PLANNING FOR UNIQUE, ILLIQUID, ILLEGAL AND UNUSUAL ASSETS: GOOD GRIEF, GRANDMA'S GOT A GUN COLLECTION!

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REGULATED ASSETS: WHAT DO YOU DO WHEN YOU FIND OUT GRANDMA HAD A GUN COLLECTION, WINE, PLANES, AND CANNABIS?

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I. INTRODUCTION

This outline examines a few unusual and highly regulated assets that an estate planner may encounter from time to time, often after the client has died. These include aircraft, wine, guns, and cannabis. While the rules with respect to handling these assets can vary widely from state to state, this outline is intended to provide a broad overview. Because the purpose trust—a trust that exists to carry out a specific purpose rather than for the benefit of a particular individual or group of individuals—is an often used planning tool in the context of unusual assets, this outline will begin with a brief discussion of this type of trust.

II. PURPOSE TRUSTS

A. Background.

A purpose trust exists to carry out a specific objective rather than for the benefit of individual beneficiaries. Examples include trusts for a non-charitable purpose—most frequently for the care of pets, or the ownership of regulated assets such as firearms and aircraft—and trusts for charitable purposes—notably, private foundations organized as trusts and charitable land banks.

A charitable purpose trust breaches a number of basic tenets of traditional trust law. First, it violates the rule against perpetuities because it lacks a measuring life. Next, it has no ascertainable beneficiary whose identity can be established (although individuals may benefit through scholarships or grants).[1] Finally, it lacks someone with standing to enforce it.[2]

The Uniform Trust Code (UTC) and the Uniform Probate Code (UPC) specifically permit purpose trusts. UTC section 409, adopted in Washington as RCW 11.98.015, permits the creation of "[a] trust . . . for a noncharitable purpose without a definite or definitely ascertainable beneficiary or for a noncharitable but otherwise valid purpose to be selected by the trustee."[3] While a purpose trust may be used to maintain a cemetery plot, it may not be used to maintain human remains.[4]

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[1] *See* Jonathan Klick & Robert H. Sitkoff, *Agency Costs, Charitable Trusts, and Corporate Control: Evidence from Hershey's Kiss-Off*, 108 Colum. L. Rev. 749, 780 (2008).

[2] *See* Alexander A. Bove Jr., *The Purpose of Purpose Trusts*, 18 Prob. & Prop. 34 (May/June 2004). The law permits charitable purpose trusts because the attorney general of the applicable jurisdiction has the authority to enforce their terms. *See* Restatement (Second) of Trusts §348 (1959) (defining a charitable trust as "a fiduciary relationship with respect to property arising as a result of a manifestation of an intention to create it, and subjecting the person by whom the property is held to equitable duties to deal with the property for a charitable purpose"); *see generally* Joshua C. Tate, *Should Charitable Trust Enforcement Rights Be Assignable?*, 85 Chi.-Kent L. Rev. 1045 (2010) (providing a history of the charitable purpose trust and the inherent challenges of enforcement of its purpose).

[3] Unif. Trust Code §409 (amended 2005); 7C U.L.A. 494 (2006).

[4] The right to human remains is limited to possession for the purpose of burial or other lawful disposition, which is not a property right. *Wilson v. Wilson*, 138 So. 3d 1176 (Fla. Dist. Ct. App. 2014).

Before purpose trusts were legally recognized, courts considered them honorary trusts, which were unenforceable if the named trustee failed to carry out the specified purpose. However, the residuary beneficiaries could sue to terminate the trust.[5]

Several countries have enacted legislation specifically to promote the use of non-charitable purpose trusts and serve as non-charitable purpose trust havens.[6] In 2008, Delaware enacted legislation to treat non-charitable and charitable purpose trusts as equivalent entities, except with respect to their federal tax consequences.[7]

B. Taxation of Purpose Trusts.

Because a purpose trust lacks an individual beneficiary, the federal tax consequences are complex and not clearly defined.[8] Typically, the Internal Revenue Code (Code) would allow a deduction to the trust for distributions to an individual beneficiary carrying out income and require the beneficiary recipient to pay income tax on that distribution.[9] Different rules apply, however, when the beneficiary is not a person, as defined by Code §7701(a), and thus not a taxpayer, but instead is a family cabin or a pet.

A purpose trust may be taxed as a grantor trust or a non-grantor trust, depending upon its drafting. If the purpose trust is a grantor trust, the taxation is relatively straightforward. All incidents of taxation pass through to the grantor. However, if the gift to the grantor trust was incomplete at funding, then, as funds are distributed, the grantor will be deemed to have made taxable gifts that are ineligible for annual exclusion treatment.[10] When the gift to the trust was incomplete and a distribution is made to an entity, there is a look-through to the shareholders or owners, who are considered the recipients of the gifts in proportion to their interests.[11]

On the other hand, a non-grantor trust typically creates a tax liability for its beneficiaries to the extent of distributions received. "If the trust is a non-grantor trust and the funding of the trust was a completed gift, no additional gifts would result when trust distributions are made in furtherance

[5] *See* Restatement (Third) of Trusts §47 (2003); *see also* Adam J. Hirsch, *Delaware Unifies the Law of Charitable and Noncharitable Purpose Trusts*, 36 Est. Plan. 13, 15 (Nov. 2009).

[6] *See* Bove Jr., *supra* note 2, at 34; Alexander A. Bove, Jr., *Rise of the Purpose Trust*, 144 Tr. & Est. 18, 22 (Aug. 2005).

[7] *See* Hirsch, *supra* note 5, at 14.

[8] *See* Gerry W. Beyer & Jonathan P. Wilkerson, *Max's Taxes: A Tax-Based Analysis of Pet Trusts*, 43 U. Rich. L. Rev. 1219, 1229 (2009) (discussing the federal tax consequences of purpose trusts and pet trusts in particular).

[9] *See* I.R.C. §§651, 661.

[10] *See* Treas. Reg. §25.2511-1(c)(1); *see also* I.R.C. §2501.

[11] *See* Treas. Reg. §25.2511-1(h)(1).

of [its] purpose."[12] However, if an entity receives a distribution, the entity would pay income tax, and the trust would be able to take a distribution deduction.[13]

If the recipient is not an individual or an entity, income tax may be payable by "U.S. persons connected with or benefiting from the object or purpose of the trust."[14] In other words, although a distribution to a caretaker for the family cabin or the family pet would be treated as taxable income to the caretaker and entitle the trust to a distribution deduction, no authority clearly validates this position.[15] Another approach would be to have the trustee pay the tax without taking a deduction for distributions.[16]

Distributions may also be subject to generation-skipping transfer (GST) tax.[17] If the purpose trust has no individual beneficiaries, a distribution should have no GST tax consequences because it has no skip-person.[18] On the other hand, if the trust's purpose permits distributions to or for the benefit of a non-charitable entity, distributions may be treated as if passed through to individuals. For example, if the purpose is to maintain a family corporation, distributions from the trust would be deemed to be for the benefit of the corporation's shareholders.[19] Accordingly, if a distribution is attributable to a shareholder who is a skip-person, it could be construed as a taxable distribution for GST tax purposes.[20]

With this background in mind, the following is a discussion concerning planning with highly regulated assets where purpose trusts can be useful, followed by a discussion concerning cannabis where it intersects with the estate plan and probate.

III. PET TRUSTS

A. Pet Trusts Historically.

Historically, gifts in trust for pets failed because, among other reasons, the gifts, which had no human measuring life, violated the rule against perpetuities.[21] Attempts to circumvent this problem

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[12] Bove Jr., *supra* note 6, at 24.

[13] *Id.* at 24–25.

[14] *Id.*

[15] *Id.*

[16] Note, however, in CCA 201016073, it was noted that a trustee could choose not to take a distribution deduction under I.R.C. §661 and instead pay the tax on the income at the trust level. However, it was also stated that whether or not the deduction was taken under I.R.C. §661 would not affect whether or not the beneficiary had income under I.R.C. §662. It is not clear whether this would apply to purpose trusts.

[17] *See* Bove Jr., *supra* note 2, at 37.

[18] *See* I.R.C. §2613(a).

[19] *Id.* §2651(f)(2).

[20] *Id.* §2612(b); *see also* Treas. Reg. §25.2511-1(h)(1).

[21] *See, e.g.*, Restatement (Second) of Trusts §112 (1959) ("A trust is not created unless there is a beneficiary who is definitely ascertained at the time of the creation of the trust or definitely ascertainable within the period of the rule

by creating honorary trusts also failed because they lacked a human or legal entity with standing to enforce the trust as a beneficiary. Honorary trusts created great uncertainty for the grantor, who had no assurances that the trust corpus would be used for the trust's intended purpose, because the terms of the gift were predatory in nature and unenforceable.

In 1990, the National Conference of Commissioners on Uniform State Laws (NCCUSL) recognized the importance of pets and the need to have some confidence that pet owners' intent would be carried out with respect to the care of their pets.[22] As a result, the Commissioners amended the UPC to validate a "trust for the care of a designated domestic or pet animal."[23] The original amendment allowed the trust to last for a period of 21 years.[24] That limitation was modified in 1993 to allow adopting states to add a different duration.[25]

In 2000, the NCCUSL amended the UTC to add section 408, which specifically allows trusts for animals. Section 408 limits the purpose of a pet trust to care for animals alive during the grantor or testator's lifetime.[26] Additionally, the UTC allows for the appointment of a third party (either a trust protector appointed in the instrument or a guardian *ad litem* appointed by the court) to enforce the terms of the trust.[27] The UTC also addresses the problem of excess funds. If the court determines that the trust property exceeds the amount needed for the intended purpose and that the terms of the trust do not direct the disposition, any excess funds must be held for the benefit of the grantor or the grantor's successors in interest.[28]

The UTC and the UPC contain default provisions that, depending upon how a particular state adopts them, govern the administration of a pet trust absent specific requirements in the governing instrument.[29]

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against perpetuities."); Beyer & Wilkerson, *supra* note 8, at 1221–25 (discussing the history of the pet trust); *see also* Gerry W. Beyer, *Pets Trusts: Fido with a Fortune?* (Dec. 6, 2009), Trusts and Estates Law Section, New York State Bar Association Annual Meeting, January 2010, Texas Tech Law School Research Paper No. 2010-22, *available at* http://ssrn.com/abstract=1519123 (last visited Mar. 29, 2016) (setting forth a comprehensive set of forms, links to all pet trust statutes, and a frequently asked questions section that can be used as a client handout).

[22] *See* Beyer & Wilkerson, *supra* note 8, at 1222.

[23] Unif. Probate Code §2-907 (amended 2008), 8 U.L.A. 184 (Supp. 2011).

[24] *See* Beyer &Wilkerson, *supra* note 8, at 1222–23.

[25] *Id.*

[26] *See* Unif. Trust Code §408(a) (amended 2005), 7C U.L.A. 490 (2006).

[27] *Id.* §408(b).

[28] *Id.* §408(c).

[29] *See* State Pet Trust Statutes, http://www.professorbeyer.com/Articles/Animal_Statutes.html (last visited April 14, 2017).

B. Pet Trusts Generally.

To date, over 45 states and the District of Columbia have adopted some form of pet trust legislation.[30] In some states, this provision applies only to a specific pet.[31] In others, it applies to descendants as well.[32]

For example, Washington's Pet Trust Act (WPTA) was passed in 2001 and permits trusts created for the benefit of non-human vertebrate animals.[33] WPTA provides that, unless otherwise stated in the trust document, the trust will terminate upon the death of all animals designated as beneficiaries of the trust. Disposal of the remaining trust property occurs either as a part of the testator's residuary estate, if the trust constituted a pre-residuary bequest under a will, or if the trust itself consisted of the residuary estate, to the grantor's then-living heirs.[34] WPTA permits a person named in the trust instrument, a person appointed by the court, or the person with custody of the animal to enforce the trust for the benefit of the animal beneficiary.[35]

The IRS has ruled that if a pet trust is valid under applicable state law, then pursuant to Code §641, the income of such trust would be taxable under section 1(d).[36] As a result, the Service treats income distributed to a caretaker for the care of a pet as the caretaker's taxable income to the extent of distributable net income.[37] Some practitioners have advocated for the trust to pay the income tax, and others advise trustees to gross up distributions to the caretaker to defray the tax consequence of having to include the distribution in taxable income.[38]

C. Drafting Tips.

The following are a few pet trust drafting recommendations:

1. Beneficiary of Trust. If substantial sums or valuable animals are involved, specifically identifying the animal that the trust is to benefit is important to avoid the possibility of a different pet benefiting from the trust. A grantor can use photos and a description of unique characteristics, veterinary records, a tattoo, a microchip, or DNA testing to provide sufficient identification.[39]

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[30] *Id.*

[31] *Id.*

[32] *Id.*

[33] *See* RCW 11.118.005–.010.

[34] RCW 11.118.040.

[35] RCW 11.118.050.

[36] *See* Rev. Rul. 76-486, 1976-2 C.B. 192.

[37] *See* Beyer & Wilkerson, *supra* note 8, at 1229.

[38] *Id.*

[39] *See* Stephanie B. Casteel, *Estate Planning for Pets*, 21 Prob. & Prop. 9, 12 (Nov./Dec. 2007).

