

# MATERIAL PURPOSE - THE NEW “GOAL STANDARD” OF ESTATE PLANNING

The wealth transfer intent of a deceased person cannot be determined by a contemporaneous conversation. To uncover the intent of a decedent you consult a previously written document appropriately labelled as their “will.” Curiously, the modern tax-based will and its cousin the revocable trust usually have very little, if any, actual language discussing your personal desires. This paucity of personalized intentions usually caused minimal concern for affluent clients, lawyers and heirs from 1976-2009. In those years, a successful wealth transfer plan was more often measured by tax minimization than goals optimization.

However, when the Tax Relief Act of 2010<sup>1</sup> effectively repealed the estate tax for one year and altered or eliminated certain tax-motivated bequests, unwritten donative intent became very important. For example, in response to the one-year “repeal,” Florida allowed its courts to look outside the deceased person’s will or trust to find evidence of gift intent, even if the evidence contradicted the “plain words” of the document.<sup>2</sup>

Wealth transfer intent has now become so important that what began as a one year exception in one state has become a trend in the law to interpret unwritten intent in other states<sup>3</sup>. Minimally, a clearly written Statement of Wealth Transfer Intent (SOWTI) within the will or trust document is a good idea. An SOWTI should serve as the “material purpose” that prevents the unintended alteration, termination or modification of a long-term trust by spendthrift beneficiaries.<sup>4</sup> The SOWTI, as a personalized declaration of your donative goals, also helps protect against misuse, mismanagement and misappropriation of your bequests. Individuals rarely articulate a personal goal for any portion of their wealth transfers within their estate-planning documents. A SOWTI changes all that. While a SOWTI will not eliminate the need for sound, legally-tested dispositive and administrative language, it would surely seem that a document entitled “Last Will and Testament” should have some personal testimony.

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## WHAT A SOWTI IS NOT

A "Statement of Wealth Transfer Intent" may be a new term for many, so it is critical to have a clear definition. Perhaps the easiest way to define a SOWTI is to state what it is not:

1. It is not an ethical (spiritual) will;
2. It is not a precatory statement for discretionary trust distributions; and
3. It is not a family mission statement or family constitution.

### **Ethical Will**

An ethical will expresses and transmits the personal values of the writer. It is not a legal document at all, despite its name. In many ways, it is simply a letter about life, to be applied after death. Commentators seem to agree that the first ethical (spiritual) wills were probably created in ancient Israel.<sup>5</sup> Some reference the Jewish patriarch Jacob as providing the first recorded instance of an ethical will.<sup>6</sup> Perhaps a more germane example of an ancient Israeli ethical will is King David's "death bed" admonitions:

"These are the last words of David:

*'...When one rules over people in Righteousness, when he rules in the fear of God, he is like the light of morning at sunrise on a cloudless morning, like the brightness after the rain that brings grass from the earth.'*"<sup>7</sup>

Note the elements of an ethical will found in this short statement. King David sums up his personal history as a ruling monarch in the form of an admonition to his descendants as to how to rule. He then adds the positive consequence of these ethics by stating that those who display these qualities will be as awesome as a cloudless sunrise and as productive as bright sunlight on rain-drenched grass. The "last words of David" also make it clear why ethical wills have been referred to as "spiritual wills."

While the application of an ethical will to the thoughts and actions of descendants are compellingly important, it may be very difficult to apply these ethical statements to wealth transfer. Ethical wills are about transcendent goals and spiritual values; wealth transfer is about practical goals and material values.

Another example of an ethical will comes from President Obama's letter to his two daughters as he moved to the White House:

*"[Your Grandmother] helped me understand that America is great not because it is perfect but because it can always be made better – and that the unfinished work of perfecting our union falls to each of us. It's a charge we pass on to our children, coming closer with each new generation to what we know America should be.*

*I hope both of you will take up that work, righting the wrongs that you see and working to give others the chances you've had."*<sup>8</sup>

The Internet is full of other examples of ethical wills.<sup>9</sup> They are as interesting as the ancient epitaphs on gravestones, but they are not necessarily effective in explaining the author's wealth transfer intentions. And even if they were, the executor, personal representative or trustee may not be able to consider them because they are intentionally separated from the dispositive testamentary documents.

