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Case law in Israel – how to set up a trust to survive death

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Introduction

The transfer of assets to the next generation may pose many challenges, from the risk of inheritance disputes to the complexity of transferring a family business. A trust properly created under the Israeli Trust Law 1979 provides an efficient instrument to overcome such challenges and execute the transfer of assets in accordance with the settlor's desire to the greatest extent possible.

Under the Israeli Trust Law 1979, a private trust may be either by a contract with a trustee (an *inter-vivos* trust) or by an instrument of endowment known under the Trust Law as '*Hekdesh*'. A *Hekdesh* may be created in accordance with the procedures set forth in Section 17 of the Trust Law, out of which the following are the most common ones:

- a trust deed signed by the settlor before a notary (an *inter-vivos* trust); and
- a written will of the settlor, which includes the terms of the trust (a testamentary trust).

It therefore follows that there are two approaches to create a trust to survive the death of the settlor: to set up an *inter vivos* trust (a contract with the trustee or a trust deed signed before a notary as a *Hekdesh*); or to set up a testamentary trust.

The main obstacle such a trust would have to overcome in order to successfully survive the death of the settlor can be found in Section 8 of the Succession Law, which provides as follows:

Transactions with future inheritances

8. *(a) An agreement about a person's estate and a waiver of his estate, made while that person was alive, is void.*

   (b) A gift made by a person with the intention that it be vested in the donee only upon the donor's death is not valid, except if made by a will under the provisions of this Law.

The form of the trust

According to Section 8(a) of the Succession Law, a person may not make an undertaking with respect to his or her estate in an agreement. Would a trust dealing with the estate of the settlor be considered as such agreement?

In the case of John Doe (Family Appeal Motion 7033/15), the deceased left a few wills and a draft will. In the first wills, the deceased bequeathed most of his assets to his family members. Shortly prior to his passing, the deceased added partners to his personal bank account. In his last will and the draft will, the deceased asked the partners to pay for activities not listed in the will. The partners argued that the deceased had created a private trust known as *Hekdesh* under Section 17 of the Trust Law, or a trust under an oral contract, whose purpose is the memorialisation of the deceased and his wife. The Supreme Court held that no oral contract between the deceased and the partners had been entered into, and even if such existed, it would be null and void under Section 8(a) of the Succession Law. Moreover, the Court held that the creation of a trust such as in this case should have been done as a *Hekdesh* under Section 17 of the Trust Law, and in the specific circumstances of the case, such a *Hekdesh* had not been created.

It can therefore be inferred that in order to create a trust to survive the death of the settlor, it must be created as a *Hekdesh*, either as an *inter vivos* trust (a trust deed signed before a notary), or as a testamentary trust. A trust created by a contract with the trustee shall become void upon the death of the settlor, and the trust assets shall revert to the estate of the settlor.

The transfer of assets to the trust

The transfer of the assets from the settlor to the trustee is done by way of gift. In light of Section 8(b), a valid transfer of assets to the trustee during the settlor's lifetime must be made by way of a *completed* gift.

When the assets are transferred to the trustee of a testamentary trust under a probate order, it is obvious that the transfer is completed, as it cannot be revoked. When the assets are transferred to the trustee of an *inter-vivos* trust during the lifetime of the settlor, the Gift Law 1968 would apply and the gift would be considered as completed in the following two instances:

- An *immediate gift* in accordance with Section 2 of the Gift Law. In such a case, the "gift is completed by the donor transferring the ownership of the subject of the gift to the donee, while it is agreed between them that the subject is disposed of by way of gift". Accordingly, the transfer of assets to the trustee is completed when the ownership of the assets is completely vested in the trustee.

A valid undertaking to grant a gift that the donor intended to fulfil during his or her lifetime, even if in practice the donor did not complete the granting of the gift in full, is a valid gift.

- An *irrevocable undertaking to grant a gift* in accordance with Section 5 of the Gift Law. According to Section 5, the undertaking must be in writing, yet the donor may still retract from it in any of the following instances:
  - when the donor has not waived his right to retract, and the donee has not altered his situation in reliance thereon;
  - when the donee has behaved in a disgraceful manner towards the donor or his family members; and
  - when a considerable deterioration occurred in the donor's economic situation.

When would an undertaking to grant a gift be regarded as a completed gift, and when would such an undertaking be declared invalid under Section 8(b) of the Succession Law?

In the case of *Lola Baer* (Civil Appeal 3727/99), the deceased, Lola Baer, wrote a letter to Ben-Gurion University, where she made an undertaking to pay the university an amount of US$50,000 annually, and she further stated that should she pass away, the administrator of her estate is to pay the university the balance up to the amount of US$1 million. The deceased bequeathed her estate in her will to her family members. Eventually, the deceased indeed passed away before paying the university the entire amount of US$1 million. The university petitioned the court and asked to prevent the distribution of the estate until the payment was completed per the deceased's letter.

The Supreme Court regarded the deceased's undertaking as one continuous undertaking to grant one gift in the amount of US$50,000, therefore it was a valid undertaking as it complied with the requirement of Section 5 of the Gift Law.

The Supreme Court further held that since the deceased did not complete the granting of the gift during her lifetime, the undertaking binds her estate and heirs. Although Section 5 allows the donor to retract from the granting of the gift, this right does not transfer to the estate and heirs, therefore the undertaking became irrevocable.

To conclude, a valid undertaking to grant a gift that the donor intended to fulfil during his or her lifetime, even if in practice the donor did not complete the granting of the gift in full, is a valid gift. Therefore, it follows that the transfer of assets to the trust should preferably be made as an immediate gift. If, however, this cannot be done under the circumstances, the undertaking to transfer the assets to the trust must be in writing, and include an explicit waiver of the settlor from his right to retract the granting of the assets to the trustee. Furthermore, the settlor must be solvent at the time of transferring the assets to the trustee.

