Cut Down in the Prime Of Her Estate Planning

For the first time, a judge has said compensation in a wrongful death case can include damages for a decedent's inability to complete a tax-saving strategy. *Del Broccolo*—and its implications

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What remedies are available when an unexpected death short-circuits an estate plan, leaving heirs to pay more taxes than they would have had their benefactor lived a little longer? In wrongful death cases, one state may now permit estate-tax planning losses to be factored into compensatory damages. But advisors beware: There's a general duty to mitigate damages. Advisors should therefore take note of post-mortem mitigation techniques, which vary depending upon the decedent's state and country of domicile.

Whether a beneficiary's loss of estate-tax planning advantages can be deemed a proper element of damages in a wrongful death action has been addressed under the laws of only four states: Florida, Illinois, Kansas and New York.[1] Until recently, all courts have agreed that such damages are not recoverable in wrongful death cases, because these damages are too speculative, given all the unknown circumstances and changing tax laws that could have impacted the decedent's estate plans had he survived to implement them.

But on June 16, George R. Peck, a trial judge in Nassau County, N.Y., found otherwise. In *Del Broccolo v. Torres*,[2] he opened the door for the first time to the possibility of collecting damages in a wrongful death case for lost tax-planning opportunities.

THE TIDE TURNS

Domenica Del Broccolo was killed in an automobile accident in 1998. The executor of her estate sued for wrongful death and claimed that damages should be awarded for lost tax advantages. The facts were uncontroverted: Del Broccolo had engaged in a lifetime giving plan, created a qualified personal residence trust (QPRT) and, as a result of her death, the estate stood to recognize income in respect of a decedent (IRD). In denying the defendant's motion for summary judgment, Peck adhered to an earlier memorandum decision by the state's highest court[3] that concluded, because the tax law and the decedent's tax and economic status could be expected to change, damages for unanticipated IRD and inability to complete a lifetime giving plan were speculative and, as such, unrecoverable.

But the judge broke new ground by also finding that—because the QPRT was just eight months before termination—the lost tax advantage was "not speculative or subject to change," and therefore damages could be assessed, based on the estate owing more taxes than would have been the case had the QPRT term been completed.

Unfortunately, Peck did not outline what factors determine whether a lost tax advantage is too speculative to recover. But for those heirs who might be similarly situated, *Del Broccolo* does provide precedent for the proposition that lost tax advantages are not, as a matter of law, unrecoverable.

Of course, once an action can be brought to recoup damages resulting from lost estate-planning opportunities, claimants will need to mitigate damages, if possible. Local law largely governs the extent to which post-mortem planning can mitigate damages for such losses. In New York, for example, a testamentary or *inter vivos* trust can be amended for certain tax purposes, such as to permit the trust to qualify as a charitable remainder trust, qualified domestic trust or QPRT.[4] But changes to accomplish these goals can be made only if they are administrative in nature and cannot affect the dispositive provisions of the will or trust.

In other countries, though, the viability of mitigating damages are far greater. The United Kingdom, for one, permits more flexibility in post-mortem planning.

Let's say, for example, that Andy and Ben are brothers, born and raised in London. Ben remains in England, but Andy goes off to college in New York, settles there and ultimately becomes a U.S. citizen. Tragically, both are killed in a car accident while Ben's family visits Andy's in New York. The other driver is found liable for their wrongful deaths. The question arises as to whether loss of estate-planning advantages should be reflected in the damages the defendant is ordered to pay.

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As a U.K. domiciliary, the ability of Ben's heirs to mitigate damages through post-mortem planning is quite different than their New York cousins. Let's assume that, just before his departure for the states, Ben executed a homemade emergency will and made an appointment to meet with his family lawyer upon his return. Assume further that Ben's emergency will left his stock in the family company to his wife and significant cash legacies to his two sons. Unsurprisingly, this will did not maximize Ben's U.K. inheritance tax position. First, as both Ben and his wife were domiciled in Great Britain, anything passing between them on death would be free of U.K. inheritance tax,[5] and anything passing to his sons would be taxed at 40 percent,[6] unless it benefited from some other specific exemption. Moreover, stock in trading companies not listed on a stock exchange are wholly exempt from U.K. inheritance tax.[7] Clearly, it would have made much more sense for Ben to have left the stock to his sons (tax free) and the cash to his wife (also tax free). It is almost certain that, had he been able to meet with his lawyer, he would have been advised to change his will accordingly.

So, should the extra tax payable based on Ben's emergency will form part of the damages ordered against the other driver? It might under *Del Broccolo*. But Ben's heirs would be able, and likely required, to mitigate damages. In the United Kingdom, the beneficiaries of a decedent's estate, whether under a will or under the rules of intestacy, can contract to modify how the estate should be divided between them. Provided they do so within two years of a decedent's death, heirs can consent to make an election to alter the disposition of the decedent's estate, which is subsequently taxed as if the modified terms were originally prescribed in the decedent's will.[8] The court may act as proxy in such an election and consent on behalf of those not of full age and capacity.[9]

This election applies to both inheritance tax[10] and for capital gains tax purposes.[11] In our hypothetical, all U.K. inheritance tax on Ben's estate could be avoided, without any tax charge falling on Ben's widow or her sons, and the sons could take the stock in the family company with a step-up in basis. Their damages, in this regard at least, would be fully mitigated.

In a jurisdiction where wrongful death damages can include compensation for lost tax-planning benefits, it behooves counsel to become familiar with post-mortem tax planning techniques, particularly for purposes of mitigating damages. Moreover, as in the case of Ben and Andy, it is important for counsel to the decedent's estate to recognize that post-mortem tax planning opportunities will be quite different if the decedent was a domiciliary of another country, such as the United Kingdom.

Endnotes

1. *Kernke v. Menninger Clinic, Inc.*, 172 F. Supp. 2d 1347 (D. Kansas 2001) (applying Kansas law); *Lindsay v. Allstate Ins. Co.*, 561 So.2d 427 (Fl. Dist. Ct. App. 1990); *Farrar v. Brooklyn Union Gas*, 73 N.Y.2d 802 (1988); *Elliott v. Willis*, 92 Ill.2d 530 (Sup. Ct. Ill 1982). See also *Hiatt v. United States*, 910 F.2d 737 (11th Cir. 1990) (applying Florida law).
2. 2004 N.Y. Misc. LEXIS 710 (Sup. Ct., Nassau Cty. June 16, 2004).
3. *Farrar v. Brooklyn Union Gas*, 73 N.Y.2d 802 (1988).
4. New York's Estates, Powers and Trusts Law Section 11-1.11.
5. Inheritance Tax Act 1984 Section 18.
6. Inheritance Tax Act 1984 Section 7 and Schedule 1.
7. Inheritance Tax Act 1984 Sections 103 to 114.
8. Inheritance Tax Act 1984 Sections 17 and 142.
9. Under the Variation of Trusts Act 1958 and/or the Trustee Act 1925 Section 57.
10. Inheritance Tax Act 1984 Sections 17 and 142.
11. Taxation of Chargeable Gains Act 1992 Section 62.

COLLECTORS' SPOTLIGHT

Howard Chandler Christy's 1918 painting, "I Wish I Were a Man," was commissioned by the Navy to entice young men to enlist. The famous poster sold to a collector for $3,220 at a Swann Galleries auction on Aug. 4 in New York.