### **Precatory Language**

Precatory language is the nonbinding words of instruction that are typically attached to trust provisions as a further explanation of your trust direction. Classic precatory language is found in provisions within a family bypass trust that state, for example: "the trustee may, but is not required to, consider the income of the beneficiary from sources outside the trust in making a discretionary payment." The words "may, but is not required" make the statement precatory. Unfortunately, after reading this phrase the trustee really has no better understanding of your intent. Should the trustee consider outside income to make the trust assets the funds of last resort, or ignore outside income to make the trust assets the funds of first resort? A SOWTI would give the "why" of the nonbinding instruction.

A trust document could have a very short SOWTI related to a specific trustee duty. For instance, the phrase, "it is my desire to support my wife with the luxuries and comforts that I would provide her if I were still living," technically qualifies as a SOWTI. However, a much broader and more personalized declaration of purpose is advisable – one that will be a reference point for all precatory language and provide context for all other provisions of a wealth transfer document.

### **Mission Statement**

A mission statement is a description of organizational purpose. When properly crafted, the mission statement can be used to guide the decisions of the organization as it acts through its various constituent members. A generic example of a mission statement that applies to all of us is the preamble to the U.S. Constitution:

*We the People of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this Constitution for the United States of America.*

Often family mission statements are used to form a family constitution that governs the workings of the family as a unit. A SOWTI is also about purpose, but it is not about the purpose of a group or organization. It is about your purpose for the wealth

transfer. A mission statement can be useful for the profitable activity of a business because it differentiates the business from its competitors. In a family-operated business, a mission statement is frequently an important and useful guide to define the impact of family relationships on this profitable activity. Mission statements can also be helpful tools for family governance in the context of a business or family-owned assets. However, wealth transfer is not about governance.

For wealth transfer purposes, the mission statement will work only if the wealth in question is regarded as the family's wealth. James E. Hughes Jr., in his comprehensive treatise on family wealth transfer, *Family: the Compact Among Generations*,<sup>9</sup> implicitly assumes that the current wealth of the grantor-parents is implicitly the "family" wealth of their descendants. Hughes Jr. and many commentators like him assume a "family-owned model" for post-mortem wealth. The mission statement and family constitution (or the "compact among generations") would be an ideal vehicle to codify the post-mortem goals of the family as a group of wealth beneficiaries.

A different opinion of wealth transfer views the current title holder rather than the family group as the wealth owner. Under this view, the primary determinant of wealth transfer isn't the wealth owner's family, but the individual wealth owner.<sup>10</sup> A grantor's SOWTI is the better solution for purposing wealth transfer under this individual ownership view.

Finally, a family mission statement requires a family to agree on a mission. A SOWTI simply requires you, as the wealth owner, to have an explicit, unambiguous purpose for transferring your wealth. A professional advisor will have enough difficulty assessing and codifying your wealth transfer intentions. It's exponentially more difficult to assess the future intentions of a constantly changing family group. In reality, the SOWTI is much simpler and much more useful to you and to the drafting attorneys, trust administrators, personal representatives and courts.

### **DEFINING EXPECTATIONS**

Once you agree that an individual wealth owner should have the final say in transferring wealth, then use your current financial planning process as a roadmap for how to achieve goals-based wealth transfer. For example, when you give up current consumption to save or invest money, there is always an explicit or implicit reason for that decision. Values can often be nothing more than the priority of personal preferences. And the preference to save rather than consume or gift will often uncover very important values about you.

Sometimes wealth accumulation is such a strong habit that there appears to be no underlying reason. However, beneath every good habit is a belief held as a value. Is the saving for unforeseeable personal emergencies? Is the accumulation to

prevent wasteful consumption or an imprudent lifestyle? Is it for some personal aspirational desire? Or, is it to help educate family members? For a professional money manager to properly invest a client's savings, he must have an answer to the question "Why are you saving this?" The same is true in wealth transfer, except the question is, "Why are you transferring wealth to this beneficiary at this time?"

Once you discern the "why" of accumulation, you can establish appropriate investment goals. These goals will then inform the portfolio management process. Once you answer the question, "Why are you transferring this?" you can establish your SOWTI. With a SOWTI that reads and feels like you, it is possible to create a wealth transfer document that has optimal wealth planning and transfer tax minimization.