2. Trustee, Representative Payee, and Caretaker of the Pet. The grantor may want to bifurcate duties, naming a trustee to manage funds and a caretaker to take possession of the pet. In some instances (such as a prize racehorse with extraordinary expenses), the trust will name a third party as representative payee to receive distributions on behalf of the pet and make disbursements, except for distributions made directly to the caretaker for out-of-pocket expenses or compensation. In other cases, one named individual will fill all three roles. If substantial funds are involved, multiple individuals should divide the labor and allow for a system of checks and balances. In that case, a mechanism for distributions to the caretaker and representative payee should be provided.

3. Fiduciaries and Successors. In addition to naming initial fiduciaries and successors, the trust agreement might place certain conditions on their appointment. For example, the agreement could instruct the personal representative to deliver the animal into the caretaker's possession only after obtaining a written promise from the caretaker to provide proper care and an agreement to relinquish the animal to a successor if that promise is not met. The agreement should also name a sanctuary or shelter of last resort in the event that the pet outlives the caretakers or none of the caretakers are able to serve.[40]

4. Distributions for Proper Care and Reasonable Expenses. The trust agreement should define what proper care means. Proper care could include hiring a full-time caretaker for certain animals, such as farm animals, race horses, and other large or valuable animals.[41] Reasonable expenses could include food, housing, veterinary and dental care, toys, exercise routines, grooming, compensation for individuals involved in caring for the pet (including walkers), travel, and burial or cremation fees.[42] If acupuncture, aromatherapy, massage, and other unusual expenses are regularly incurred and expected to continue, the agreement should describe them in detail.

5. Liability Insurance. The trust agreement may permit the purchase of property and casualty insurance to protect the fiduciaries for damage that the pet may cause to property or individuals.

6. Trust Protector. The grantor should consider a trust protector or a mechanism for the appointment of one. The trust agreement could give a trust protector the power to remove and replace fiduciaries, periodically check on the animal, consult with the pet's health care providers, and review trust financial records. The trust protector might also have the authority to locate an appropriate animal sanctuary if no suitable caretaker can be found.[43]

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[40] *See* Rachel A. Hirschfeld, *Estate Planning Strategies for People Who Have Pets*, Est. Plan., July 2009, at 24, 30.

[41] *Id.*

[42] *Id.*

[43] *See* Casteel, *supra* note 39, at 10.

In the absence of a trust protector, both the UPC and the UTC allow for court-appointed oversight of a trust.[44]

7. Termination of Trust. If permitted under applicable state law, the trust agreement should specify whether the trust will terminate upon the death of the named animals or their offspring. Often, one or more charities may be named. Note, however, that the Service has stated that an otherwise qualified charitable remainder trust for the lifetime of a pet would not qualify as a charitable deduction for the value of the remainder passing to charity.[45]

8. Reimbursement for Taxes. If the caretaker or representative payee will be subject to additional income taxes as a result of trust distributions, the agreement should specify whether distributions should be grossed up to account for that additional tax liability.

9. Special Needs of Particular Animals. While typically considered in connection with domesticated cats and dogs, pet trusts may also be used for the care of more demanding animals, such as horses. Horses live longer than a house pet, and have more complex and expensive needs. In addition to the drafting suggestions above, provisions should be made for the services of a farrier, trainer, stable manager, and all of the other specialists who typically work with the type of horse involved.

Attached as Exhibit A is a form of Pet Trust to be adapted based on applicable state law.

IV. GUNS AND GUN TRUSTS

When an estate includes firearms, a fiduciary must be careful to avoid violating federal, state, and local firearms laws. Federal law prohibits possession of and access to certain weapons, regulates the transfer of permissible weapons, and bars certain persons from owning or having access to firearms. Failure to comply with these laws may result in criminal liability, fines and forfeiture of any weapons involved.[46]

A. Regulatory Scheme.

First, an understanding of the basic regulatory scheme under federal and state law governing firearms is helpful. Federal firearms laws, codified under the Gun Control Act of 1968 (GCA), categorizes weapons as either Title I firearms or Title II firearms.

[44] *See* Unif. Probate Code §2-907(c)(7) (amended 2008), 8 pt. 1 U.L.A. 240 (1998); Unif. Trust Code §408(b) (amended 2005), 7C U.L.A. 490 (2006).

[45] *See* Rev. Rul. 78-105, 1978-1 C.B. 295.

[46] *See* I.R.C. §5872; 27 C.F.R. §479.182.

Title I of the GCA, 18 U.S.C. ch. 44, generally regulates the interstate disposition of rifles, shotguns, and handguns, the vast majority of guns privately owned in the United States.[47] State law generally regulates the intrastate transfer of Title I firearms.[48]

The National Firearms Act of 1934 (NFA), 26 U.S.C. ch. 53, regulates Title II firearms (also referred to as NFA weapons), which include automatic firearms (machine guns), silencers, short or short-barreled (that is, sawed-off) shotguns, short or short-barreled rifles, destructive devices (such as missile bearing rockets, grenades, and bombs), and "any other weapon."[49]

The NFA Branch of the Bureau of Alcohol, Tobacco, Firearms, and Explosives (BATFE) administers the National Firearms Registration and Transfer Record (NFA Registry).[50] The transfer or possession of an unregistered Title II weapon is a criminal act covered by Code §5861(e).

Under the NFA, Title II weapons are subject to strict registration, transfer, and tax requirements.[51] It is illegal for any person to possess an NFA weapon that is not registered to that person in the NFA Registry.[52]

B. Transfer of an NFA Firearm.

Transferring an NFA weapon without complying with several NFA transfer rules[53] or possessing such a weapon is also illegal.[54] Transfer of a NFA firearm includes "selling, assigning, pledging,

[47] *See* Gun Control Act of 1968, Pub. L. No. 90-618, 82 Stat. 1213 (codified at 18 U.S.C. §§921–931 (2006)).

[48] See http://smartgunlaws.org/ for a state by state summary of gun regulations. I-594, in Washington State, institutes background checks and certain additional notification requirements, for the possession and transfer of firearms by fiduciaries and their transferees. RCW 9.41.113. I-594 exempts the transferee (presumably a personal representative or trustee) of "a firearm *other than a pistol*" from its provisions where the firearm was acquired by operation of law upon the death of the former owner. RCW 9.41.113(4)(g) (emphasis added). The transferee who acquires a pistol upon the death of the former owner, however, must either lawfully transfer it (i.e., through a Federal Firearm Licensee), or notify the Department of Licensing that "he or she is in possession of the pistol and intends to retain possession of the pistol, in compliance with all federal and state laws." So, in theory, a fiduciary can transfer a long gun without having to notify the Department of Licensing, but not so a pistol (unless the transferee takes it to a Federal Firearm Licensee to effect a transfer).

[49] *See* I.R.C. §5845(a)–(h); 27 C.F.R. §479.11. The definition of "any other weapon" includes smooth-bore rifles, muzzle-loading cannons, and other somewhat exotic firearms.

[50] 27 C.F.R. §479.101.

[51] *See* I.R.C. §5861(d) (requiring the registration of certain particularly dangerous weapons under the NFA); *see also id.* §5845(a) (listing those weapons that require registration under title 18, section 5861(d) of the U.S. Code).

[52] *See* I.R.C. §5861(d). Other federal law prohibits possession of any machine gun not registered with BATFE by May 19, 1986. *See* 18 U.S.C. §922(o) (2006). Under the NFA, constructive possession will be treated the same as actual possession. *See United States v. Turnbough*, 114 F.3d 1192 (7th Cir. 1997).

[53] *See* I.R.C. §5861(e).

[54] *Id.* §5861(b).

leasing, loaning, giving away or otherwise disposing of an NFA firearm."[55] When an individual transfers or purchases an NFA weapon, the Chief Law Enforcement Officer (CLEO) of the city or county where the individual resides must sign a document called a Form 4, Application for Transfer and Registration of Firearm.[56] Title II has a broad definition of *transfer*.

Any transfer is also subject to a transfer tax, and the transferor must submit and attach to the form a photo of the transferee, as well as the transferee's fingerprints in duplicate.[57] A Form 4 is also required for the transfer to a trust. [58] The transfer by a fiduciary requires the filing of Form 5, Application for Tax Exempt Transfer and Registration of a Firearm.

Finally, under federal law certain persons cannot possess or receive any firearms (whether Title I or Title II).[59] These excluded individuals include convicted felons, persons either adjudicated a "mental defective" or committed to a mental institution, and persons convicted of misdemeanor domestic violence offenses.[60] However, the list also includes categories that may not be so self-evident, including users of any illegal drug, dishonorably discharged veterans, and persons who have renounced their U.S. citizenship.[61]

What happens when a person previously permitted to own a firearm is no longer qualified to do so? In a May 2015 decision, the Supreme Court unanimously held that while a convicted felon is prohibited from possessing a firearm, nothing strips the individual of his property interest in the firearm, and thus he retains the right to sell or otherwise dispose of it.[62] In addition, the Court held that 18 U.S.C. §922(g) does not bar such a transfer if the court is satisfied that the recipient will not give the felon control over the firearm, so that he could either use it or direct its use.[63] In other words, the felon will not need to turn over his firearms to law enforcement; instead he may dispose of it by giving it to a friend or family member (a provision that could be inserted into a trust, discussed below).

C. Fiduciaries and Firearms.

Fiduciaries need to determine the registration status of firearms coming into their possession. Retroactive registration may not be an option, putting the fiduciary in the position of having to

[55] 26 U.S.C. §5845(j).

[56] *Id.* §5812; 27 C.F.R. §479.84–.85 (2011).

[57] *See* 27 C.F.R. §479.85.

[58]Until June 13, 2016, Form 5 did not require a photo or fingerprints, discussed below.

[59] *See* 18 U.S.C. §922(d), (g) (2006).

[60] *Id.* §922(g).

[61] *Id.* §922(g)(3), (6)–(7); *see also* Nathan G. Rawling, *A Testamentary Gift of Felony: Avoiding Criminal Penalties from Estate Firearms*, 23 Quinnipiac Prob. L.J. 286 (2010) (discussing who may possess firearms, the various restrictions on transfer, and penalties for impermissible transfers).

[62] *Henderson v. United States*, 135 S. Ct. 1780 (2015).

[63] *Id.*

turn over an unregistered weapon to law enforcement. Transfers of firearms to satisfy bequests could subject a fiduciary, an heir, or both, to criminal penalties.[64] Life gets worse for both the fiduciary and an heir if the fiduciary unlawfully transfers an NFA weapon to an out-of-state heir.[65] Federal law makes it unlawful for certain categories of persons to ship, transport, receive, or possess Title II firearms. These categories include convicted felons, wanted fugitives, users of illegal controlled substances, individuals adjudicated as mentally defective or those committed to any mental institution, illegal aliens, those who have renounced U.S. citizenship, and individuals dishonorably discharged from the military.[66]

Appraisals, an integral part of any estate administration, can be problematic. Fiduciaries should only use appraisers who are licensed to take possession of the weapons to be appraised. Appraisers are usually licensed gun dealers. Before returning a weapon, an appraiser may ask the fiduciary to confirm that the he or she is lawfully able to possess a firearm. If the fiduciary is not, then the appraiser may not return the weapon.

Effective June 13, 2016, the Department of Justice added a new section to 27 C.F.R. Part 479 to address the possession and transfer of NFA items registered to a decedent. The new section clarifies that the executor, administrator, personal representative, or other person authorized under state law to dispose of property in an estate may possess a firearm registered to a decedent during the term of probate without such possession being treated as a "transfer" under the NFA. It also specifies that the transfer of the firearm to any beneficiary of the estate may be made on a tax-exempt basis.

While federal law provides a safe harbor to the fiduciary, state and local laws may complicate the fiduciary's job. Several states have assault weapons bans that make it illegal to own some Title I weapons (mostly certain semi-automatic rifles, pistols, and shotguns) that would be legal to possess under federal law.[67] States or localities might further regulate or prohibit ownership of NFA weapons. State law must be reviewed for proper compliance, before transferring any weapon to another person.

Because of the potential liability a fiduciary faces when transferring a firearm to a beneficiary, a fiduciary may want to consider adding special provisions to a receipt when releasing a firearm to a beneficiary, such as the following:

> I certify that: I possess a valid, current [State] Weapons Carry License; I am legally entitled to receive, own, possess and use the Gun[s], under all applicable federal, state and local laws and regulations; I have no knowledge of, and I have never been informed of, any restrictions or prohibition on my right to receive, own, possess or use the Gun[s] or other such firearms; and I will fully comply with all federal, state

[64] *See* 18 U.S.C. §922(d).

[65] *See* I.R.C. §5861(b), (e).

[66] 18 U.S.C. §922(d), (g).

[67] *See, e.g.*, Cal. Penal Code §12280 (2009).

and local laws and regulations regarding my ownership, possession and use of the Gun[s].

D. Gun Trusts.

Individuals may transfer NFA weapons to, and fiduciaries may purchase NFA weapons in, an entity, such as a corporation, limited liability company (LLC), or revocable trust, to avoid some of the rules that otherwise regulate such transfers. Individuals often opt for trusts because they avoid annual filing fees, public disclosure, or a separate tax return.[68] A trust designed specifically for the ownership, transfer, and possession of an NFA weapon may be known as a gun trust, NFA Trust, Firearm Trust, or Title II Trust. While a gun trust could be used to hold both Title II and Title I firearms, doing so could unwittingly subject Title I firearms to rules that would otherwise only apply to Title II firearms. (Ownership and transfer of Title I firearms can generally be handled through a standard estate planning revocable trust.)

