbarp](http://www.topica.com/lists/wsbarp) and [www.topica.com/lists/wsbapt](http://www.topica.com/lists/wsbapt). For assistance relating to the Web site or the electronic discussion groups, please contact the RPPT Web site editor, Doug Lawrence, at [doug.lawrence@stokeslaw.com](mailto:doug.lawrence@stokeslaw.com).

### Speak Out!

Wanted: Lawyers to volunteer to speak to schools and community groups on a variety of topics. For more information about the WSBA speakers bureau call Amy O'Donnell at 206-727-8213.



### WSBA Service Center

800-945-WSBA • 206-443-WSBA

[questions@wsba.org](mailto:questions@wsba.org)

# Non-Judicial Foreclosure Checklist

(non-judicial proceeding)

	<b>Date Accomplished</b>	<b>Item</b>	<b>Statutory Requirement</b>
1.	_____ Default Date	Default Date _ At least 190 days prior to sale _ Default letter sent by beneficiary	RCW 61.24.040(8)
2.		Original Note and Deed of Trust Received from Beneficiary?	
3.	_____ Date Recorded	Resignation and Appointment of Successor Trustee (if required) _ Draft Appointment of Successor Trustee _ Record in same county(ies) as Deed of Trust	RCW 61.24.010(2)
4.		Check Deed of Trust. Does it contain: _ Power of Sale Clause _ Non Agricultural Clause _ Has default occurred _ No judicial action pending _ Deed of Trust recorded in each county in which land is situated	RCW 61.24.030
5.		Verify Trustee has street address where personal service of process may be made (i.e. no P.O. Box )	RCW 61.24.030(6)
6.	_____ Date Ordered	Order Trustee's Sale Guarantee (i.e. title report)	
7.		Review Title Report for Junior Encumbrances Junior Lienors:  _____ _____ _____ _____ _____ _____	
8.		Review documents creating junior liens	
9.		Review Title Report for Senior Encumbrances Senior Lienors:  _____ _____ _____ _____	

Date Accomplished	Item	Statutory Requirement
10.	<p>Draft Notice of Default</p> <p>Must contain:</p> <ul style="list-style-type: none"> <li>_ description of property</li> <li>_ county(ies) DOT recorded and Auditor's No</li> <li>_ beneficiary has declared a default and a concise statement of default alleged</li> <li>_ itemized statement of amounts in arrears</li> <li>_ itemized statement of charges to be paid to reinstate before recording of Notice of Sale</li> <li>_ the sum of all arrears and fees clearly and conspicuously designated as amount to reinstate DOT before recording Notice of Sale</li> <li>_ a statement indicating that failure to cure an alleged default within 30 days of the mailing or personal service of the Notice of Default may lead to recordation, transmittal, and publication of a notice of sale and that the property may be sold at public auction at a date no less than 120 days in the future</li> <li>_ a statement indicating that the effect of the recordation, transmittal and publication of a Notice of Sale will be to increase the costs and fees and publicize the default and advertise the grantor's property for sale</li> <li>_ a statement indicating that the effect of the sale of the grantor's property will be to deprive the grantor of all its interest in the property</li> <li>_ a statement indicating that the borrower, grantor and any guarantor have recourse to the courts pursuant to RCW 61.24.130 to contest the alleged default on any proper ground</li> </ul>	<p>RCW 61.24.030</p> <p>(must be given 30 days before Notice of Trustee's Sale)</p>
11.	<p>_____</p> <p>Date Mailed</p> <p>_____</p> <p>Date Served</p> <p>_____</p> <p>Date Posted</p> <p>Serve Notice of Default on Grantor.</p> <ul style="list-style-type: none"> <li>_ Mail, regular and certified;</li> <li>_ Personally serve, and</li> <li>_ Post Notice of Default on Property                             <ol style="list-style-type: none"> <li>1. get picture of posting</li> </ol> </li> </ul>	RCW 61.24.030(7)
12.	Draft and Mail Validation Notice pursuant to the Fair Debt Collections Practices Act	
13	Draft Affidavit of Mailing and Affidavit of Service and Affidavit of Posting	
14.	<p>_____</p> <p>Sale Date</p> <p>Calculate Trustee's Sale Date</p> <ol style="list-style-type: none"> <li>1. Notice of Default given 30 days before Notice of Trustee's Dale</li> <li>2. Notice of Trustee's Sale recorded 90 days prior to sale date</li> <li>3. Must be held on a Friday (or Monday if previous Friday is a holiday)</li> </ol>	61.24.030(6)
15.	<p>_____</p> <p>Date Ordered</p> <p>Order Supplemental Title Report (i.e. date down report)</p> <ol style="list-style-type: none"> <li>1. verify if IRS liens</li> <li>2. verify if new parties to be served</li> </ol>	
16.	<p>Draft Notice of Trustee's Sale and Notice of Foreclosure</p> <ul style="list-style-type: none"> <li>_ must be in the same form as set forth in statute</li> <li>_ must be recorded no later than 90 days prior to sale</li> </ul>	<p>RCW 61.24.040(1)(f)</p> <p>RCW 61.24.040(2)</p>