Defining wealth transfer expectations is not that easy. Just as investment management success can be hindered because of unrealistic return expectations, wealth transfer planning can be thwarted by unexpressed or miscommunicated personal values. Wealth transfers should always be in furtherance of genuinely held and previously expressed personal values. However, uncovering personal values can be a difficult task for many wealth owners. Dr. Guenther Weil, Harvard Ph.D. and founder of Value Mentors, says, "People don't really know what their true values are. They talk about their aspired values, purported values, or what they may consider to be politically correct values, but they don't really know what their actual values are."<sup>10</sup> We believe that wealth transfer values can be discovered from the underlying priority of preferences that determine daily financial decisions. A SOWTI is the summary of your "priority of preferences" for wealth transfers.

### THREE MINIMUM REQUIREMENTS

With your values properly profiled, it is possible to draft a written statement of intent. The goal of the SOWTI should be to provide insight into your overarching wealth transfer philosophy. The SOWTI should use goal-based language that clearly establishes your material purpose for the will or trust. It should be intentionally designed to give the attorneys, accountants, beneficiaries, fiduciaries, money managers and courts guidance on your purpose for the wealth transfer. Remember death itself gives no independent meaning or purpose to your post mortem wealth transfers – only a SOWTI can provide that meaning or purpose.

Here are three minimum requirements for an effective SOWTI. It should:

1. **Demonstrate a unique intention that is tied to your personal history, personal values or personal perspectives.** The test is whether the information expressed in the writing could be known without specifically asking you. Therefore, a generalized statement, "I want my descendants to be productive citizens," would not be a very effective indicator of

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intention because the statement could probably be attributed to *any* parent. However, the statement: "As an immigrant to the United States my goal is that my descendants take advantage of the economic opportunities offered by this country's freedoms that would not be available in the country of my birth" would be much more effective.

- 2. Clearly articulate a direct tie between your unique personal intentions and the creation of the specific trust in question.** The words, "This trust is for the benefit of my descendants," is far too general. However, a sentence that reads, "This trust is specifically designed to serve as a financial catalyst for the personal and professional achievements of my descendants," would tie in much better to the intentions expressed in the preceding paragraph.
- 3. Give some indication of your opinion on modification and/or early termination of the trust by the beneficiaries, trustees or courts.** A statement that the trust should be terminated "when it is no longer economically prudent to continue it" is boilerplate. A more useful sentence would be, "The drive for personal fulfillment and achievement never ends and, therefore, this trust should be maintained to augment and support such efforts of my beneficiaries over multiple generations and should not be modified to serve an alternative purpose unless and until there are compelling circumstances that make the material purpose of this trust untenable, and these 'compelling circumstances' for change could not have been imagined by me when I created this trust."

### SAMPLE SOWTI PARAGRAPH

*Here's a statement of wealth transfer intent that includes the three minimum requirements:*

I acquired the wealth transferred into this trust at age 60 through starting a business that grew out of a personal passion. As an immigrant to this country it is essential to me that my descendants also demonstrate a lifelong commitment to economic achievement that is not available in my birth country. Therefore, this trust was created by me to serve as a financial catalyst for the personal, cultural and professional achievement of my descendants. The human need for productive personal fulfillment never retires or ends. I intend that the funds in this trust be strategically distributed throughout the entire lifetime of the designated beneficiaries. Since I have transferred substantial funds to my children outside of this trust, I intend that this trust should not be terminated prematurely to serve any alternative material purpose.

### OTHER SOWTI EXAMPLE PARAGRAPHS

A sample trust created by Jon J. Gallo, Eileen Gallo and James

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Grubman includes another short but helpful introductory paragraph for a SOWTI.<sup>13</sup>

*To my descendants and their Trustees, both living and those to be conceived and born in the future: On the most basic level, the purpose of this trust is to further the pursuit of happiness by my descendants. I use the phrase the pursuit of happiness in the same way as our Founding Fathers used it in the Declaration of Independence. Neither they nor I were or are talking about acquiring more material goods or taking longer vacations, but rather the sense of self-sufficiency that is derived from becoming self-reliant and financially sound, having a sense of emotional, social, and mental competence and giving back to the community.*