According to IRS Info. Ltr. 2015-0039 (Dec. 24, 2015), a gun trust is still considered a "trust" for tax purposes under Treas. Reg. §301.7701-4 even when there are no ascertainable beneficiaries.[69]

While NFA firearms can only be transported and shot by their registered owner, a trust can name numerous trustees, each of whom may lawfully own the weapon without triggering transfer requirements. Once a weapon becomes a trust asset, any beneficiary may use it (including a trustee, but only if named as a beneficiary and not solely in a trustee capacity). Conversely, if an individual owner allowed another individual owner subject to trustee approval to use an NFA weapon not held in a trust, that use could be considered an unlawful transfer subject to criminal penalties. The trust can name minors as beneficiaries, subject to any state mandated use restrictions, until they are old enough to possess the weapon outright. Moreover, the grantor can be a life beneficiary—although not the sole beneficiary (or the doctrine of merger will cause the trust to be disregarded).

The trust agreement can direct the disposition of NFA weapons in the event an owner becomes an excluded person by, for example, providing that upon a felony, the felon will lose all ability to have direct or indirect use of the weapons in the trust and that the weapons will pass outright or in trust to the contingent beneficiaries.

Gun trusts have been popular historically because of the ability to avoid federal laws requiring an NFA trust to submit fingerprints or seek CLEO approval required for individual firearm purchases or transfers. Instead, the federal government would verify and investigate the application.[70]

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[68] David Goldman, an attorney in Jacksonville, Florida is credited with drafting the first gun trust, which he refers to as an NFA firearms trust, in 2007. *See* Margaret Littman, *In Goldman Guns Trust*, 97 A.B.A. J. 12, 13 (Feb. 2011).

[69] Dep't of the Treasury, Internal Revenue Service (Nov. 9, 2015), *available at* https://www.irs.gov/pub/irs-wd/15-0039.pdf (last visited May 1, 2016).

[70] *See* 18 U.S.C. §923 (2006 & Supp. 2010); 28 C.F.R. §25.1 (2010).

Effective June 13, 2016, the Department of Justice amended the regulations of the BATFE regarding the making or transferring of a firearm under the NFA. [71] This final rule, referred to as "41F," defines a new term, "responsible person." A "responsible person" is any individual who possesses the power to direct the management and policies of a gun trust and includes persons with such power and those who have the power to receive, possess, ship, transport, deliver, transfer or otherwise dispose of a firearm for or on behalf of the trust.[72] Responsible persons include settlors, trustees and trust protectors of gun trusts.

41F also requires *each* responsible person, in connection with a trust or legal entity holding an ATF firearm, to complete ATF Form 5320.23, entitled "Responsible Person Questionnaire" and to submit photographs and fingerprints when the trust or legal entity files an application to make an NFA firearm a trust asset. It requires that a copy of all applications be forwarded to the CLEO of the locality in which the applicant/transferee or responsible person is located. But it eliminates the requirement for a certification signed by the CLEO. The purpose of the new form is to ensure that the purported responsible person is not in fact a "prohibited person" who may not possess an NFA firearm.

Any new responsible persons added to the trust now must submit Form 5320.23. If a trust was executed and funded prior to the new rules coming into effect, new beneficiaries may be added without having to comply with the responsible person questionnaire filing requirement.

A thorough discussion concerning the unique provisions of an NFA gun trust is beyond the scope of this article, but the provisions are numerous and complex. A standard revocable trust form is wholly inadequate in this context. The trust agreement should specifically state that its purpose is to own, possess, manage, and dispose of NFA firearms. The settlor need not be a trustee, however, the settlor may not use a trust-owned firearm unless also named as a trustee. Where multiple persons will use trust property, each should be named as a trustee.

Gun trusts may be irrevocable, but generally they are revocable so that the settlor may retain the power, among other things, to add or remove trust property, as well as add and remove beneficiaries.

A trustee has an obligation to safeguard firearms owned by a gun trust. The trust agreement should include details that provide guidance to the trustee and beneficiaries to assist them in avoiding unintentional violations of the NFA rules. Specifically, the trust agreement should provide which trustees and beneficiaries can have access to firearms and ammunition, under what circumstances, and what happens if a trustee, successor trustee, trust protector, or beneficiary becomes a "disqualified person." Persons who are not allowed to buy or own firearms cannot serve as trustees. The trust agreement should also require trustee compliance with any applicable transfer rules.

[71] 27 C.F.R. pt. 479, *as amended by* Docket No. ATF 41F; AG Order No. 3608-2016, Fed. Reg. Vol. 81, No. 10 (Jan. 15, 2016).

[72] 27 C.F.R. §479.11.

The risk created by new 41F is that a successor trustee appointment becomes effective and the new trustee is not aware of the need to qualify as a responsible person, thus failing to comply with 41F. Similar situations could arise for beneficiaries or for people later appointed to a trust containing firearms subject to 41F. New trusts should also contain guidance and savings language with respect to "responsible persons," to avoid non-compliance with 41F.

The trust may not permit the transfer a firearm to a person who may not lawfully buy or own firearms. The transfer of an NFA firearm into a trust or other entity will be subject to a transfer fee. Accordingly, a trustee often purchases NFA weapons directly to avoid the second transfer fee that would accrue if an individual purchaser purchased a weapon and then transferred it to the trust. While the transfer of an NFA weapon to an heir in satisfaction of a bequest is exempt from the transfer tax, such a transfer still requires the filing of Form 5\. Any distribution of a Title II firearm should not be permitted until approval of Form 5 has been obtained.

The trustee's power to change the trust name should be limited. Because a firearm is registered in the trust's name in the NFA Registry, a change in trust name would require re-registration of the firearms and payment of a transfer tax.

Because each state has different laws and local ordinances regulating firearms, unlike revocable trusts used for general estate planning purposes, trusts used to hold NFA firearms are not necessarily portable.[73] A gun owner desiring to cross state lines must still provide advance notice to the BATFE and receive approval. Generally, the BATFE will approve a 365 day period to multi-state use.

Gun trusts are not a panacea. They do not avoid constructive possession, which can occur when a gun owner leaves a firearm where a prohibited person or any other individual not allowed to possess the firearm resides or has access to such weapon. Gun trusts do not bypass rules regarding waiting periods nor do they avoid criminal liability if prohibited parties are allowed to use firearms.

Even with a gun trust, the trustee is responsible for determining the capacity of the beneficiary and the federal, state, and local laws that apply to the individual before allowing a beneficiary to use a trust weapon or distributing an NFA weapon to a beneficiary. Unlike a traditional revocable trust, which can be revoked at any time by the grantor, BATFE must approve termination of the gun trust and distribution of its assets to its beneficiaries, as it would any other transfer. Nor may a trustee or beneficiary transport any of the assets across state lines where registered, without prior BATFE approval.

V. WINE

With the wine market exploding, nationally and internationally, it is not unusual for a fiduciary to come into the possession of a sizeable and valuable wine collection in an estate or trust. Ideally, this would not come as a surprise to the fiduciary or his counsel, because the estate planning

[73] *See* NFA Gun Trust Lawyer Blog, http://www.guntrustlawyer.com (last visited Mar. 30, 2016) (compiling applicable state laws).

attorney would have asked the clients at the planning stage whether their portfolio included unique assets that might require special care and/or a fiduciary with special knowledge. Often this is not the case.

It is important to keep in mind that wine is a regulated asset and, therefore, selling it is different from selling most other estate assets. The sale of wine in most states is subject to the three-tier system. This system is a byproduct of the Twenty-First Amendment of the U.S. Constitution. When first passed in 1933, it overturned the Eighteenth Amendment, which outlawed the manufacture, distribution, and sale of all types of alcoholic beverages in 1919 (with only a few exceptions regarding medicinal or religious uses).

As a result of the three-tier system, which is still in place in most states, retailers can only purchase alcohol from distributors, and distributors can only purchase from manufacturers or importers. The typical personal representative does not fit into any one of these categories and, therefore, must typically turn to someone who does.

A. Drafting for the Wine Collector.

At the planning stage, a collector should consider special provisions in his or her estate planning documents for the distribution of wine—whether to distribute to individuals, give to charity, sell at an auction, or store long-term, for either sale or consumption, in which case a wine trust should be considered. As discussed below, maintaining the collection, which will involve inventories, appraisals, insurance, storage, and transportation, comes at a steep price. There is also the option of simply having it consumed by the collector's loved ones at the funeral or memorial service. (Keep in mind that the value of the collection will still be included in the decedent's gross estate for estate tax purposes.)

When handling an estate, one of the fiduciary's first and most important jobs is to marshal the assets. This includes locating the wine collection. Often a fiduciary might use a personal property insurance rider as a guide to a client's most valuable assets. These are often incomplete as to typical valuables such as art and jewelry, and rarely list fine wine. Therefore, a fiduciary is going to have to dig deeper, sometimes literally.

This might be an easy task for clients who have built sophisticated cellars to properly store and often display their prized wines. However, for most families, the wine is often located in basements so dusty and dirty that the identity of its contents can be obscured. On the other hand, the urban client might have what appears to be a small collection at home, but may have rented temperature controlled off-site storage for a collection, or at least for part of a collection that did not fit in the home storage. Moreover, the collector may also have placed orders for future distributions, even future releases, or may belong to a wine club that ships regularly. An older client may have decided to downsize a collection, and consigned bottles or cases to be sold. In other words, never assume that what you see is all there is. A thorough review of a collector's records (i.e., letters, faxes, confirmation emails, invoices, canceled checks, credit card bills, etc.) by a fiduciary is necessary to locate all of the bottles, present and future.

B. Advising the Fiduciary.

Like jewelry and artwork, the fiduciary has a duty to preserve and store a collection appropriately. If the fiduciary does not have experience with fine wine, he or she may need to be educated about the basics: store it on its side to avoid drying out the cork, do not store it on wood that emits fumes that could seep into the wine, and avoid sunlight, which degrades the wine over time. Storage should be not only humidity-and temperature-controlled (55˚F is considered ideal by some), but secure. Stories abound of the fiduciary showing up with an appraiser to find that the collection had already been consumed by thirsty heirs. If the temperature is maintained with a heating or cooling system, it should have a backup power supply. It should also be protected from flooding and moisture damage. If that is done with a sump pump, it too needs a backup power supply. And on and on.

A fiduciary should not put off having a collection inventoried, and under certain circumstances appraised. It is important to know the extent of the collection to determine whether it needs to be insured, or if the insurance in place is adequate.

If the estate is taxable for federal or state purposes, the fiduciary must ascertain the value of the collection at the time of the decedent's death or as of six months after the decedent's death, if the alternate valuation date is elected.[74] The necessity for an appraisal arises where one bottle of wine may have a value of more than $3,000, or a collection in its entirety may have a value that totals more than $10,000.[75]

C. Estate Tax Issues.

Wine is reported on Schedule F, "Other Miscellaneous Property Not Reportable Under Any Other Schedule," of the estate tax return. Even if consumed at the funeral, it is considered an asset of the estate (although the value might be deducted as a funeral expense). Liquidity (no pun intended) is going to be an important concern for the fiduciary of an estate. It may be necessary to sell some of the wine to raise funds for taxes. So, the fiduciary will need to begin planning early for the payment of estate tax on the illiquid "liquid assets." On the other hand, putting too much of one wine on the market at once may result in a blockage discount when it comes to pricing it, a concept borrowed from the securities market and now frequently used for the sale of large collections, such as art and wine.[76] Many contributing factors enter into the blockage discount, somewhat based on a sense of supply and demand. In other cases, factors such as the quality of the wine, whether the bottle is in pristine condition, or its rarity may be considered.

If wine is to be distributed to an individual or charity, or auctioned off, the fiduciary should consider distribution as soon as feasible, to eliminate the risk of loss from theft or damage in the estate, and to reduce the expense of storage and insurance. In other circumstances, the decedent may not have left provisions in his or her estate plan for the distribution of the wine collection.

[74] Treas. Reg. §§20.2031-1(b), 2032-1(a).

[75] Treas. Reg. §20.2031-6(b).

[76] The IRS recognizes that the price may be depressed when multiple cases or bottles of the same wine are appraised or placed on the market. This is referred to as a blockage discount. Treas. Reg. §§20.2031-2(e), 25.2512-2(e).

Thus, a fiduciary may simply elect to sell the collection as part of settling the estate. Prior to selling, however, the fiduciary must consider federal and state alcohol distribution laws. Some states still maintain a three-tier system for distribution of alcohol, put in place following the end of prohibition. In these states, individuals may only buy from retailers, who may purchase from importers or manufacturers. A few states allow direct sales to the consumer or have exceptions for brewpubs. And a few allow a one-time permit to sell from an estate. Otherwise, it is necessary to use an auction house to facilitate a sale.[77]

To protect against blockage discounts and allow wine to be sold over an extended period of time, or simply to hold wine to be consumed by extended family members, wine could be left in trust.

D. Practice Tips.

Purpose trusts should not be forgotten as a planning tool for a wine collection meant to be held long-term. When wine is left in trust, the fiduciary should waste no time in making arrangements for long-term storage. If collectors opt for a trust, they should also direct that sufficient funds be distributed to the trust to maintain the collection.

A wine trust is a good candidate for a trust protector. A trust should either name one or contain a mechanism for the appointment of one. The trust agreement could give a trust protector the power to remove and replace fiduciaries, periodically check on the wine, and review trust records, including records of sales, auction results, and consignment agreements. The trust should also contain a provision for termination—when the wine has been sold, drunk, or otherwise liquidated. Or, perhaps, when the inventory reaches a certain level, the remaining bottles could be donated to charity.