Date Accomplished	Item	Statutory Requirement
17.	Mail Notice of Trustee's Sale and Notice of Foreclosure to Borrower/Grantor (regular and certified mail)	RCW 61.24.040 RCW 61.24.040(2)
18.	Mail Notice of Trustee's Sale (regular and certified mail) to: 1. junior lien holders (see above) 2. guarantor 3. occupants of the property 4. vendee in any real estate contract 5. lessee of any lease 6. persons requesting notice 7. any attorney of record for any junior lien holder (Do not need to serve senior lien holders)	RCW 61.24.040(1)(b)
19.	Draft Notice to Guarantor (commercial loan) Must State: ___ the guarantor may be liable for a deficiency judgment to the extent the sale price obtained at the trustee's sale is less than the debt secured by DOT ___ the guarantor has the same rights to reinstate the debt, cure the default, or repay the debt as is given to the grantor in order to avoid the trustee's sale ___ guarantor will have no right to redeem the property after the trustee's sale ___ subject to such longer periods as are provided in the Washington deed of trust act, chapter 61.24 RCW, any action brought to enforce a guaranty must be commenced within one year after the trustee's sale, or the last trustee's sale under any deed of trust granted to secure the same debt ___ in any action for a deficiency, the guarantor will have the right to establish the fair value of the property as of the date of Trustee's sale, less prior liens and encumbrances, and to limit its liability for a deficiency to the difference b/w the debt and the greater of such fair value or the sale price paid at the trustee's sale, plus interest and costs	RCW 61.24.042
20.	Personally Serve occupants or Post Notice of Trustee's Sale	RCW 61.24.040(1)(e)
21.	Mail Notice to Guarantor (if applicable) 1. certified and regular mail	
22.	Draft Affidavit(s) of Mailing	
23.	Draft Affidavit of Service or Posting	
24.	_____ Date Recorded Record Notice of Trustee's Sale (must be recorded no later than 90 days prior to sale date)	RCW 61.24.040(1)(a)
25.	_____ 1 <sup>st</sup> publish date Publish Notice of Trustee's Sale (excluding acknowledgement) 1. publish in each county in which property situated 2. must publish: _____ 2 <sup>nd</sup> publish date a. b/w 35 <sup>th</sup> and 28 <sup>th</sup> day before sale b. b/w 14 <sup>th</sup> and 7 <sup>th</sup> day before sale	RCW 61.24.040(3)

