Matter of Hoppenstein
2017 NY Slip Op 30940(U)
March 31, 2017
Surrogate's Court, New York County
Docket Number: 2015-2918/A
Judge: Rita M. Mella

SURROGATE'S COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

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In the Matter of the Accounting by the Trustees of the Trust u/a dated December 20, 2004, by

REUBEN HOPPENSTEIN,

Settlor.

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DECISION and ORDER
File No.: 2015-2918/A

M E L L A, S.:

Papers considered	Numbered
Notice of Motion by Cheryl Hoppenstein, Yitzchak Hoppenstein, Yonatan Hoppenstein, Aryeh Hoppenstein, and Yara Hoppenstein, for Partial Summary Judgment, dated July 13, 2016	1
Affidavit of Andrew M. La Bella, Esq., in Support of Motion, sworn to July 13, 2016, with Exhibits A through KK, including Answer and Objections in underlying accounting proceeding	2
Affidavit of Andrew M. La Bella, Esq., in Further Support of Motion, sworn to August 30, 2016, with Exhibit 1	3
Affirmation of Jason J. Smith, Esq., in Opposition to Motion, dated September 30, 2016, with Exhibits A through L	4
Memorandum of Law in Opposition to Motion, dated September 30, 2016	5
Reply Memorandum of Law in Support of Motion, dated October 10, 2016, with Exhibits A through F	6
Reply Affidavit of Andrew M. La Bella, Esq., sworn to October 10, 2016, with Exhibit 1	7
Affirmation of Jason J. Smith, Esq., in Further Opposition to Motion, dated November 4, 2016, with Exhibits A and B	8
Reply Memorandum of Law in Support of Motion (in Response to Affirmation in Further Opposition), dated November 15, 2016, with Exhibit A	9
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for a Protective Order, dated August 15, 2016, with Exhibits A through L	10
Notice of Cross-Motion for Sanctions by Nathan Davidovich, Charles H. Hoppenstein, and Ava Hoppenstein Shore, dated September 30, 2016	11
Affirmation of Jason J. Smith, Esq., in Opposition to Motion for a Protective Order and in Support of Cross-Motion for Sanctions, dated September 30, 2016, with Exhibits A through D	12
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These are motions in a contested proceeding for settlement of the account of the trustees of an irrevocable trust created by Reuben Hoppenstein (Settlor) on December 20, 2004 (the 2004 Trust). The objectants seek partial summary judgment to void the trustees' distribution of a $10 million insurance policy on the Settlor's life from the 2004 Trust to a new trust created by the Settlor in 2012 (the 2012 Trust). The objectants have also moved for a protective order precluding the trustees from taking their depositions. The trustees have cross-moved for an award of costs incurred in opposing the motion for a protective order.

Background

The Relevant Trust Provisions

The 2004 Trust provided for distributions of income during the Settlor's lifetime to his descendants, in the discretion of the trustees. The trust instrument also gave the trustees broad discretionary authority to make distributions of trust principal to the Settlor's descendants. The relevant provision is Article 2 (c), which states:

> "During the Settlor's lifetime, the Trustees are further authorized, from time to time, to pay such sums out of the principal of the trust (even to the extent of the whole thereof) to the Settlor's descendants, living from time to time, in equal or unequal amounts, and to any one or more of them to the exclusion of the others, as the Trustees, in their absolute discretion, shall determine; provided, however, that the Trustees shall notify each of the Settlor's descendants of their intention to make any distribution pursuant to this paragraph not less than forty-five days before the intended distribution, whereupon each of the Settlor's descendants shall have the prior right to withdraw principal pursuant to subdivision (b) of this Article 2 within thirty days after receipt of such notice."

The Article 2 (b) provision referred to in the proviso gave the Settlor's descendants, wife, and sons- and daughter-in-law the right, known as a "Crummey power," to withdraw from additions to trust principal an amount designed to qualify each addition to the trust as a "present interest" eligible for the federal gift tax annual exclusion.[1] Article 2 (b) directed the trustees to give these individuals fifteen days' written notification of their power of withdrawal "with respect to each addition." The instrument provided further that any unexercised withdrawal rights lapsed annually to the extent (computed by a formula) that the lapse would not be subject to gift tax as a donative transfer to the trust from the holder of the unexercised withdrawal

[1] See Internal Revenue Code § 2503 (b).

rights.[2]

Discord with Daughter Cheryl

The trustees allege that the Settlor was unhappy with one of his daughters, Cheryl Hoppenstein (Cheryl), in part because of what he felt were her excessive demands for money. The Settlor had reserved the right to exclude any beneficiary from the group eligible to exercise his or her Crummey power of withdrawal and, after the alleged falling out with Cheryl, he exercised that right: he delivered a letter to the trustees stating that Cheryl, her husband, her descendants, and David Shore (a former son-in-law) were to be excluded "from exercising his or her power of withdrawal with respect to any additions I make to the Trust from this date forward." The letter was dated December 4, 2008.