VI. AIRCRAFT

Aircraft ownership and registration is a technical area not typically familiar to the average estate planning attorney. The following is by no means a thorough examination of the laws applicable to aircraft owners. Rather, it outlines considerations for the attorney advising aircraft owners with respect to estate planning, and fiduciaries who find themselves in possession of aircraft. It is, as they say, just enough to make you dangerous. It should also cause sufficient fear to convince you to seek the help of an expert any time things with wings in an estate plan are involved.

Aircraft include airplanes, rotorcraft, gliders, and anything else that may become airborne and is required to be registered with the Federal Aviation Administration (FAA). Planning should also cover an interest in a fractional ownership program, hangar leases, long-term service contracts, expensive aviation equipment, and certain aircraft components and parts.

Because aircraft are generally depreciating assets and expensive to use and maintain, they are not ideal assets for lifetime gifting. However, they often show up on the inventory of a high-net-worth

[77] More and more places conduct wine auctions now – not just Christie's. Beyond Christie's, a fiduciary may also look to organizations such as New York-based Scarsdale, Zachy's, winebid.com, winecommune.com or Chicago-based Hart Davis Hart to auction the estate's wine collection.

decedent's estate. Because aircraft can be quite valuable, illiquid, and subject to multiple regulatory schemes, they can make an estate administrator's job extremely complex.

Federal excise tax, as well as state sales and use tax, while not discussed in detail below, must also be addressed when advising clients regarding the purchase or lease of aircraft.

The FAA's Aircraft Registration Branch regulates aircraft registration and transfers.

Like cars, weapons, and cannabis (in states where legal), aircraft are highly regulated. Aircraft owners must be registered with the FAA civil aircraft registry.[78] Owners may include individuals and entities, including trusts. Where an owner is a non-U.S. citizen, specialized trusts or corporations are required. Failing to follow the strict regulations of the FAA can result in an invalid registration, leading to a cascade of further problems, including loss of insurance coverage.

A. Transfer of Ownership.

Transfer of an aircraft is accomplished using FAA form "Aircraft Bill of Sale," available online at http://www.faa.gov/documentLibrary/media/form/ac8050-2.pdf. Where an estate or trust is involved, additional rules apply. When a transfer is by an estate executor or administrator, a certified copy of Letters of Administration or Letters Testamentary must be included. Where no probate was conducted, an heir may submit an affidavit attesting to a lack of probate and legal entitlement to ownership. A trustee may transfer ownership by including a certified copy of the court order appointing the trustee or, if no court order is involved, a certified copy of the trust instrument.

B. Taxation Basics.[79]

Many states impose a personal property sale or use tax on transfers of aircraft, in addition to annual excise taxes. For example, information regarding registration and taxation of aircraft in Washington is found at http://www.wsdot.wa.gov/aviation/registration/register3steps.htm. Washington imposes an annual excise tax on any aircraft, with limited exceptions, used within the state.[80]

[78] 49 U.S.C. §44102; 14 C.F.R. §47.3. Documentation required for registration includes original signed documents filed with the FAA, a bill of sale transferring title (which reflects a complete chain of title from the last registered owner), and an Aircraft Registration Application (AC Form 8050-1, found at http://www.faa.gov/documentLibrary/media/Form/AC_8050-1_OMB_4-2017.pdf), which requires detailed information regarding the aircraft and the owner, and proof of citizenship of the individual owners or the underlying owners of an entity (for trusts, all trustees and beneficiaries must be U.S. citizens unless a "non-U.S. citizen trust" is used, in which the beneficiary is not a U.S. citizen but the trustee-owner is).

[79] A good resource for taxes applicable to aircraft owners is maintained by the Aircraft Owners and Pilots Association (AOPA), *available at* http://www.aopa.org/Pilot-Resources/Aircraft-Ownership/The-Pilots-Guide-to-Taxes.aspx (last visited May 1, 2016).

[80] RCW 82.48.020, 82.48.100 (exempt aircraft).

If an aircraft is first delivered in a state without a sales tax, it still may be subject to use tax if later brought into a state that imposes one. If sales tax was previously paid, use tax may be imposed on the difference between the state's sales or use tax and the tax paid to the state where the sale occurred. A fiduciary delivering aircraft to a beneficiary in another jurisdiction must keep these potential taxes in mind when completing the transfer.

Keep in mind that some states, like Washington, consider an aircraft owned by a non-resident to be based in-state if it has spent more than 90 days in the state during any 12-month period, subjecting the aircraft to use tax in that state.[81] This is true even if the aircraft is legally based and pays tax in another state.

Most states consider transfers of aircraft to a revocable trust not to be a taxable event.[82] Nevertheless, in some jurisdictions, taxes may be imposed when ownership is restructured and even when ownership of the aircraft is transferred to a trust simply for estate planning purposes.[83] Moreover, some jurisdictions tax the transfer of a plane by a corporation or partnership to one of its affiliates solely for liability protection purposes.[84]

C. Ownership Through an Entity.

An LLC or corporate entity is often used to hold aircraft and shelter the owner's other assets from the high possibility of owner or operator liability. For estate planning purposes, revocable trusts are commonly used simply for probate avoidance, but they do not afford liability protection. To obtain both liability protection and probate avoidance, a revocable trust may hold interests in the entity to which the aircraft is registered, but raises new issues, discussed below.

D. Trusts.

A trust holding an airplane is a type of purpose trust.[85] Similar to the structure of an Illinois Land Trust, the trustee is the titled and registered owner of the aircraft, but the beneficiary has the right to dissolve the trust at any time and return possession of the aircraft back to him- or herself, or on to a qualified third party. Furthermore, the FAA has the right to obtain information directly from the owner/operators because, in spite of the trust structure, they have non-delegable regulatory obligations to the FAA. Typically, the beneficiary will be the one to insure the aircraft, and to operate and maintain it in accordance with FAA requirements.

Also similar to an Illinois Land Trust, title to the aircraft can be transferred at any time from the trustee to any party designated by the beneficiary using an FAA form bill of sale. This, however,

[81] RCW 8.48.100(3).

[82] *See, e.g.*, Cal. Rev. & Tax Code §6285(b); 68 Okla. Stat. §6003(17).

[83] *See, e.g.*, 35 Ill. Comp. Stat. 157/10-15.

[84] *See, e.g.*, Fla. Admin. Code r. 12A-1.007(25)(d). *But see* 23 Va. Admin. Code §10-220-5 (transfer to corporate affiliate is exempt).

[85] A purpose trust exists to carry out a specific objective, in this case holding and maintaining aircraft, rather than for the benefit of individual beneficiaries.

would have the effect of cancelling the aircraft's registration. The trustee cannot sell the aircraft without the beneficiary's direction. While this is an inherent aspect of a trust holding aircraft, it should be specifically provided in the trust instrument.

The trust agreement should create an affirmative duty on the part of the aircraft operator (where the operator is not the beneficial owner) to regularly maintain and provide current information regarding the aircraft and its operations.

The FAA imposes a number of requirements for trusts holding aircraft. Under Federal Aviation Regulation (FAR) 47.7(c), each trustee must be either a U.S. citizen or a resident alien.[86] The trustee must also submit an Affidavit of Citizenship from each trustee, a copy of the trust agreement, and an Aircraft Registration Application to the FAA. If the trustee does not want to make a representation regarding the citizenship of the beneficiary, the beneficiary must provide a separate affidavit of citizenship.

Again, beware that states may subject the transfer of title to a special purpose entity to sales or use tax.

E. Advising the Trustee.

If a trust was established during the grantor's lifetime, a successor fiduciary should, immediately upon appointment, confirm that registration with the FAA and airworthiness directives (ADs) are all in good standing. ADs are legally enforceable regulations issued by the FAA in accordance with 14 C.F.R. Part 39 to correct an unsafe condition in a product. Part 39 defines a product as an aircraft, engine, propeller, or appliance. Note that ADs[87] are delivered electronically or by paid subscription, so a search of the grantor's email may be necessary. A periodic review of the FAA website by product name for applicable ADs is also a prudent practice. If ADs are not timely acted upon, registration may lapse.

Aircraft can be registered to a single applicant as trustee, or to several applicants as co-trustees. To register, the trustee(s) must submit:[88]

- An affidavit showing that each beneficiary under the trust is either a U.S. citizen or a resident alien. This includes each person whose security interest in the aircraft is incorporated in the trust. If any beneficiary is not a U.S. citizen or a resident alien, the trustee must provide an affidavit stating that the trustee is not aware of any reason or relationship that would give the non-citizen a share of control greater than 25% to influence or limit the exercise of the trustee's authority. Furthermore, the

[86] U.S. citizen is defined for FAA purposes under 14 C.F.R. §47.2.

[87] Airworthiness Directives, both current and historical, may be found here: http://www.airweb.faa.gov/Regulatory_and_Guidance_Library/rgAD.nsf/MainFrame?OpenFrameSet.

[88] For more information, download the form at Information to Aid in the Registration of U.S. Civil Aircraft, AC Form 8050-94.

trust agreement must provide that those persons together may not have more than 25% of the aggregate power to direct or remove a trustee for cause.[89]

- A certified copy of the complete trust instrument and a "copy of each document legally affecting a relationship under the trust."[90]
- An original signed bill of sale from the present registered owner to the trustee(s).
- An original application for registration showing the trustee(s) as applicant, signed by the trustee(s).
- A $5 registration fee payable to the FAA.

If a client prefers to use an existing trust or a trust organized for a different purpose to own the aircraft, the trust agreement will need to be amended in order to satisfy the FAA requirements mentioned above. The FAA must approve all trust agreements used to register an aircraft. Because the agreement will be shared with the FAA, confidentiality of the terms regarding other assets held in a trust will be lost. Where confidentiality is a concern, clients should use a single purpose trust for aircraft.

Finally, like in a family cabin trust, the grantor should be encouraged to fund the trust with either a substantial endowment or a life insurance policy to fund the maintenance and operation of the aircraft in the future. Without this sinking fund, it is not likely that multiple family members will be able to agree upon how to maintain the aircraft, and it will likely be sold.

F. Corporations and LLCs.

It is important that a client have a clear understanding of the type of conduct qualifying as commercial versus non-commercial use. FAA regulations classify aircraft into various categories, generally commercial and non-commercial, and grant airworthiness certificates authorizing aircraft for flights under one of these categories. An owner who operates aircraft for personal use holds a certificate under 14 C.F.R. Part 91 of the FAA regulations. The personal use regulations impose significantly less stringent operational and maintenance standards than those applicable to charter carriers, which may include family offices (under 14 C.F.R. Part 135) and airline carriers (under 14 C.F.R. Part 121).

The inclination in estate planning is to use an entity—a corporation or LLC—to own property with which risk is associated, to shield a client from liability. However, where the sole purpose for an entity's existence is to hold title to aircraft, there is a risk that this will be considered a commercial

[89] 14 C.F.R. §47.7(c)(3). While the C.F.R.s do not define "cause," the FAA's Notice of Policy Clarification for the Registration of Aircraft to U.S. Citizen Trustees in Situations Involving Non-U.S. Citizen Trustors and Beneficiaries, 78 Fed. Reg. 36,412 (June 18, 2013), refers to the Restatement of Trusts as illustrative of the definition, and suggests that willful misconduct and gross neglect satisfy this limitation.

[90] 14 C.F.R. §47.7(c)(2)(i).

arrangement, subject to the more stringent rules applicable to charter carriers under 14 C.F.R. Part 135.

Under Part 91, the owner/user of the aircraft is responsible for full control over the operation of the aircraft. The flight crew may not operate the plane for compensation. Practically speaking, the owner must also be the operator. The mere fact that the owner/operator funded the expenses of a flight crew has brought the operator within the definition of a commercial operator and no longer covered by Part 91. The practical solution to this problem is typically to have the owner/operator enter into a "dry lease" arrangement with an entity, which provides support services, including pilots, crew and maintenance.

The FAA classifies aircraft leases as either "dry leases" or "wet leases."

Under a dry lease, the aircraft owner provides only the aircraft and no crew to the lessee.[91] An entity may be formed for the sole purpose of ownership of an aircraft by the lessor. It may lease that aircraft without a crewmember or any other amenities to a related company or party, the lessee. The lessee is considered to be in "operational control" of the aircraft in a dry lease arrangement, and provides its own flight crew, maintenance, and any other amenities. Dry leasing is not considered a commercial operation from the FAA's perspective as long as the pilots do not have a financial or employment relationship with the lessor.

A wet lease is a leasing arrangement, defined under FAR 91.501(c)(1), whereby the lessor of an aircraft provides the aircraft, crew, maintenance, and any other services required by the lessee. The lessee typically pays the lessor based on hours operated. The lessee may also be required to cover the cost of fuel, airport fees, and any other fees.

Operation under the wrong certificate is subject to steep fines.[92] On top of the fines, insurance coverage is contingent on the aircraft being operated in compliance with FAA regulations, and may be lost if an operator is not covered by the proper certificate.

G. Practical Alternatives to Aircraft Ownership.

Some families are attached to their planes, especially those with historic, sentimental, or collectible value. However, for the client who strictly wants to provide the convenience of private travel to her heirs, she might consider the advantages of fractional ownership or a jet card.[93] The testator needs to realize that once a plane passes to multiple heirs, it cannot be in two places at once, making its use even harder to allocate than the family cabin, which at least stays in one place. Either arrangement— fractional ownership or a jet card (akin to an expensive Starbucks card)—

[91] 14 C.F.R. §91.1001(b)(2).

[92] 14 C.F.R. §13.305(d) (providing for fines of $11,000 for each violation of operating under a Part 91 certificate rather than a Part 135 certificate).

