

# Michigan Law Review

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Volume 62 | Issue 8

---

1964

## Fiduciary Administration-Power of Court to Authorize Inter Vivos Distribution from Incompetent's Estate

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### Recommended Citation

Robert C. Bonges, *Fiduciary Administration-Power of Court to Authorize Inter Vivos Distribution from Incompetent's Estate*, 62 MICH. L. REV. 1471 (1964).

Available at: <https://repository.law.umich.edu/mlr/vol62/iss8/15>

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**FIDUCIARY ADMINISTRATION—POWER OF COURT TO AUTHORIZE INTER VIVOS DISTRIBUTION FROM INCOMPETENT'S ESTATE**—The guardians of an eighty-six-year-old incompetent multi-millionaire petitioned for authorization to give a portion of the ward's assets to his children and grandchildren. It was not suggested that the proposed beneficiaries were currently in need of funds,<sup>1</sup> but rather the sole purpose of the inter vivos distribution was to minimize the impact of federal estate taxes on the ward's estate at his death. It was alleged and proved, however, that the proposed distribution would follow a plan which accorded substantially with the terms of the ward's will, and which the ward presumably would have followed himself, had he remained competent to manage his own affairs.<sup>2</sup> On petition to the Delaware Chancery Court, *held*, authorization granted. An incompetent's guardian may be authorized to distribute assets of the estate while the ward is still alive in order to effect substantial federal estate tax savings, so long as it is proved that the ward probably would have done the same thing had he remained competent. *In re duPont*, 194 A.2d 309 (Del. Ch. 1963).

The substitution of judgment rule provides that a court having jurisdiction of the property of an incompetent may, under certain circumstances, permit distributions from his estate to persons who otherwise have no lawful claim for support against the incompetent. This rule was first announced in *Ex parte Whitbread*,<sup>3</sup> where Lord Eldon authorized payments out of a ward's surplus income for the benefit of his brothers and sisters, who were found to be in need.<sup>4</sup> The ground of decision was not that the brothers and sisters had any right to an allowance, but that the court was merely authorizing what the ward himself probably would have done, if competent.<sup>5</sup>

The principle of the *Whitbread* case has subsequently been recognized

<sup>1</sup> On the contrary, they were presumably provided for quite adequately. Principal case at §10.

<sup>2</sup> Under the terms of the ward's will the remainder of his estate, after certain bequests to charities, was to be left by testamentary trust for the benefit of his children and grandchildren. After allowing for charitable contributions and expenses the ward's net taxable estate would be worth about \$135,200,000. The guardians therefore proposed that assets valued at about \$36,000,000 be given to the ward's children and grandchildren under an inter vivos trust which, except for the fact that the distribution would constitute a present gift, would conform in all substantial aspects to the terms of the ward's will, and which would enable the \$36,000,000 to be taxed at the more advantageous gift tax rates. Principal case at §10.

<sup>3</sup> 2 Mer. 99, 35 Eng. Rep. 878 (Ch. 1816).

<sup>4</sup> *Ibid.*

<sup>5</sup> *Ibid.*

or adopted in a number of American states.<sup>6</sup> However, the American authorities which have adopted the rule, like their English counterparts,<sup>7</sup> have authorized such allowances only upon proof of two conditions. It must be shown that the ward probably would have done likewise, if competent, and the purpose of the allowance must be to aid relatives who are in need of funds for their support.<sup>8</sup> Few changes have been made in the traditional *Whitbread* rule, but in some states it has been extended to allow payments for support even though the principal of the incompetent's estate will be invaded.<sup>9</sup>

In some states the *Whitbread* rule has been rejected, but not because of disagreement with the principles which underlie it. Courts rejecting the rule have stated that the statutes delimiting their powers preclude its adoption.<sup>10</sup> Courts which have adopted the rule, however, have not found the authority to do so expressly granted to them by the legislature.<sup>11</sup> By liberally construing the statutes which define their authority, these courts have found implicit power to distribute the ward's assets to relatives who otherwise have no legal claim for support against the incompetent.<sup>12</sup> The court in the principal case took just such an approach.<sup>13</sup>