Pursuant to their discretionary power to distribute principal granted in Article 2 (c), and as reflected on Schedule E of the account, on October 12, 2012, the trustees distributed the life insurance policy from the 2004 Trust to the 2012 Trust, on the authority of the independent co-trustee, Nathan Davidovich.[3] The 2012 Trust was similar in all respects to the 2004 Trust, except that it eliminated Cheryl and her descendants as beneficiaries. Notice required by the Article 2 (c) proviso was made by letter dated August 17, 2012, from Davidovich to each of the Settlor's adult descendants in their individual capacities and on behalf of their minor children.[4]

The Settlor died in May 2015 and the proceeds of the life insurance policy were paid to

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[2] See Internal Revenue Code § 2514 (e).

[3] Article 9 (f) of the 2004 Trust expressly allows the distribution of trust property payable to a beneficiary to be applied "by payment to a trust for his or her benefit."

[4] Article 9 (l) of the 2004 Trust provides that notice of a minor's right to withdraw principal shall be given to the minor's natural or legal guardian.

the 2012 Trust.

The Motion for Partial Summary Judgment

Cheryl and her four adult children, Yonanton Hoppenstein, Yitchak Hoppenstein, Aryeh Hoppenstein, and Yara Hoppenstein (Objectants) have objected to the distribution of the $10 million life insurance policy from the 2004 Trust to the 2012 Trust on numerous grounds.

The Objectants claim, first, that the life insurance policy was not income subject to the discretionary power of the trustees to distribute income to the Settlor's descendants. This is irrelevant because the trustees are not relying on their discretionary power to distribute income, but rather on their discretionary power to distribute principal. The distribution was not an act in contravention of the trust – which would violate EPTL 7-2.4, as the Objectants contend – but was expressly permitted by Article 2 (c) of the instrument.

The Objectants also argue that they were not given notice of their Crummey power to withdraw the policy when it was placed in the 2004 Trust. The policy, however, was not subject to a new withdrawal right. The trustees show that $260,000 cash was added to the 2004 Trust on December 27, 2004, as to which the Objectants, as well as all the other holders of the Crummey powers, were given the requisite notice by letter dated January 10, 2005. Schedule F of the account ("Statement of New Investments, Exchanges, and Stock Distributions") reflects that the 2004 Trust purchased the policy on January 28, 2005. The policy was not an addition to the principal of the trust, but a change in the form of the principal.[5]

In a further argument, the Objectants assert that the Article 2 (c) authorization to

[5] The court notes it would serve no tax purpose for a Crummey power to be granted for a change in the form of principal, because such change would not constitute a taxable gift.

distribute principal does not apply to the life insurance policy because the trust language does not specify the policy. There is no requirement, however, that a power to distribute principal be limited to principal that is specifically identified, and the life insurance policy was unquestionably part of the principal of the trust.

The Objectants also claim that Article 9 (o) of the trust instrument provides that any transfer between trusts can only be made if the trusts have identical beneficiaries. Article 9 (o), however, concerns consolidation of certain trusts and has no application to the subject distribution.

The Objectants claim further that the transfer did not comply with the requirements of EPTL 7-1.9 (allowing a trust creator to revoke a trust with the consent of all beneficiaries) or EPTL 10-6.6 (the "decanting" statute). These assertions are immaterial because petitioners do not rely on either of these statutes, but rather on their power to make discretionary distributions of principal under Article 2 (c) of the instrument, as discussed above. It is noted that EPTL 10-6.6 (k) provides, in relevant part:

> "This section shall not be construed to abridge the right of any trustee to appoint property in further trust that arises under the terms of the governing instrument of a trust or under any other provision of law or under common law . . . ."

The procedure for decanting outlined in EPTL 10-6.6 has no bearing on this case.

In their reply memorandum of law, the Objectants contend that because they were not given notice of their Crummey powers for cash additions the settlor made between 2005 and the date in 2008 when their powers were revoked, they held unexpired withdrawal rights when the

life insurance policy was transferred in 2012.[6] Therefore, they contend, they had a vested right in the policy.

This argument is flawed because the lapse of unexercised Crummey powers was not contingent upon receipt of notice of the Crummey power. Further, the beneficiaries' right to withdraw principal did not depend on notice of the right. Article 2 (b) (1) defines their powers of withdrawal with reference to the amount that "would qualify for the Federal gift tax annual exclusion under Section 2503 (b) of the [Internal Revenue] Code for a gift made directly to [the] descendant . . . ." Even if the Objectants were unaware of their right to withdraw from the later additions, the additions would not be disqualified from eligibility for the gift tax exclusion. The Tax Court so held in *Estate of Turner v Comm'r* (T.C. M. 2011-209), explaining:

> "[T]he fact that some or even all of the beneficiaries may not have known they had the right to demand withdrawals from the trust does not affect their legal right to do so."