[93] Some of the more popular fractional ownership companies include NetJets, FlexJet or FlightOptions; and popular charter jet card arrangements are provided through companies such as Marquis Jet (a division of NetJets), Blue Star Jets, Skyjet and JetCard.

can provide the family with on-demand transportation with less cost, liability, and opportunity for family strife.

VII. CANNABIS

A. Introduction.

For decades, marijuana transactions in the United States were conducted under implicit or explicit prohibition. In the last few years, states have increasingly moved to legalize, tax, and regulate marijuana for medical and/or recreational purposes. At least 28 states and the District of Columbia permit its use for medical reasons.[94] In many states, measures have been introduced that would establish a regulatory framework for commercial sales of marijuana. And other states are considering measures that would decriminalize medical and recreational marijuana by eliminating criminal penalties for possession of small amounts of the substance, and join the broader state-by-state effort to end its prohibition.

The continued introduction of bills and passage of legalization laws is a clear indication that the issue of legalized or decriminalized marijuana will remain on the table in the years to come. This widespread shift in the public's attitude toward the substance is providing operators and investors with opportunities for business growth and development. Many believe that the industry is on the verge of becoming mainstream.

According to studies by Arcview Market Research, legal marijuana is among the fastest-growing markets in the United States. Arcview estimates that $6.7 billion worth of legal marijuana was sold in 2016, a 30% increase from the prior year.[95] It is likely that additional states will legalize marijuana for recreational adult use in the next several years, creating exponential growth in the cannabis market, significant wealth for many in the industry, and complex ethical and legal issues for estate planners.

This following is a very general overview of the federal and state legal landscape and discusses the estate planning, tax, leasing, intellectual property, and ethical considerations for attorneys advising in this area.

B. Federal Law.

Under the federal Controlled Substances Act (CSA), the cultivation, distribution, and possession of cannabis are prohibited for any reason other than to engage in federally approved research. The purpose of the CSA is to regulate and facilitate the manufacture, distribution, and use of controlled substances for legitimate medical, scientific, research, and industrial purposes, and to prevent these substances from being diverted for illegal purposes. The CSA places various plants, drugs, and chemicals into one of five schedules based on a substance's medical use, potential for abuse, and

[94] *See* NORML, Medical Marijuana, http://norml.org/legal/medical-marijuana-2 (last visited Apr. 18, 2017).

[95] Gene Marks, *How much marijuana was sold in 2016? A lot!*, The Washington Post (Jan. 6, 2016) citing Arcview Market Research found at https://www.arcviewmarketresearch.com/.

safety or dependence liability.[96] Schedule I substances are deemed to have no currently accepted medical use in treatment and can only be used in very limited circumstances, whereas substances classified in Schedules II, III, IV, and V have recognized medical uses and may be manufactured, distributed, and used in accordance with the CSA. Federal civil and criminal penalties are available for anyone who manufactures, distributes, imports, or possesses controlled substances in violation of the CSA.[97]

When Congress enacted the CSA in 1970, marijuana was classified as a Schedule I drug.[98] Today, marijuana is still categorized as a Schedule I controlled substance and is therefore subject to the most severe restrictions contained within the CSA. Pursuant to the CSA, the unauthorized cultivation, distribution, or possession of marijuana is a federal crime.[99]

C. Recreational Use of Marijuana.

The sale and use of recreational cannabis first became legal after voters approved Amendment 64 of the Colorado Constitution in the November 2012 elections. Since then, other states have passed similar measures.[100] Each state's laws differ, but they generally follow the system put in place in Colorado, which is summarized below.

1. Colorado.

In November 2012, Colorado voters approved an amendment to the Colorado Constitution to ensure that it "shall not be an offense under Colorado law or the law of any locality within Colorado" for an individual 21 years of age or older to possess, use, display, purchase, consume, or transport one ounce of marijuana, or to possess, grow, process, or transport up to six marijuana plants.[101]

The amendment also provides that it shall not be unlawful for a marijuana-related facility to purchase, manufacture, cultivate, process, transport, or sell larger quantities of marijuana so long as the facility obtains a current and valid state-issued license. However, the amendment expressly permits local governments within Colorado to regulate or prohibit the operation of such facilities.

Colorado's law also sets forth a three-tier distribution and regulatory system, similar to that established in Washington, involving the licensing of marijuana cultivation facilities, marijuana

[96] Controlled Substances Act, Pub. L. No. 91-513, 84 Stat. 1236 (1970).

[97] For a detailed description of the CSA's civil and criminal provisions, see Brian T. Yeh, CRS Report RL30722, *Drug Offenses: Maximum Fines and Terms of Imprisonment for Violation of the Federal Controlled Substances Act and Related Laws* (Jan. 20, 2015), *available at* https://www.fas.org/sgp/crs/misc/RL30722.pdf.

[98] 21 U.S.C. §812(c).

[99] Very narrow exceptions to the federal prohibition do exist. For example, one may legally use marijuana if participating in an FDA-approved study or in the Compassionate Investigational New Drug program.

[100] See, e.g., http://www.businessinsider.com/where-can-you-legally-smoke-weed-2017-1.

[101] Colorado Amendment 64, *amending* Colo. Const. art. XVIII, §16(3), *available at* www.fcgov.com/mmj/pdf/amendment64.pdf (last visited Mar. 30, 2016).

product manufacturing facilities, and retail marijuana stores. To implement the amendment, the Colorado General Assembly passed three bills that were signed into law on May 28, 2013.[102]

Unlike the relatively specific Washington initiative (discussed below), Colorado's constitutional amendment provided only a general framework for the legalization, regulation, and taxation of marijuana in Colorado—leaving regulatory implementation to the Colorado Department of Revenue.

On September 9, 2013, the Colorado Department of Revenue and State Licensing Authority adopted regulations to implement licensing qualifications and procedures for retail marijuana facilities. The regulations establish procedures for the issuance, renewal, suspension, and revocation of licenses; provide a schedule of licensing and renewal fees; and specify requirements for licensees to follow regarding physical security, video surveillance, labeling, health and safety precautions, and product advertising.[103]

In late 2013, the Colorado Marijuana Enforcement Division issued its first recreational marijuana licenses to 348 businesses (136 retail stores, 31 product companies, 178 growing facilities, and 3 testing laboratories).[104] While these businesses were granted state approval to produce and sell marijuana, they may have also needed to gain additional licensing approval from local governments prior to their operation.

In Colorado, to be eligible to apply for a Colorado Retail Marijuana Business License, all owners must meet each of the following statutory requirements:

a. Must be a resident of Colorado for two years prior to application;

b. Must be 21 years of age;

c. May not have any controlled substance felony conviction in the 10 years immediately preceding his or her application date;

d. May not have any other felony convictions that have not been fully discharged for five years immediately preceding his or her application date;

e. May not be financed in whole or in part by any other person whose criminal history indicates he or she is not of good moral character (after considering the factors in Colo. Rev. Stat. § 24-5-101(2)) and reputation satisfactory to the respective licensing authority;

f. May not have a criminal history that indicates that he or she is not of good moral character after considering the factors in Colo. Rev. Stat. § 24-5-101(2);

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[102] *See* Colo. Dep't of Revenue, Permanent Rules Related to the Colorado Retail Marijuana Code (Sept. 9, 2013).

[103] *Id*.

[104] John Ingold, *Colorado Issues First Licenses for Recreational Marijuana Businesses*, Denver Post, Dec. 23, 2013.

g. May not employ, be assisted by, or financed, by any other person whose criminal history indicates he or she is not of good character and reputation;

h. May not be a sheriff, deputy sheriff, police officer, or prosecuting officer, or an employee of a local or state licensing authority; and

i. May not employ any person at the retail marijuana business who has not passed a criminal history record check.[105]

2. Oregon.

In Oregon, Measure 91, the Control, Regulation, and Taxation of Marijuana and Industrial Hemp Act, allows Oregonians to grow limited amounts of marijuana on their property and to possess personal limited amounts of recreational marijuana for personal use as of July 1, 2015 under Oregon law. The measure also gives the Oregon Liquor Control Commission (OLCC) authority to tax, license, and regulate recreational marijuana grown, sold, or processed for commercial purposes. The OLCC does not regulate the home growing and personal possession provisions of the law. Nor does it regulate the sale of small amounts of recreational marijuana through medical marijuana dispensaries that began on October 1, 2015. The OLCC began accepting applications for growers, wholesalers, processors, and retail outlets on January 4, 2016.

3. Alaska.

Alaska passed Measure 2 on November 4, 2014, legalizing recreational use of cannabis by adults. Measure 2 went into effect 90 days later, on February 24, 2015, and regulations were issued governing retail licenses, zoning, what kind of products may be sold and to whom.[106]

The following is a summary of the law, which can be found in more detail on the Alaska Department of Commerce, Community and Economic Development, Alcohol & Marijuana Control Office web site at: https://www.commerce.alaska.gov/web/amco/MarijuanaFAQs.aspx.

a. Use. Like alcohol, adults 21 and over can possess, consume, and purchase products from a recreational marijuana store. All recreational products must be consumed in Alaska. There are limits as to how much you can possess at any one time. Growing your own marijuana plants for personal use, privately and away from public view in a secure place is legal for adults 21 and over. Property owners can ban the cultivation of marijuana on their property. Multiple people living in a single residence cannot combine personal-use plants and/or harvested marijuana limits to increase the amount of marijuana they can possess and cultivate in their residence. Any violation of the cultivation rules is subject to a fine.

[105] Colo. Rev. Stat. §12-43.4-306.

[106] Alaska Stat. ch. 17.37

b. Medical Marijuana. Medical marijuana has been legal in Alaska since 1998. Measure 2 does not affect the medical marijuana system. The possession rules are the same as those for recreational use. Measure 2 provides that "nothing in this chapter shall be construed to limit any privileges or rights of a medical marijuana patient or medical marijuana caregiver."[107]

c. Purchasing Marijuana. Licensed recreational stores are the only outlets that may sell marijuana in Alaska.

d. Consumption. It's legal to use cannabis products in Alaska on private property and outside the view of the general public. Marijuana may not be consumed in public[108], on federal land, and on some Indian reservations. An employer is under no obligation to accommodate even the medical use of marijuana in any workplace.[109]

Lieutenant Governor Byron Mallott released an emergency regulation defining "in public" as "a place to which the public or a substantial group of persons has access."[110] Consumption in a banned place may be fined.

e. Enforcement. Measure 2 specifically states it makes no changes to Alaska impaired driving laws, which already contained a provision for driving under the influence of an intoxicating substance.

f. Commercial Licenses. The State of Alaska Alcohol & Marijuana Control Office issues four types of licenses to approved parties, which include: (i) Marijuana cultivation facilities and growers, (ii) Marijuana product manufacturing facilities – the processors that turn plants into bud, extracts, and other cannabis products; (iii) Marijuana testing facilities – the testers who will make sure products meet quality control requirements, and (iv) Marijuana retail stores – the shops that will sell weed and cannabis products to adults 21 and over

g. Taxes

(1) Income Tax. Alaska's corporate income tax applies to the cannabis industry.

(2) Sales Tax. Alaska does not impose a general sales tax and no sales tax applies to cannabis.

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[107] Alaska Stat. 17.38.010(d).

[108] Alaska Stat. 17.38.040.

[109] Alaska Stat. ch. 17.38.

[110] Memorandum from the Office of Lieutenant Governor Alaska, Emergency Regulations re: definition of "in public" (3 AAC 304.990), Feb. 24, 2015 available at https://aws.state.ak.us/OnlinePublicNotices/Notices/Attachment.aspx?id=98820.

(3) Excise Tax. Alaska imposes an excise tax on the sale or transfer of marijuana from a marijuana cultivation facility to a retail marijuana store or marijuana product manufacturing facility. Alaska Stat § 43.61.010, 15 Alaska Admin Code § 61.100. Although certain parts of the marijuana plant are exempt from the excise tax or are subject to tax at a lower rate. Alaska § 43.61.010(b). The excise tax does not apply to the sale of medical marijuana.

4. Washington.

In 2012, voters in Washington approved I-502, an initiative amending state law to provide that the possession of small amounts of marijuana is not a violation of Washington law.[111] Under the initiative, individuals over the age of 21 may possess certain quantities of marijuana for private use. In addition to legalizing possession, the initiative provided that the "possession, delivery, distribution, and sale" by a validly licensed producer, processor, or retailer, in accordance with the regulatory scheme administered by the Washington State Liquor and Cannabis Board (formerly known as the Washington State Liquor Control Board) (WSLCB), is not a criminal or civil offense under Washington state law.[112]

The recreational use of marijuana is regulated and taxed in a manner similar to alcohol.[113] And, an employer is under no obligation to accommodate the medical use of marijuana in any place of employment. Additionally, an employer may terminate an employee based on a failed drug test even where employee is a qualifying patient engaged in only at-home use of medical marijuana.[114]

The initiative established a three-tier production, processing, and retail licensing system that permits the state to retain regulatory control over the commercial life cycle of marijuana. Qualified individuals must obtain a producer's license to grow or cultivate marijuana; a processor's license to process, package, and label the drug; or a retail license to sell marijuana to the general public.[115] The WSLCB adopted detailed rules for implementing the initiative, including marijuana license qualifications and an application process, application fees, marijuana packaging and labeling restrictions, recordkeeping and security requirements for marijuana facilities, and reasonable time, place, and manner advertising restrictions. By lottery, the WSLCB issued 334 retail licenses in 2014.