Although consistent with past authority in most respects, the decision in

<sup>6</sup> *In re Hudelson's Estate*, 18 Cal. 2d 401, 115 P.2d 805 (1941); *In re Brice's Guardianship*, 233 Iowa 183, 8 N.W.2d 576 (1943); *In re Buckley's Estate*, 330 Mich. 102, 47 N.W.2d 33 (1951); *State ex rel. Kemp v. Arnold*, 234 Mo. App. 154, 113 S.W.2d 143 (1938); *Potter v. Berry*, 53 N.J. Eq. 151, 32 Atl. 259 (Ct. Err. & App. 1895); *In re Willoughby*, 11 Paige 257 (N.Y. Ch. 1844); *Hambleton's Appeal*, 102 Pa. 50 (1883); *In re DeNisson*, 197 Wash. 265, 84 P.2d 1024 (1938).

<sup>7</sup> *In re Mackenzie*, 43 L.T.R. (n.s.) 681 (Ch. 1880); *In re Frost*, L.R. 5 Ch. App. 699 (1870); *Ex parte Whitbread*, 2 Mer. 99, 35 Eng. Rep. 878 (Ch. 1816).

<sup>8</sup> *In re Rodgers*, 96 N.J. Eq. 6, 125 Atl. 318 (Ch. 1924); *Matter of Flagler*, 248 N.Y. 415, 162 N.E. 471 (1928); *Monds v. Dugger*, 176 Tenn. 550, 144 S.W.2d 761 (1940); see cases cited note 6 *supra*.

<sup>9</sup> See *In re Brice's Guardianship*, 233 Iowa 183, 8 N.W.2d 576 (1943); *In re Fleming*, 173 Misc. 851, 19 N.Y.S.2d 234 (Sup. Ct. 1940), 54 HARV. L. REV. 143 (1940); *In re DeNisson*, 197 Wash. 265, 84 P.2d 1024 (1938).

<sup>10</sup> *Kelly v. Scott*, 215 Md. 530, 137 A.2d 704 (1958); *Binney v. Rhode Island Hosp. Trust Co.*, 43 R.I. 222, 110 Atl. 615 (1920); *Lewis v. Moody*, 149 Tenn. 687, 261 S.W. 673 (1923). Interestingly enough, the *Whitbread* case was decided at a time when the Lord Chancellor's authority over the property of an incompetent was governed by Statute, *De Praerogativa Regis*, 1326, 17 Edw. 2, c. 10, and in *Kelly v. Scott*, *supra*, the Maryland court construed Statute, *De Praerogativa Regis* as precluding the application of the *Whitbread* rule.

<sup>11</sup> See *In re Brice's Guardianship*, 233 Iowa 183, 8 N.W.2d 576 (1943); *In re Buckley's Estate*, 330 Mich. 102, 47 N.W.2d 33 (1951); *State ex rel. Kemp v. Arnold*, 234 Mo. App. 154, 113 S.W.2d 143 (1938); *Potter v. Berry*, 53 N.J. Eq. 151, 32 Atl. 259 (Ct. Err. & App. 1895); *Hambleton's Appeal*, 102 Pa. 50 (1883); *In re DeNisson*, 197 Wash. 265, 84 P.2d 1024 (1938).

<sup>12</sup> A Michigan court, when confronted with a statute authorizing the court to permit payments out of the incompetent's estate for the support of his family, construed the word "family" to include "blood relatives, or any group constituting a distinct domestic or social body." *In re Buckley's Estate*, 330 Mich. 102, 112, 47 N.W.2d 33, 38 (1951); MICH. STAT. ANN. § 27.3178(217) (1962); see MO. ANN. STAT. § 475.125 (1956); *State ex rel. Kemp v. Arnold*, 234 Mo. App. 154, 113 S.W.2d 143 (1938).