*The money in this trust will help make things more convenient for my descendants but it cannot make them happy. I believe that the family's money, including the money in this trust, should be viewed as a tool to support the growth of the family's real capital, which consists of the family members and their knowledge achieved through life experience and education. This is why I believe that travel, involvement in philanthropy and education to one's maximum potential are so important.*

The Gallo sample SOWTI is the first paragraph of a trust that provides discretionary trust provisions for travel and education. There is also precatory language in the Gallo example that encourages generous distributions to beneficiaries and to charity. A well-crafted SOWTI should make it significantly easier for the trustee and the beneficiaries to manage expectations, as well as discretionary distributions.

Although traditional estate planning documents are built around legally tested clauses and “boilerplate” language, a SOWTI, by definition, has no boilerplate. Each wealth owner's life story and wealth transfer goals are, by definition, unique. The drafting tendency will be to imitate well-written phrases like the Gallo example. However, that will simply not work as an effective SOWTI.

To demonstrate the detail and specificity that will be most helpful in a SOWTI, two complete examples<sup>14</sup> have been included as addendums. Note the differences in tone, style and facts within these examples. The goal is that heirs, beneficiaries, executors, trustees, attorneys, judges as well as disgruntled relatives will all recognize the tone and words of the SOWTI as consistent with how the decedent communicated important matters.

## CONTINUING THE CONVERSATION

The conversation about wealth transfer was never really about the inevitability of death or the propriety of tax minimization. It was and is about extending defined benefits of wealth to someone other than the current wealth owner. Most of us probably have nagging, counterintuitive, suspicion that *giving away wealth* might actually be more fulfilling than *accumulating wealth*. And that

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"suspicion" is why successful estate planning is defined by the accomplishment of the wealth transfer goals set out in your SOWTI. Therefore, an accurate and articulate SOWTI may be the most important provision in your estate planning documents. The accomplishment of the goals articulated in the SOWTI may be one of the most important measures of your success.

## FOR MORE INFORMATION

As a leader in trust and estate services, Northern Trust can help you meet your unique goals for today and tomorrow. With your values as our guide, we may be able to create sophisticated wealth transfer strategies that help you maintain your current lifestyle while providing for your loved ones and giving to the community. To learn more, contact your Northern Trust relationship manager or visit [northerntrust.com](http://northerntrust.com).

1. *Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (P.L. 111-312), enacted Dec. 17, 2010. Note also, the American Taxpayer Relief Act of 2012 (HR 4) signed into law on January 4, 2013 has permanently increased and unified the applicable exclusion amount at \$5,250,000 (indexed) potentially allowing more than 98% of U.S. wealth owners to avoid payment of transfer taxes.*
2. *"The Florida legislature has amended § 733.1051 of the Florida Probate Code and § 736.04114 of the Florida Trust Code to grant Florida courts broad authority to determine and effect the Testator/Settlor's probable intent in employing a formula bequest, in the event such bequest does not function correctly due to the lack of a federal estate or generation-skipping transfer ("GST") tax in 2010. The statutes allow the court to consider "the terms and purposes" of the document, the "facts and circumstances" surrounding its creation and the Testator/Settlor's probable intent. In the course of this analysis, the court is allowed to consider evidence relevant to intent, "even though the evidence contradicts an apparent plain meaning of the trust instrument." Nathaniel Birdsall "Florida legislature grants courts the broad power to construe wills and trusts in the absence of a federal estate tax", Proskauer Rose LLP August 1 2010. Florida Statutes 736.04114 (3)*
3. Fred Franke and Anna Katherine Moody *"The Terms of the Trust: Extrinsic Evidence of Settlor Intent" 40 ACTEC L.J. 1 (2014).* In this comprehensive article about the use of extrinsic evidence the authors discuss the common law evolution and provide a summary of each state's law in an appendix. The notable conclusion of the article is that even though the UTC and THE RESTATEMENT (THIRD) OF TRUSTS show a strong trend to allow extrinsic evidence for almost any purpose, "For the attorney charged with drafting trusts, the goal ought to be to capture settlor intent within the four corners of the document regardless of the extrinsic evidence rules." *Id* at page 12. "The general principle is well settled that extrinsic evidence is not admissible to vary, contradict, or add to the terms of a will, or to show a different intention on the part of the testator from that disclosed by the language of the will." 94 A.L.R. 26 II. c.