As an initial matter, the WSLCB may not issue a license to: (a) an individual under the age of 21 years; (b) a person doing business as a sole proprietor who has not lawfully resided in the state for at least three months prior to applying for a license; (c) a partnership, employee cooperative,

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[111] Washington Initiative 502 §20, *amending* RCW 69.50.4013 (July 8, 2011), *available at* http://sos.wa.gov/_assets/elections/initiatives/i502.pdf.

[112] *Id*. §4.

[113] RCW ch. 69.50.

[114] RCW ch. 69.51A.

[115] *Id*.

association, non-profit corporation, or corporation, unless it is formed under the laws of the state, and unless all of the members thereof are qualified to obtain a license; or (d) a person whose place of business is conducted by a manager or agent, unless the manager or agent possesses the same qualifications required of the licensee.[116] In addition, the WSLCB may conduct a criminal background information check, and consider any prior criminal conduct of the applicant, including an administrative violation history record with the WSLCB.[117]

Prior to the passage of I-502, a qualifying patient or designated provider could lawfully use, produce, possess, or administer marijuana to treat a terminal or debilitating illness. A qualifying patient or designated provider could not be arrested, prosecuted or subject to other criminal sanctions or civil consequences, for possession, manufacture, delivery, or possession with intent to manufacture or deliver, marijuana under state law. Qualifying patients could possess amounts of marijuana in various forms as specified under the statute. In 2015, Senate Bill 5052 brought medical marijuana under the system and rules of I-502.[118]

5. Transfer of Ownership.

Generally, states limit ownership of retail licenses based on age, residency, and criminal history. For example, Washington requires approval from the WSLCB for a transfer to anyone other than a surviving spouse.[119] To date, no state anticipates ownership of a license by a trust, nor is there guidance for a fiduciary that may be tasked with managing a marijuana license.

Each state's procedures to transfer ownership are different but the goal is the same: to ensure that the transferee is qualified to hold a license.

In Oregon, for example, two rules, in particular, must be followed:

- OAR 845-025-1160(4) provides that "[a] licensee that proposes to change its corporate structure, ownership structure or change who has a financial interest in the business must submit a form prescribed by the Commission… prior to making such a change."

- OAR 845-025-1160(4)(d) provides that "[i]f a licensee has a change in ownership that is 51% or greater, a new application must be submitted in accordance with OAR 845-025-1030.

Presumably the death of the holder of a license and the appointment of a personal representative or Trustee would be considered a 51% or greater change in ownership. Whether the new applicant is the fiduciary or the beneficiary (if that can even be established immediately following the death of a license holder), a new license must be applied for and issued. In light of these strict rules, it

[116] RCW 69.50.331.

[117] *Id*.

[118] Adopts a comprehensive act that uses the regulations in place for the recreational market to provide regulation for the medical use of marijuana.

[119] RCW 69.50.339.

may be a good business practice to make sure that an entity is structured so that no single owner has more than a 51% interest. Other states have similar statutes that must be carefully followed.

D. The Ogden and Durkin Memos.

From 2009 to 2011, the DOJ issued guidance related to the legalization of medical marijuana. The policy of the DOJ in that guidance was an intent to pursue any commercial enterprise selling or producing marijuana.

On October 19, 2009, Deputy Attorney General David W. Ogden issued a memorandum (the "Ogden Memo") to select United States Attorneys to "provide[] clarification and guidance to federal prosecutors in States that have enacted laws authorizing the medical use of marijuana."[120] According to the Ogden Memo, the DOJ remained "committed to the enforcement of the [CSA] in all States."[121] However, given the DOJ's "limited investigative and prosecutorial resources," the Ogden Memo advised U.S. Attorneys to focus on prosecuting "significant marijuana traffickers" and disrupting "illegal drug manufacturing and trafficking networks," rather than "on individuals whose actions are in clear and unambiguous compliance with existing state laws providing for the medical use of marijuana," particularly seriously ill individuals who use marijuana as part of a medically recommended treatment regimen, or their caregivers.[122]

Then, on April 14, 2011, U.S. Attorney Jenny A. Durkan of the Western District of Washington and the U.S. Attorney Michael C. Ormsby of the Eastern District of Washington issued guidance (the "Durkan Statement") to Washington State Governor Christine Gregoire.[123] The Durkan Statement was issued in response to a letter from Governor Gregoire seeking guidance on pending legislation establishing a licensing scheme for medical marijuana growers, dispensers, and processors. The Durkan Statement advised Governor Gregoire that the proposed licensing scheme would "permit[] large-scale marijuana cultivation and distribution," "conduct [that is] contrary to federal law."[124] Accordingly, the DOJ could consider civil and criminal legal remedies against marijuana growers and dispensers; others who knowingly facilitate their actions, "including property owners, landlords, and financiers"; and "state employees who conducted activities mandated by the Washington legislative proposals."[125]

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[120] Deputy Attorney General David W. Ogden, U.S. Department of Justice, Memorandum for Selected United States Attorneys on Investigations and Prosecutions in States Authorizing the Medical Use of Marijuana (Oct. 19, 2009), https://www.justice.gov/sites/default/files/opa/legacy/2009/10/19/medical-marijuana.pdf.

[121] *Id.* at 1.

[122] *Id.* at 1-2.

[123] Letter from United States Attorney Jenny A. Durkan and United States Attorney Michael C. Ormsby to Governor Christine Gregoire (Apr. 14, 2011), https://reason.com/assets/db/13050453232855.pdf.

[124] *Id.* at 2.

[125] *Id.*

E. Cole Memoranda.

In light of the developments at the state level, U.S. Department of Justice Deputy Attorney General James Cole issued a memorandum that expresses the DOJ's position that, although marijuana is a dangerous drug that remains illegal under federal law, the federal government will not pursue legal challenges against jurisdictions that authorize marijuana in some fashion, assuming those state and local governments maintain strict regulatory and enforcement controls on marijuana cultivation, distribution, sale, and possession that limit the risks to "public safety, public health, and other law enforcement interests."[126]

Then, on August 2013 (Cole II Memo), expanding on the Cole I memo, to all U.S. Attorneys that provides guidance to federal prosecutors concerning marijuana enforcement under the CSA. [127] The Cole II Memo guidance applies to all of the Department of Justice's federal enforcement activity, including civil enforcement and criminal investigations and prosecutions, concerning marijuana in all states. It makes clear that the Ogden Memo was never intended to shield large-scale commercial cultivation, sale, distribution, and use of marijuana "for purported medical purposes" from federal enforcement action and prosecution.[128] Cole I also advised that "[t]hose who engage in transactions involving the proceeds of such activity may also be in violation of federal money laundering statutes and other federal financial laws."[129]

The Cole II Memo instructs federal prosecutors to prioritize their "limited investigative and prosecutorial resources to address the most significant [marijuana-related] threats"[130] and identified the following eight activities as those that the federal government wants most to prevent:

1. Distributing marijuana to children;

2. Revenue from the sale of marijuana going to criminal enterprises, gangs, and cartels;

3. Diverting marijuana from states that have legalized its possession to other states that prohibit it;

4. Using state-authorized marijuana activity as a pretext for the trafficking of other illegal drugs;

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[126] James M. Cole, Deputy Attorney General, *Memorandum for All U.S. Attorneys, Guidance Regarding Marijuana Enforcement* (Aug. 29, 2013), *available at* http://www.justice.gov/iso/opa/resources/305201382913275685746 7.pdf.

[127] James M. Cole, Deputy Attorney General, Memorandum for All U.S. Attorneys, *Guidance Regarding the Ogden Memo in Jurisdictions Seeking to Authorize Marijuana for Medical Use* (June 29, 2011), *available at* http://www.drugpolicy.org/sites/default/files/DOJ_Guidance_on_Medicinal_Marijuana_1.pdf.

[128] *Id.* at 1-2.

[129] *Id.* at 2.

[130] *Id*. at 1.

5. Using firearms or violent behavior in the cultivation and distribution of marijuana;

6. Exacerbating adverse public health and safety consequences due to marijuana use, including driving while under the influence of marijuana;

7. Growing marijuana on the nation's public lands; and

8. Possessing or using marijuana on federal property.[131]

The memorandum advises U.S. Attorneys and federal law enforcement to devote their resources and efforts toward any individual or organization involved in any of these activities, regardless of state law. Furthermore, the memorandum recommends that jurisdictions that have legalized some form of marijuana activity "provide the necessary resources and demonstrate the willingness to enforce their laws and regulations in a manner that ensures they do not undermine federal enforcement priorities."[132] However, the memorandum cautions that, to the extent that state enforcement efforts fail to sufficiently protect against the eight harms listed above, the federal government retains the right to challenge those states' marijuana laws.

In December 2014, President Obama signed the Consolidated and Further Continuing Appropriations Act of 2015. Section 538 of that law states that: "None of the funds made available in this Act to the [DOJ] may be used, with respect to the [medical marijuana states], to prevent such States from implementing their own State laws that authorize the use, distribution, possession, or cultivation of medical marijuana."[133]

Nearly identical language was also included in the Consolidated Appropriations Act of 2016.[134]

Then, on February 27, 2015, Patty Merkamp Stemler, Chief of the DOJ's Appellate Section, issued a memorandum to all federal prosecutors, explaining that Section 538 applied only to states, rather than individuals, and therefore, "the [DOJ's] position is that Section 538 does not bar the use of funds to enforce the CSA's criminal prohibitions or to take civil enforcement and forfeiture actions against private individuals or entities consistent with the Department's guidance regarding marijuana enforcement."[135]

More recently, in *United States v. Marin Alliance for Medical Marijuana* (MAMM),[136] the U.S. District Court for the Northern District of California held that the Department of Justice's permanent injunction against MAMM's distribution of marijuana in violation of the CSA could

[131] *Id*. at 1-2.

[132] *Id.* at 2-3.

[133] Pub. L. No. 113-235 § 538, 128 Stat. 2130, 2217 (2014).

[134] *See* Pub. L. No. 114-113 § 542, 129 Stat. 2242 (2015).

[135] Chief Patty Merkamp Stemler, U.S. Department of Justice, Criminal Division, Appellate Section, Memorandum For All Federal Prosecutors on Guidance Regarding the Effect of Section 538 of the Consolidated and Further Continuing Appropriations Act of 2015 on Prosecutions and Civil Enforcement and Forfeiture Actions Under the Controlled Substances Act at 2 (Feb. 27, 2015), https://www.scribd.com/doc/273620932/Depart-of-Justice-Says-Medical-Marijuana-Law-Doesn-t-Impact-Prosecutions.

[136] No. C 98-00086 CRB (N.D. Cal. Oct. 19, 2015).

only be enforced against MAMM to the extent it was in violation of state law concerning the use, distribution, possession, or cultivation of medical marijuana. While this is a medical marijuana case, it highlights the move toward ending federal government interference in marijuana-related activities that are legal under state law.

Because of the relaxed laws regarding cannabis, Colorado, Oregon and Alaska, which permit personal use, have become destinations for cannabis tourism. Notwithstanding the federal guidance to the DOJ not to pursue cannabis activities permitted under state law, that guidance is non-binding and provides "prosecutorial discretion." This puts non-U.S. citizens at great risk. Those arriving at our borders may be asked by Customs and Border Protection if they have used marijuana. A "yes" answer, or any evidence to that effect, could lead to being "inadmissible" to the U.S., potentially for life. Similarly, those arriving by boat or cruise ship will be questioned by the Coast Guard, which enforces federal law, not the law of any state. Non-citizens, whether on vacation or here holding a green card or visa, as well as refugees and those granted asylum, need to think long and hard about whether using a state-permitted substance is worth the possibility that the federal government will assert its prosecutorial powers.

F. Treasury Department Guidance.

In addition to the guidance issued by the Department of Justice, the Financial Crimes Enforcement Network (FinCEN), a division of the Treasury Department, issued its own guidance in 2014 to clarify Bank Secrecy Act (BSA) expectations for financial institutions seeking to provide services to marijuana-related businesses in light of state initiatives to legalize certain marijuana-related activity.[137]

The FinCEN guidance points out that the decision to open, close, or refuse any particular account or relationship should be made by each financial institution based on a number of factors specific to that institution. These factors may include its particular business objectives, an evaluation of the risks associated with offering a particular product or service, and its capacity to manage those risks effectively. Thorough customer due diligence is a critical aspect of making this assessment. In assessing the risk of providing services to a marijuana-related business, a financial institution is obligated to conduct customer due diligence that includes:

1. Verifying with the appropriate state authorities whether the business is duly licensed and registered;

2. Reviewing the license application (and related documentation) submitted by the business for obtaining a state license to operate its marijuana-related business;

3. Requesting from state licensing and enforcement authorities available information about the business and related parties;

[137] FinCEN, BSA Expectations Regarding Marijuana-Related Businesses (Feb. 14, 2014), *available at* http://www.fincen.gov/statutes_regs/guidance/html/FIN-2014-G001.html.

4. Developing an understanding of the normal and expected activity for the business, including the types of products to be sold and the type[s] of customers to be served (e.g., medical versus recreational customers);

5. Ongoing monitoring of publicly available sources for adverse information about the business and related parties;

6. Ongoing monitoring for suspicious activity, including for any of the red flags described in this guidance; and

7. Refreshing information obtained as part of customer due diligence on a periodic basis and commensurate with the risk.[138]

In addition, under the FinCEN guidance, a financial institution that decides to provide financial services to a marijuana-related business would be required to file a Suspicious Activity Report if the financial institution knows, suspects, or has reason to suspect that a transaction involves funds derived from a marijuana-related business.