Accordingly, whether or not the Objectants received formal notice of their rights to withdraw, they held those rights and the rights were subject to lapse to the extent provided in the trust instrument.

Mary S. Croly, Esq., the guardian ad litem appointed for Cheryl's infant daughter, calculated the cumulative amount of the property subject to the rights of withdrawal and the amount by which the rights lapsed annually until the policy was transferred in 2012. Using the policy cash surrender value for each year, she determined that the value of the lapsed rights exceeded the value of the property subject to withdrawal by more than $200,000. These figures

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[6] The trustees now maintain that the cash transferred to the 2004 Trust in 2005, 2006, and 2007 was in the form of a series of loans, evidenced by promissory notes, and therefore not "additions" to the trust requiring Crummey notices. The court need not determine whether the transfers were loans in view of the determination reached here.

were confirmed by Jennifer F. Hillman, Esq., the guardian ad litem appointed for the other four infant beneficiaries. Both guardians concluded that the Objectants held no unexercised rights of withdrawal when the policy was transferred in 2012.

The court rejects the Objectants' argument that transfers to the trust after the Settlor excluded them from exercising Crummey powers in 2008 should not have been taken into account in calculating the value of any unexercised powers. The cancellation of their Crummey powers applied only to *additions* made to the trust after the date of the letter, and not to any unexercised powers they had previously acquired. It was appropriate to consider the value of post-2008 lapses under the formula in the trust instrument. The court agrees with the conclusion of the guardians ad litem.

The court also finds no merit in the Objectants' claim that the trustees' failure to send certain Crummey notices was a breach of fiduciary duty that somehow voided the transfer of the life insurance policy. The transfer was made in full compliance with the trust provisions, including the provision for prior notice to the Settlor's descendants. Contrary to the Objectants' argument, the trust instrument did not require that the life insurance policy be specifically identified in the notice, or that the notice specifically refer to Article 2 (c).

For all the foregoing reasons, the motion for partial summary judgment is denied.

Summary Judgment for Trustees

The Objectants' prayer for relief in their Answer and Objections to the underlying accounting petition makes sixteen demands. Their motion for partial summary judgment was directed to the first three demands, all of which, in one form or another, seek to void the transfer of the life insurance policy. In accordance with the determinations above, the court finds that the

transfer of the policy was valid. Because there is no triable issue of fact concerning the propriety of the challenged distribution, the court grants summary judgment on the first three demands in favor of the trustees, pursuant to CPLR 3212 (b).

The Objectants' remaining thirteen demands for relief depend upon a finding that the policy transfer was void.[7] These demands are for information or return of the policy proceeds needed to place the 2004 Trust in its pre-transfer position (albeit with new trustees). They cannot be read as objections to the account, but rather as requests to aid in fashioning a remedy to undo the transfer. The court's determination here that the transfer was valid moots these requests. Accordingly, the court grants summary judgment approving the trustees' account. CPLR 3212 (b).

Motion for a Protective Order and Cross-Motion

The Objectants have moved for a protective order denying the trustees' right to take the depositions of the Objectants and of Cheryl's husband and attorney, Andrew La Bella, Esq. The trustees have stated that the testimony was required to investigate the Objectants' allegations of fraud, and to discover what transpired at a meeting that Mr. La Bella attended in 2005 with the attorney who either drafted or supervised the drafting of the 2004 Trust.

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[7] The fourth demand seeks reconveyance of the policy to the 2004 Trust. The next two demands are for injunctions directing the disclosure of the affairs of the 2012 Trust, delivery of its assets to the 2004 Trust, and delivery of any distributions made from the 2012 Trust to the 2004 Trust. The next ten demands are for an assessment of value to determine what would be necessary to place the 2004 Trust in its position prior to the policy transfer; to surcharge the trustees accordingly and require them to restore the 2004 Trust to its pre-transfer position; to remove or suspend the trustees of the 2004 Trust and the 2012 Trust; to appoint a successor trustee or trustees of the 2004 and 2012 Trusts; for preliminary injunctions preventing dissipation of the assets of the 2004 and 2012 Trusts (previously denied in the court's decision dated June 29, 2016); to provide accountings for both trusts (although the underlying proceeding is a final account for the 2004 Trust); and for costs and punitive damages.

Because the accounting has been approved, there is no need for further discovery and the motion for a protective order is denied as moot. The trustees' cross-motion for costs incurred in defending the motion is denied in the discretion of the court.

This decision constitutes the order of the court.

Settle decree on accounting.

Clerk to notify.

Dated: March 31, 2017

SURROGATE