Date Accomplished	Item	Statutory Requirement	
26.	Search for tax liens 30 days prior to sale (i.e. order additional date down report) 1. if IRS lien, generate IRS tax lien notice 2. mail notice to IRS (regular and certified) 3. draft affidavit of mailing	26 USC 7425(b)	
27.	_____ Last day to Reinstate	Last day to reinstate by paying amounts in default (11 days prior to sale)	RCW 61.24.090(1)
28.	_____ Date Reinstated	Did Grantor Reinstate? Yes: _ prepare reinstatement/payoff checklist _ notice of discontinuance recorded _ amount tendered for reinstatement \$ _____ (only accept good funds)	
29.	_____ New Sale Date	Trustee to determine if sale to be continued Not more than 120 days from original sale date give notice of time and place of postponed sale publish notice in newspaper more than 7 days before new sale date	RCW 61.24.060(6)
30.	_____ Bid Amount	Secure Bid Amount from Client	
31.		Draft Trustee's Sale Script	
32.		Confirm Trustee's Sale w/Auctioneer (if applicable)	
33.		Obtain supplementary foreclosure report from title company through morning of sale	
34.		Trustee' Sale 1. Obtain Bid (only accept cash) 2. Complete sale receipt	
35.		Contact Client re: Sale	
36.		Order Date Down Report	
37.		Draft Trustee's Deed	
38.		Record Trustee's Deed	
39.		Write or Stamp on original Note "PAID BY FORECLOSURE SALE"	
40.		Owner's Title Policy Ordered	
41.	_____ Date to be Retained	Retain file for 6 years and 1 month	

## HOW TO REACH US

### Section Officers 2002-2003

**Warren E. Koons, Chair**

Davis Wright Tremaine LLP  
10500 N.E. 8<sup>th</sup> Street, Suite 1800  
Bellevue, WA 98004  
Ph: 425-646-6117  
Fax: 425-646-6199  
warrenkoons@dwt.com

**Barbara C. Sherland, Past Chair**

Stoel Rives LLP  
600 University Street, Suite 3600  
Seattle, WA 98101-3197  
Ph: 206-386-7691  
Fax: 206-386-7500  
bcsherland@stoel.com

**Thomas M. Culbertson, Chair-Elect and Treasurer**

Lukins & Annis, P.S.  
West 717 Sprague Avenue, Suite 1600  
Spokane, WA 99201-0466  
Ph: 509-455-9555  
Fax: 509-747-2323  
tculbertson@lukins.com

**Lora L. Brown, Probate and Trust Council Director**

Stokes Lawrence, P.S.  
800 Fifth Avenue, Suite 4000  
Seattle, WA 98104  
Ph: 206-626-6000  
Fax: 206-464-1496  
lora.brown@stokeslaw.com

**William Reetz, Real Property Council Director**

LandAmerica Financial Group  
1200 Sixth Avenue, Suite 1910  
Seattle, WA 98101  
Ph: 206-628-2803  
Fax: 206-343-7220  
breetz@landam.com

**EX OFFICIO MEMBERS**

**N. Elizabeth McCaw, Newsletter Editor**

Williams, Kastner & Gibbs PLLC  
601 Union Street, Suite 4100  
Seattle, WA 98101  
Ph: 206-628-6600  
Fax: 206-628-6611  
bmccaw@wkg.com

**Michael A. Barrett, Assistant Newsletter Editor**

Perkins Coie LLP  
1201 Third Avenue, Suite 4800  
Seattle, WA 98101  
Ph: 206-583-8615  
Fax: 206-583-8500  
barrm@perkinscoie.com

**Douglas C. Lawrence, Web site Editor**

Stokes Lawrence P.S.  
800 Fifth Avenue, Suite 4000  
Seattle, WA 98104-3179  
Ph: 206-626-6000  
Fax: 206-464-1496  
doug.lawrence@stokeslaw.com

**Jean McCoy, Assistant Web site Editor**

Landerholm, Memovich, Lansverk & Whitesides  
915 Broadway, Suite 400  
PO Box 1086  
Vancouver, WA 98660  
Ph: 360-696-3312  
Fax: 360-696-2122  
jeanm@landerholm.com

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