G. Enforcement Guidelines Regarding Marijuana Under the Trump Administration

Finally, based on recent statements from current White House press secretary Sean Spicer, there is an indication that under the Trump administration, the DOJ will do more to enforce federal marijuana laws. However, despite this statement from Spicer, recent news articles [139]note that Attorney General Jeff Sessions has privately reassured some Republican senators that he will not deviate from the current policy of allowing states to implement their own marijuana laws or retract the existing Ogden Memo and Cole Memo regarding enforcement priorities.

H. Cannabis in the Estate Plan.

As the stigma around marijuana diminishes and the legal and regulatory environments evolve, estate planners will likely be in the position of advising clients with marijuana-related assets. The laws governing the transfer of assets by a decedent are those of the decedent's domicile prior to death. But the law of the beneficiary's domicile will apply to determine whether or not he or she may take possession.

Once it is established that a testamentary instrument may legally transfer ownership the next step will be to determine whether the beneficiary may take ownership.

At the drafting stage, testators and grantors often wish to limit gifts based on certain conditions, one of which is often the use of illegal drugs. Drafters will now need to carefully specify when the restriction applies, what law applies (if state, then which one, or federal), and whether marijuana is included as an illegal drug. One option would be to refer instead to "mind altering

[138] *Id*.

[139] http://www.politico.com/story/2017/03/jeff-sessions-marijuana-crackdown-senators-react-235616.

drugs, whether legal or illegal." The following is an example of a clause making distributions conditional on drug use:

> Suspension of Distributions. If the trustee at any time suspects that a beneficiary is using any substance (including, without limitation, drugs, chemicals or alcohol) in an abusive manner or is engaging in any abusive addictive behavior, the trustee is authorized to request that the beneficiary submit to one or more examinations determined to be appropriate by a licensed and practicing physician, psychiatrist or other appropriate health care professional selected by the trustee. The trustee may request the beneficiary to consent to full disclosure by the examining doctor or facility to the trustee of the results of all such examinations, and the trustee may totally or partially suspend or withhold all distributions until the beneficiary consents to one or more examinations and disclosure to the trustee, and those examinations indicate no such use or behavior.

When an estate or trust includes a retail, processor, or producer marijuana license, a named fiduciary first must determine whether he, she, or it is willing to serve, given marijuana's status as a Schedule I controlled substance under the CSA. While an individual may be comfortable relying on the enforcement priorities outlined in the Cole II Memo, it is likely that a named corporate fiduciary will decline its appointment when the trust or estate includes a marijuana license. In addition, given the FinCEN guidance, described above, a fiduciary should consider whether a financial institution will work with a trust or estate that even includes property related to or derived from the production or sale of marijuana.

If a fiduciary agrees to serve and is qualified to do so, he or she must then determine whether trust, estate, and named beneficiaries are eligible to own licenses based on state law. Both Washington and Colorado impose age, residency, and criminal history requirements on license ownership.[140] It is unclear how those requirements will be interpreted if a trust or estate becomes the owner of a license. The fiduciary will need to work with the state or local licensing authority to determine whether the trust or estate is eligible for a license.

What can be done during the estate planning process to diminish the risks associated with post-death transfers? Individuals who own marijuana licenses or interests in entities that own such licenses should carefully consider business succession planning strategies, to avoid transfers to individuals not qualified to become owners.

When a marijuana business is owned by two or more unrelated entities, the owners should investigate cross-purchase plans, buy-sell agreements, or entity purchase plans. Through careful planning, individuals may be able to avoid some of the more difficult issues related to the transfer of marijuana licenses.

The testamentary instrument transferring any interest in cannabis (or any other highly regulated asset) should consider allowing the fiduciary to appoint an independent fiduciary to carry out those

[140] RCW 69.50.331; Colo. Rev. Stat. §12-43.4-306.

duties the appointing fiduciary may not. The following is a provision identifying only a partial list of tasks for an independent trustee:

> Independent Trustee – Special Powers. In addition to all other powers as Trustee, an independent trustee shall have the following powers and authority: (i) to amend the trust as the independent trustee deems necessary to carry out my intent in establishing the trust or to otherwise allow the trust to be administered in a more administrative or tax efficient manner given current or future federal or state laws; provided that any amendment may not affect the beneficial enjoyment of the trust estate; (ii) in general, to avail the trust and beneficiaries of opportunities under existing and future laws that may require extraordinary action such as, but not limited to: division of trusts into separate shares, creation of new trusts for the purposes of holding specific property or interests, limiting distributions from a new trust to an ascertainable standard or to permissible recipients, and (iii) to deal with any regulated assets that a fiduciary is not able to administer because of state law or other circumstances, which prevent such fiduciary from administering such assets. All actions taken by an independent trustee hereunder should be consistent with, though not necessarily in literal compliance with, the dispositive scheme of the trust. An independent trustee shall be under no duty to exercise any power granted under this section and shall be held harmless and indemnified against any liability, claim, judgment, expense or cost arising from or attributable to his or her exercise or failure to exercise any power granted under this section, except as provided in [section re trustee standard of care].

Finally, delivery of a cannabis-related asset to a beneficiary by a fiduciary needs to be considered. As a Schedule 1 drug, it may not be sent using the U.S. Postal Service.[141] The most lenient penalty for violation of 18 U.S.C. 1716 is 5 years in a federal penitentiary, increasing from there.[142]

I. Federal Income and Estate Tax Considerations.

Because marijuana remains illegal under federal law, few business deductions are allowed on federal tax returns, and the gross revenue is taxable.[143] Although beyond the scope of this outline, in some instances, the cost of goods sold (costs incurred for the purchase, conversion, materials, labor, and allocated overhead incurred in bringing the marijuana inventories to their present

[141] 18 U.S.C. 1716.

[142] https://www.dea.gov/druginfo/ftp3.shtml.

[143] I.R.C. §280E, enacted as part of the Tax Equity and Fiscal Responsibility Act of 1982. IRC § 280E provides that:

> No deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any State in which such trade or business is conducted.

location and condition) may be deductible under Code §280E,[144] but the ordinary and necessary expenses related to sale are not.

At death, it is important to keep in mind that even illegal property has a value. The IRS has held that the fact that a market is illicit does not obviate the existence of that market for estate tax valuation purposes.[145]

To make matters more complicated, under the Electronic Federal Tax Payment System, since January 11, 2011, tax payments may not be made in cash.[146] A 10% penalty may be imposed for each cash payment, although exceptions may be made for certain taxpayers unable to obtain bank accounts.[147]

J. Leasing Issues.

While leasing issues are seemingly beyond the scope of estate planning, many of our clients make their fortunes in real estate. Some will be tempted to branch out into leasing to the cannabis industry. And some of those leases will be left behind to be handled by a fiduciary and heirs. The following are a few tips when dealing with cannabis-related leases.

The rent must not be connected in any way to the success or failure of the cannabis business. A landlord may not have any ownership interest in the underlying business, which would include a percentage of profits.

The timeline for starting a cannabis venture is slightly different from other conventional businesses. It begins with an initial application submission. Assuming that is accepted, documents including the lease, the operating plan, and the site plan must be submitted for approval. Following that, there is a build out and a final inspection, and *then* a license may or may not be issued. At each point on this timeline, a lessor may want to retain the right to terminate the lease, receive partial payments, and enter the premises.

A lease should include a number of escape clauses, including the right for the landlord to terminate upon a change in the law, a federal forfeiture action, or a foreclosure or call on the lessee's financing. In addition, at a minimum, a landlord should require a bond to cover business interruption.

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[144] Jeffrey Gramlich, Ph.D., & Kimberly Houser, *Marijuana Business and Sec. 280E: Potential Pitfalls for Clients and Advisers*, The Tax Adviser (June 30, 2015), *available at* http://www.thetaxadviser.com/issues/2015/jul/houser-jul15.html.

[145] *Jones v. Comm'r*, T.C. Memo. 1991-28 (Jan. 24, 1991) (the street market of illicit drugs was the relevant market for 42 kilograms. of cocaine); *Browning v. Comm'r*, T.C. Memo. 1991-93 (Mar. 4, 1991) (the fair market value of marijuana based on the wholesale street market value).

[146] Treas. Reg. §31.6302-1(h)(3).

[147] IRM 20.1.4.2.

While lessees of real property are not subject to the same strict regulations that apply to producers, retailers, and processors, they can unwittingly get caught up in their tenants' misdeeds or in the conflict between federal and state law. For example, a landlord in Oakland, California leased a portion of commercial real estate to a medical marijuana dispensary. The U.S. Attorney filed a civil *in rem* forfeiture action against the property, seeking to shut down the dispensary. After receiving notice of the action, the landlord attempted to evict the dispensary, but when the dispensary declined to stop its operations, a California state court refused to allow the eviction, and the forfeiture action proceeded. The City of Oakland attempted to prevent the forfeiture by bringing a collateral suit, but the Ninth Circuit rejected its claim, thereby allowing the forfeiture action to continue.[148] If a lessee is involved in criminal activity, the land may be held as evidence during an investigation.

Finally, a tenant should also be given the right to terminate a lease due to a change in the law or a license application denial after the lease commencement date.

In any legal document involving cannabis, whether a lease or other type of contract, the forum selection clause should provide that any litigation must take place in state court so long as there is a concern over the conflict between state and federal interpretation of applicable law.

K. Intellectual Property Issues.

Only in the past few years have plant growers, breeders, and individuals who have for decades worked in the shadows, been able to work in a legitimate industry. Major innovation is occurring in the marijuana industry, and naturally, patents, trademarks, copyrights, and trade secrets will be assets of our clients or their businesses.[149] As a matter of policy, the U.S. Patent and Trademark Office refuses to issue trademarks to cannabis products. Courts have held that use of a trademark can create rights only when the use is lawful and that it is illogical to extend government benefit to a seller based on the seller's actions in violation of law.[150] However, in states where marijuana has been legalized, state registration may be possible and would give the right to sue under state law.[151] But enforcement under federal law is not an option because there can be no federal trademark to enforce.

Fiduciaries will need to consider the intellectual property implications of any marijuana-related asset of a trust or estate. Fiduciaries should also be aware of possible trademark infringement litigation. For example, in 2014, the Hershey Company sued Conscious Care Cooperative, a

[148] *City of Oakland v. Lynch*, 798 F.3d 1159 (9th Cir. 2015).

[149] *See* Lisa Schuchman, *Roll Another Patent (for the Road)*, Corporate Counsel, ALM Media Properties, LLC (April 1, 2015), available at: https://www.cooley.com/files/cooley-corporate-counsel-cannibas-industry.pdf.

[150] *CreAgri, Inc. v. USANA Health Scis., Inc.*, 474 F.3d 626 (9th Cir. 2007); *see also United Phosphorus, Ltd. v. Midland Fumigant, Inc.*, 205 F.3d 1219 (10th Cir. 2000).

[151] *See, e.g.*, Or. Rev. Stat. §647.095.

Washington medical marijuana dispensary, alleging that the retailer sold infringing products such as "Reefer's Peanut Butter Cups" and "Mr. Dankbar."[152]

L. Ethical Considerations.

Because of the ever-changing legal landscape around state-licensed marijuana regulation, it is critical for investors, producers, processors, retailers, and other stakeholders within the legal marijuana industry to understand how to comply. However, this presents obvious ethical challenges for lawyers seeking to represent the interests of marijuana industry members or fiduciaries who must administer property derived from the marijuana industry. Despite efforts of several states to legalize the production, distribution, and use of marijuana, a lawyer must consider whether he or she may ethically advise and assist a client seeking to engage in conduct that the lawyer knows is criminal or fraudulent (in one or more states).

Several state bar associations have issued guidance where an attorney sought to assist clients with complying with state medical marijuana laws. Those states each arrived at different outcomes:

1. Arizona. In 2011, the State Bar of Arizona reached the opposite conclusion. The opinion declined to read Arizona Ethics Rule 1.2 to forbid attorney assistance regarding conduct prohibited by the CSA yet compliant with state law. To do so, the bar reasoned, would "depriv[e] clients of the very legal advice and assistance that is needed to engage in the conduct that the state law expressly permits." The bar advised that an attorney could ethically perform legal services related to the state's Medical Marijuana Act so long as (i) the conduct was expressly permitted under the Act, (ii) the lawyer advised the client on potential federal law implications and consequences, and (iii) the client, having received full disclosure, elected to proceed with a course of action specifically permitted by the Act. The State Bar of Arizona recognized that disciplining attorneys for working within a complex regulatory system would deprive the state's citizens of legal services "necessary or desirable to implement and bring to fruition that conduct expressly permitted under state law."[153]

2. Connecticut. In 2013, the Connecticut Bar Association Professional Ethics Committee reached a similar conclusion to that of the Maine Professional Ethics Commission: while an attorney could safely advise a client on the requirements of state and federal marijuana law, advice and services in aid of functioning marijuana enterprises could run afoul of RPC 1.2(d).[154] They advised lawyers to "carefully assess" the distinction between consultation and explanation versus participating in criminal enterprises.

3. Colorado. In 2014, the Colorado Supreme Court adopted a comment to the state's RPCs regarding the provision of legal services to state-regulated medical and recreational

[152] Complaint, *Hershey Co. v. Conscious Care Coop.*, No. 2:14-cv-00815 (W.D. Wash. 2014).

[153] *See* State Bar of Arizona Ethics Opinions (Feb. 2011), *available at* http://www.azbar.org/Ethics/EthicsOpinions/ViewEthicsOpinion?id=710.