<sup>13</sup> Principal case at 317; see DEL. CODE ANN. tit. 12, § 3705 (Supp. 1962).

the principal case, by authorizing partial distribution of the ward's estate to relatives who did not need the funds for their support, represents a significant extension of the *Whitbread* rule.<sup>14</sup> In a previous case a Pennsylvania court had denied a request for authorization to make distributions from the estate of an incompetent for the purpose of minimizing federal estate taxes,<sup>15</sup> but there the court was limited by a statute which specifically stated that such distributions must be for the "care and maintenance" of the recipient.<sup>16</sup> The court went on to say, however, that in any event tax avoidance is not a legally sufficient ground for distributing any part of an incompetent's estate while he is alive.<sup>17</sup>

In the principal case the court recognized that the need of the recipient has been a salient factor in other cases which have applied the *Whitbread* rule.<sup>18</sup> Nevertheless, the court held that need on the part of the recipient is not a necessary condition where there are other indications of what the incompetent would have done.<sup>19</sup> Consequently, the need of the recipient, the possibilities of tax avoidance, and the size and condition of the ward's estate are merely evidentiary matters which are relevant only insofar as they aid the court in determining what the incompetent probably would have done.<sup>20</sup> Having eliminated the requirement of need, it was relatively easy for the court to reach the conclusion that the ward would have made similar gifts had he possessed the capacity to do so.<sup>21</sup> However, the significance of the elimination of the requirement of need is as yet unclear. In the principal case the inter vivos distribution did produce a substantial benefit to the estate of the ward in that it assured a saving in federal estate taxes of at least sixteen million dollars.<sup>22</sup> It is therefore not clear whether a substantial benefit to the estate will be required in lieu of need on the part of the recipients, or whether benefit to the estate is simply another factor which the court will look to in determining the incompetent's probable intention.<sup>23</sup> If a substantial benefit to the estate is not required, it is conceivable that a situation might arise in which it could be shown that the ward would have done something which would be detrimental to his own best interests. Although it is doubtful that any court would extend

<sup>14</sup> See note 8 *supra* and accompanying text. One leading authority, while recognizing the *Whitbread* rule, stated that even granting allowances for support should be "narrowed and discouraged . . ." *In re Fleming*, 173 Misc. 851, 858, 19 N.Y.S.2d 234, 236 (Sup. Ct. 1940).

<sup>15</sup> *Bullock Estate*, 10 Pa. D. & C.2d 682 (Orphans' Ct. 1957).

<sup>16</sup> PA. STAT. ANN. tit. 50, § 3644 (Supp. 1962). On the other hand, the applicable Delaware statute provides: "A trustee may, in the name of the mentally ill person, do whatever is necessary for the care, preservation and increase of his estate." DEL. CODE ANN. tit. 12, § 3705 (Supp. 1962).

<sup>17</sup> *Bullock Estate*, 10 Pa. D. & C.2d 682, 685 (Orphans' Ct. 1957).

<sup>18</sup> See authorities cited note 8 *supra*.

<sup>19</sup> Principal case at 315.

<sup>20</sup> *Id.* at 316-17.

<sup>21</sup> *Id.* at 312.

<sup>22</sup> See *id.* at 311.

<sup>23</sup> See *id.* at 316-17.

the operation of the substitution of judgment principle this far, such a result would be possible if the sole concern of the court is merely to do what the incompetent probably would have done, if he were capable.<sup>24</sup>

The court in the principal case could have avoided the uncertainties created by its decision had it articulated new limits for the *Whitbread* rule. It is suggested that the better approach would be to allow inter vivos distributions out of an incompetent's estate, as in the principal case, only when it can be satisfactorily shown that (1) the needs of the ward will still be adequately provided for, (2) the ward would probably have done likewise if sane, and (3) either (a) the prospective recipients actually need the funds for their support, or (b) the distribution will constitute a substantial benefit to the ward's estate. This sort of extension of the traditionally limited *Whitbread* rule seems necessary in order to adapt the law to the exigencies of modern life. Today, prudent tax planning can play a vital role in preserving an individual's estate for future generations; indeed, in some instances it is absolutely essential. Consequently, it seems both desirable and sensible to permit a guardian to protect his ward's estate in the same manner that the ward himself would probably protect it, if he were able. In addition, if need on the part of the prospective recipients cannot be shown, the alternative requirement, that a benefit to the incompetent's estate must be demonstrated, would prevent distributions detrimental to the ward's estate even though the incompetent would probably have made them if competent.

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<sup>24</sup> Unwarranted extensions of the *Whitbread* rule are particularly likely if the burden of proof requirements are relaxed. See *id.* at 316. For a discussion of the amount of proof required by various courts to establish what the incompetent would have done, if sane, see generally, Comment, 17 CALIF. L. REV. 175 (1929); 41 HARV. L. REV. 402 (1928).