A testamentary trust

As mentioned above, a *Hekdesh* created as testamentary trust is one of the possibilities to create a trust to survive the death of the settlor. In that case, the transfer of the assets to the trustee is done under a probate order issued with respect to the will containing the terms of the trust. First, such a trust must comply with the formalities required for the execution of a valid will. Second, the fact that the creation of a testamentary trust is subject to probate proceedings increases the risk that the trust would not be created as the settlor originally intended due to various reasons. For example, the trust, and the will that contains it, may be challenged by the heirs; it is subject to the revision of the Administrator General, who may intervene in the proceeding if deemed appropriate; and when the deceased or any of the assets is situated outside of Israel, private international law issues may arise.

The case of *Dr DR* (Estate File (Tel Aviv) 9947/01) provides a good example for a testamentary trust which was declared invalid due to a fundamental flaw in the will. In this case, the deceased was diagnosed with a cancer disease and was hospitalised. Within six months of her hospitalisation, she passed away at the age of 43. The deceased left two minor children. The deceased had divorced from the father of her children, and at the time of her passing she had a spouse. The deceased left a will executed before witnesses that included assets in an accumulative value of over US$6.5 million. The will was executed during the hospitalisation of the deceased, approximately six weeks prior to her passing. The main beneficiaries under her will are her two minor children in equal shares. The will was drafted by Advocate Doron Refuah.

The deceased included trust provisions in her will, providing as follows: if at the time of her passing, her children had not reached the ages of 29 and 30, the

share of each child shall be held in trust in accordance with the provisions of the will. Furthermore, the deceased appointed Advocate Doron Refuah as trustee, and directed that the trustee would have the authority to act freely, without supervision, and without any obligation to justify his decisions, which would be final. As trustee, Advocate Refuah would be entitled to an annual fee of 3% of the value of the assets in addition to VAT.

The deceased granted additional powers to Advocate Refuah in her will: Advocate Refuah was empowered to interpret the will, with his interpretation to be final; Advocate Refuah was appointed as administrator of the estate; Advocate Refuah was appointed as second in line to be appointed as the children's caregiver after their father, whereas the will granted further rights to the person who would bear this responsibility.

While the deceased was hospitalised, she signed a general power of attorney empowering Advocate Refuah, through which he executed various monetary actions during the deceased's lifetime (such as depositing rent).

In the three months prior to her death, Advocate Refuah opened a bank account, and by using the general power of attorney, he 'assembled' all of the deceased's funds to this account. After her passing, Advocate Refuah refused to transfer the contents of this account to the account of the appointed administrator of the estate until a court order was issued.

Shortly after the deceased's passing, Advocate Refuah, on his own initiative, took possession of the deceased's assets, took out funds and jewellery from her safe, and transferred them to another safe under his name for the benefit of the deceased's daughter; took all of the deceased's clothes and donated them to charity; took her car and held it in his possession. He also transferred NIS 300,000 from the deceased's bank account to his own private bank account and took out US$60,000 from a safe in the name of the deceased and her mother through the deceased's spouse and distributed US$20,000 out of this amount to the spouse on account of his share under the deceased's will.

The deceased's spouse, who was entitled to US$100,000 under the will, applied for the probation of the will. The deceased's children objected (through their father) on the grounds of Section 35 of the Succession Law, which provides as follows:

> *A testamentary provision – other than in an oral will – in favor of a person who prepared the will or witnessed it or otherwise participated in its preparation and a testamentary provision in favor of the spouse of any of these – is void.*

The children argued that Advocate Refuah took a fundamental part in the planning and consolidation of the will and its provisions, in such a manner that if probated as is, Advocate Refuah would be entitled to the benefit of the majority of the estate – up to 60% of it. On the other hand, Advocate Refuah argued that the deceased transferred all of her assets to him during her lifetime, and the trust created in the will was nothing but a continuation of the trust the deceased had created during her lifetime.

The Family Court accepted the opposition to the will and determined that Advocate Refuah's conduct at the time close to the deceased's passing and the nature of the will, including the manner and circumstances of its drafting, indicate that Advocate Refuah was the one to conjure the provisions of the will in a way to ensure his share in the estate covertly, which amounted to 60% of the vast estate of the deceased. This is a wrongful involvement deriving from ulterior motives, which do not coincide with the true wishes of the deceased. Therefore, the conditions of Section 35 of the Succession Law have been fulfilled, and the will is invalid. The Family Court further stated that the provision of Section 35 cannot be overcome by the Trust Law and the setting up of a trust. Doing so would be an infringement of the free will of the deceased and the requirement that the will be a personal act, in other words – an infringement of the core principles upon which the inheritance law is based.

Conclusion – how to set up a trust to survive death?

Assets may be transferred to the next generation by the instrument of a trust. There are two possible means of doing so:

- Creation of an *inter-vivos* trust (*Hekdesh*) by the execution of a trust deed before a notary. The settlor should then transfer the ownership in the assets to the trustee and by doing so be completely disconnected from them. If, however, this can't be done, then the settlor must make an irrevocable undertaking to grant the assets to the trustee and be solvent at the time they are transferred. Even so, there is always a risk that the undertaking will be contested.

Assets may be transferred to the next generation by the instrument of a trust.

- Creation of a testamentary trust (*Hekdesh*) by the execution of a valid will. The will must comply with all the requirements of making a valid will. However, there is always a risk that the terms of the trust eventually probated would be different as a result of the intervention by the Administrator General or the court.

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