[154] Informal Opinion 2013-02, January 16, 2013.

marijuana businesses. The comment to RPC 1.2 regarding the scope of representation and allocation of authority between the client and the lawyer now states:

> A lawyer may counsel a client regarding the validity, scope, and meaning of Colorado Constitution article XVIII, secs. 14 & 16, and may assist a client in conduct that the lawyer reasonably believes is permitted by these constitutional provisions and the statutes, regulations, orders, and other state or local provisions implementing them. In these circumstances, the lawyer shall also advise the client regarding related federal law and policy.[155]

Previously, the Colorado RPCs had prohibited attorneys from aiding clients "in conduct that the lawyer knows is criminal." Despite the fact that medical and recreational use of marijuana is legal within the state, lawyers were left at an impasse because the production, use, sale, and distribution of the drug are still illegal under federal law. Based on this prior rule, a Colorado lawyer providing anything more than basic legal advice to marijuana businesses could run afoul of ethical obligations and face disciplinary action. The comment provides a safe harbor for lawyers seeking to represent those engaged in the legal marijuana industry within Colorado.

4. Illinois. The Illinois Rules of Professional Conduct permit lawyers to counsel clients on activities permitted in Illinois that may violate federal law, so long as the lawyer counsels the client on the potential consequences :

> A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may (1) discuss the legal consequences of any proposed course of conduct with a client, (2) counsel or assist a client to make a good-faith effort to determine the validity, scope, meaning or application of the law, and (3) counsel or assist a client in conduct expressly permitted by Illinois law that may violate or conflict with federal or other law, as long as the lawyer advises the client about that federal or other law and its potential consequences.[156]

5. Maine. The Maine Professional Ethics Commission concluded in 2010 that representing or advising clients under Maine's Medical Marijuana Act would "involv[e] a significant degree of risk which needs to be carefully evaluated."[157] The Commission recognized that the federal government had deprioritized enforcement of the CSA in medical marijuana cases, but reasoned that Maine's rule governing attorney conduct "does not make a distinction between crimes which are enforced and those which are not."[158] As long as the

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[155] Colo. RPC 1.2 (2015). [Comment [14] added and effective Mar. 24, 2014.]

[156] Ill. PR Rule 1.2(d)(3) [Adopted July 1, 2009, eff. Jan. 1, 2010; amended Oct. 15, 2015, eff. Jan. 1, 2016]. See also Ill. State Bar Ethics Op. 14-07 (Oct. 2014).

[157] Maine Prof'l Ethics Comm'n, Op. 199 (July 7, 2010).

[158] *Id*.

federal law and Maine's Rules of Professional Conduct (RPCs) remain unchanged, attorneys need to determine "whether the particular legal service being requested rises to the level of assistance in violating federal law."[159] If so, the attorney risks violating RPC 1.2.

6. Oregon. In 2015 the Oregon Supreme Court adopted RPC 1.2(d), which states:

> Notwithstanding paragraph (c), a lawyer may counsel and assist a client regarding Oregon's marijuana-related laws. In the event Oregon law conflicts with federal or tribal law, the lawyer shall also advise the client regarding related federal and tribal law and policy.[160]

While the rule does not require a lawyer to provide advice regarding the intricacies of federal and tribal law, a lawyer will need to be familiar with those areas in order to spot issues and adequately advise his or her clients about those conflicts.

7. Washington. In 2014, the Washington Supreme Court adopted a comment to the Washington State RPCs regarding the provision of legal services to cannabis businesses. The comment to RPC 1.2 states:

> At least until there is a change in federal enforcement policy, a lawyer may counsel a client regarding the validity, scope and meaning of Washington Initiative 502 (Laws of 2013, ch. 3) and may assist a client in conduct that the lawyer reasonably believes is permitted by this statute and the other statutes, regulations, orders, and other state and local provisions implementing them.[161]

In addition, in June of 2015, the Washington State Bar Association issued Advisory Opinion 201501, which asked and answered five specific questions regarding the provision of legal services in the legal marijuana industry within Washington.[162] The questions are as follows:

> 1. May Lawyer A advise Client A about the interpretation of and compliance with I-502 and the Cannabis Patient Protection Act (the "CPPA"), without violating the Washington Rules of Professional Conduct (the "RPCs")?
>
> 2. May Lawyer B provide legal advice and assistance to Client B in the formation and operation of a business entity so as to

[159] *Id*.

[160] Or. RPC 1.2(d) (2015).

[161] Wash. RPC 1.2 (2015). [Comment [18] added and effective Dec. 9, 2014.]

[162] *See* Washington State Bar Association Advisory Opinion 201501 (2015), *available at* http://mcle.mywsba.org/IO/print.aspx?ID=1682.

comply with I-502 and the CPPA without violating the RPCs?

3. May Lawyer C own and operate an independent business in compliance with I-502 and the CPPA without violating the RPCs?

4. Assuming that Lawyer D's need for and consumption of medical or retail marijuana do not otherwise affect Lawyer D's substantive competence or fitness to practice as a lawyer, may Lawyer D purchase and consume marijuana in compliance with I-502 and the CPPA without violating the RPCs?

5. May Lawyer E engage in the implementation of I-502 [and] the CPPA and, if Lawyer E's competence and fitness to practice as a lawyer is not affected, purchase marijuana subject to I-502 and the CPPA without violating the RPCs?

The Advisory Opinion concludes that the answer to each question is "Yes, qualified," and provides an analysis of each of the five issues with the qualification that "if the federal government changes its position and again seeks to enforce the CSA against the kinds of activities made lawful under I-502 and the CPPA as a matter of state law, the application of the RPCs may have to be reconsidered."[163]

M. Engagement Letters.

In states where an attorney may advise a client on cannabis-related activities, it is not sufficient to use a standard engagement letter. In addition to a criminal background check to be certain that the client may engage in such business activities, it would be prudent, in the attorney's engagement letter to disclose to the potential client that because cannabis is illegal under federal law, if the federal law were to enforce the CSA against activities otherwise lawful under state law, the terms of representation would have to be revisited and representation may have to be terminated.

The following is a sample of such disclosure:

> [Law Firm] advises clients on state laws governing the business of cannabis to facilitate compliance with those state laws. Federal laws concerning cannabis currently conflict with state laws in states that have legalized cannabis or possession of cannabis. Although federal enforcement policy may at times defer to these states' laws and not enforce conflicting federal laws, interested businesses and individuals should be aware that compliance with state law in no way assures compliance with federal law. There remains a risk that conflicting federal laws may be enforced in the future.

[163] *Id*.

Attached as Exhibit B is a form of engagement letter that may be adapted, based on applicable state law, when representing cannabis industry service providers.

While the majority of states (and D.C.) have legalized marijuana in some form, marijuana use, possession, production, distribution, and marketing remain illegal under federal law. The 2013 Cole Memo, which is only a policy statement, suggests that the federal government is uninterested in overturning state laws legalizing marijuana or prosecuting individuals and businesses unless their conduct implicates one of the listed enforcement priorities. However, the DOJ policy is evolving. And under a different administration or Attorney General, the DOJ policy could be reversed entirely. Therefore, marijuana users and businesses remain at risk of civil and criminal prosecution by the DOJ.

VIII. CONCLUSION

While many practitioners will go an entire career without running into certain regulated assets, chances are that one or two will pop up now and then. This outline is intended to provide a starting point for ways of dealing with just a few: pets, aircraft, wine, guns, and cannabis. Unless the practitioner asks about the existence of these assets, their existence may never even be disclosed. Therefore, it is important to ask questions about whether these assets exist and whether the named fiduciaries and beneficiaries are qualified to own them. Without this inquiry, both the fiduciary and the fiduciary's advisor may encounter additional and otherwise avoidable complexities as a result of the strict regulations in place.

EXHIBIT A
PET TRUST

I leave [description of pet animal] and [amount of money adequate for animal's care and trust administration expenses] to the trustee, in trust, under the terms of the [name of trust] created under Article [____] of this Will below. If [animal] does not survive me by [survival period], this provision of my Will shall lapse and be of no effect. [Modify for multiple animals.]

ARTICLE [___]
[NAME OF ANIMAL] TRUST

A. Beneficiary of Trust. This trust is for the sole benefit of [animal] during [animal's] lifetime, pursuant to RCW ch. 11.118.

B. Trustees. I appoint [primary trustee] as Trustee of this trust. If [primary trustee] is unwilling or unable to serve, I appoint [alternate trustee] as successor trustee. A Trustee shall serve as such, provided [trustee] receives [name of animal] into [his] [her] home and provides [animal] with proper care as defined in Section ___ of this Article. My Personal Representative shall deliver [animal] into [Trustee's] possession after securing a written promise from [trustee] to provide [animal] with proper care. If [Trustee] (1) dies, (2) is unable to provide [animal] with proper care, or (3) is not providing [animal] with proper care, I appoint [alternate trustee] to serve as successor trustee of this trust provided [alternate trustee] receives [name of animal] into [his/her] home and provides [animal] with proper care. [Continue in like manner for additional alternates]. If there is no qualified alternate trustee, [allow the Trustee to select successor].

C. Bond. No bond shall be required of any trustee named in this Article.

D. Trustee Compensation. The trustee shall be entitled to reasonable compensation from the trust for serving as trustee. [or] No trustee shall be entitled to compensation for serving as trustee.

E. Proper Care. Proper Care means [description of care including, for example, requirement of regular visits to a veterinarian].

F. Distribution of Trust Property While [Animal] is Alive. The trustee shall use trust property for all reasonable expenses incurred by [trustee] in the Proper Care of [animal] as defined in Section (E) of this Article ___. Reasonable expenses include, but are not limited to, [food, housing, grooming, medical care, and burial or cremation fees.]

G. Termination of Trust. This trust shall terminate upon the death of [animal].

H. Distribution of Property Upon Trust Termination. Upon the termination of this trust all remaining trust property shall pass to [remainder beneficiary] if [he/she] is alive at the time of trust termination. If [remainder beneficiary] is not alive at the time of trust termination, all remaining trust property shall pass to [alternate remainder beneficiary] if [he/she] is alive at the time of trust termination. [Continue in like manner for additional alternates]

I. Trustee Powers. The trustee shall have all powers granted to trustees under Washington law. [or] The trustee shall have the following powers: [enumerate trustee powers].

J. Exculpatory Clause. The trustee shall not be liable for any loss, cost, damage, or expense sustained through any error of judgment or in any other manner except for and as a result of a trustee's own bad faith or gross negligence.

Note: The pet owner should consider naming several alternate trustees, in the event the first choice is unable to serve for the duration of the pet's life. To prevent the pet from ending up homeless, the owner may consider authorizing the trustee to name further successors, or the personal representative to name successors, should none of the named individuals be willing and able to care for the pet. The more unusual the pet, the more important this becomes.

EXHIBIT B[164]
Cannabis Engagement Letter: Client is Service Provider to Cannabis Industry

Dear _____:

Thank you for engaging LAW FIRM to provide the legal services described below to _____ (the "Company"). I am writing to confirm this representation and to indicate how our services will be provided.

Scope of Representation

Our client in this engagement will be the Company. We have discussed the firm's capabilities to assist the Company with regard to _____. As an initial matter, you have asked us to {itemize tasks we are current undertaking – e.g., prepare a form of lease to use with tenants intending to grow marijuana on the Company's property}. The terms described in this letter will also apply to such other engagements as you specifically request and we agree to undertake on behalf of the Company and/or its affiliates.

The Company will not produce, process, or sell marijuana, but it will do business with companies engaged in one or more of those activities. Doing business in this sector of the economy presents some risks, as discussed below.

Potential Risks under Federal Criminal Law

Although the Company will not produce, process or distribute marijuana, and although some states have decriminalized such activity if it complies with their statutes and implementing regulations, you should be cognizant of potential risks under federal criminal law.

The Company will do business with individuals or entities whose conduct will be illegal under one or more federal statutes, even if their conduct fully complies with state law. Consequently, the Company and its owners and management face potential risks. For example, the federal government can seize, and seek the civil forfeiture of, real or personal property used to facilitate sales of marijuana as well as money or other proceeds from such sales. In addition, there is potential risk of criminal investigation or prosecution for aiding and abetting violation of federal law or for conspiring to violate federal law. A conviction on a conspiracy charge carries a mandatory minimum prison term of five years for a first offense and, depending on the quantity of marijuana involved, a fine for such a conviction could be as high as $10 million.

Although the U.S. Department of Justice has noted that an effective state regulatory system and a marijuana operation's compliance with such a system should be considered in the exercise of investigative and prosecutorial discretion, its authority to prosecute violations of federal law is

[164] The author gratefully acknowledges Scott Warner of Garvey Schubert Barer for allowing the adaptation of their materials for this outline.

in no way diminished by recent changes in the laws of some states. Indeed, due to the federal government's jurisdiction over interstate commerce, when businesses provide services to marijuana producers, processors or distributors located in multiple states, they potentially face a higher level of scrutiny from federal authorities than do their customers with local operations.

Terms of Engagement

Insert firm language regarding terms of engagement, availability, conflicts of interest and legal fees.

We appreciate your expression of confidence in LAW FIRM. If you have any questions or concerns during the course of our relationship, I encourage you to raise them with _____, who may be reached at _____. We look forward to working with you.

Very truly yours,

INSERT NAME OF LAW FIRM

By

_____

[Name of entity] *agrees to the terms of engagement stated above.*

[NAME OF ENTITY]

_____
[Printed Name of Contact]
Title: _____
Date: _____