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General Rule. However the Restatement (Third) of Property (Wills and Donative Transfers) §10.2 (2003 Updated June 2016) states that "In seeking to determine the donor's intention, all relevant evidence, whether direct or circumstantial, may be considered, including the text of the donative document and relevant extrinsic evidence." In states adopting §415 of The Uniform Trust Code settlor intent is so important that extrinsic evidence of intent can be consulted even if the language of the trust is unambiguous

4. See Uniform Trust Code Section 411. Comment "Subsection (b), similar to Restatement Third but not Restatement Second, allows modification by beneficiary action. The beneficiaries may modify any term of the trust if the modification is not inconsistent with a material purpose of the trust."
5. Dr. Eric L. Weiner MSW, PhD, Words From The Heart – A Practical Guide to Writing An Ethical Will, Workbook First Edition, ©2010, pp. 2-3.
6. Robert G. Alexander, "Ethical Will: Gifts of the Heart" CCH Financial and Estate Planning Articles par. 32,901. The concept of ethical will isn't a new one. In fact, this concept is said to date back almost 3,000 years to the Old Testament book of Genesis in the Bible. In Genesis, Chapter 49, when the Patriarch Jacob was dying, he brought his 12 sons together, and on his deathbed he told them stories, predicted their futures and imparted to each one of them the lessons he had learned during his lifetime. In the Jewish religion, ethical wills were an oral tradition; written ethical wills are said to date back to the 20th century, when it was a custom to give written directions for the religious and secular guidance of their children.
7. Quoting from II Samuel 23:1a, 3b and 4 New International Version 1973, 1978, 1984, 2011 by Biblica.
8. President Barack Obama, excerpt from a letter written to his two daughters on Jan. 18, 2009, [life-legacies.com/ethical-wills/samples.html](http://life-legacies.com/ethical-wills/samples.html) created by Rachel Freed.
9. See [ethicalwill.com](http://ethicalwill.com) created by Dr. Barry K. Baines, MD.
10. David Bergman and Eric Sanderson, "Creating an Estate Plan: Managing the Paradox of Conflicting Values," *Journal of Practical Estate Planning*, October-November 2010, pp. 24-25, quoting Dr. Guenther Weil psychologist and founder of Value Mentors LLC James E. Hughes Jr., *Family: The Compact Among Generations*, 2007, Bloomberg Press New York.
11. The tension between the wealth owner's right to limit the future uses of their property and the right of family beneficiaries to be free from "dead hand" control is at the core of a centuries-old legal debate. See Professor Allan Newman, "The Intention of The Settlor Under The Uniform Trust Code: Whose Property Is It Anyway?" 38 *Akron Law* 649, 2004-2005. See also Shelly Kreiczler-Levy, "Inheritance Legal Systems And The Intergenerational Bond" 46-3 *Real Property, Trust and Estate Law Journal* 495, Winter 2012.

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12. *Used by permission. Although this statement of wealth transfer intent(SOWTI) is useful for showing that the trust isn't designed for remote descendants, it may not establish a material purpose that would prohibit the children from terminating or modifying the trust in Uniform Trust Code jurisdictions that permit trust modification or termination by beneficiary consent.*
13. *Jon J. Gallo, Eileen Gallo, Ph.D. and James Grubman, Ph.D., "The Use and Abuse of Incentive Trusts: Improvements and Alternatives," The University of Miami 45th Annual Heckerling Institute of Estate Planning, par. 1107 p. 11-43, January 2011. The sample wasn't labeled as a SOWTI by its author, however, the use of an over-arching purpose for the trust is the reason it is such an excellent example of a statement of wealth transfer intent. Note the authors are advocating for a "financial skills trust" that is innovative and worthy of additional study. The inherent limitation of the trust may be that it implicitly focuses the beneficiaries on personal financial behavior instead of personal achievement.*
14. *The examples are actual wealth transfer statements of intent but they have been edited to protect the identities of the client. Most of the similarities in tone and language are a result of this editing. Note also that the actual statements were significantly longer and much more detailed.*

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